

State pension (Lecture P1447 – 13.38 minutes)

Introduction

The basic state pension increases every year by whichever is the highest of the following:

1. Earnings: average percentage growth in wages in Great Britain;
2. Prices: percentage growth in UK prices as measured by the Consumer Prices Index;
3. 2.5%

This is controversial but no Government has yet decided to overturn these measures, other than a temporary removal of the first option in 2022/23 when the data was skewed by the post-Covid position.

The increase for 2024/25 has been 8.5% so that the full new State pension for this year is £221.20 per week or £11,502 per annum. This is still low compared to other countries.

For those retiring now, the earlier you can get to state pension age is 66 with this in the process of increasing to 67 (to be reached by 2028). It is likely to increase further in future due to the cost of pensions for the Government.

Qualifying years

You will need at least 10 qualifying years on your National Insurance record to get any state pension with a qualifying year being one where you were:

- working and paid NICs at a sufficient rate;
- getting NI credits (e.g. because you were unemployed, ill or a parent/ carer);
- paying voluntary NICs (including in some circumstances where you were abroad).

The rules changed in 2016 and the actual number of years you have can be complicated but the easier way to find out is to get a pension forecast from HMRC. You need 35 qualifying years to get the full state pension and you will get a proportion if you have between 10 and 35 qualifying years.

Voluntary contributions

In some cases, individuals may realise that they have insufficient years to get the maximum state pension and ask whether or not they can make voluntary contributions.

Individuals can pay Class 2 or Class 3 contributions if they meet the relevant conditions. Whether this is worthwhile would need to be considered on a case by case basis. Entitlement to pay voluntary Class 2 NICs is retained for those who meet the conditions even though Class 2 NICs have been abolished for the general self-employed population. Anyone earning more than the small profits threshold (currently £6,725) will be treated as if they have a full year of contributions for pension purposes going forward.

Those who can pay Class 2 voluntary contributions are:

- A UK self-employed individual earning less than the small profits threshold
- An individual who is in employment or self-employment overseas provided that they meet the following conditions
 1. Have been resident in the UK for 3 continuous years at any time or
 2. Paid full NICs in any 3 years and (in either case), and
 3. Was in employment or self-employment immediately before going overseas.

If you are not entitled to pay Class 2 voluntary NICs, then you can potentially pay the (higher rate) Class 3 NICs on a voluntary basis. You cannot pay if you will not benefit from the contributions. You can always pay Class 3 if you are resident in the UK and may be able to pay if you are not resident as long as you meet the first two conditions above in terms of the contributions.

There are time limits for payment of contributions.

The standard time limits are 42 days after the end of the year in respect of which the contribution was paid or before the end of the sixth year following the year in respect of which it was paid.

A longer time limit can be given if the failure to pay contributions is down to ignorance or error or if the contributor falls within the current extended voluntary Class 2 time limits. Those are as follows:

- Voluntary contributions for the tax years 2006/07 to 2015/16 can be made up to 5 April 2025 by individuals who reached state retirement age on or after 6 April 2016;
- Voluntary contributions can be made for 2016/17 and 2017/18 up to 5 April 2025 by any individual.

Is it worth it?

Class 3 voluntary contributions (which is the most expensive way to top-up but is often the way that has to be used) currently cost £17.45 per week which is £907.40 for a whole year. Buying an extra year will give you £6.32 per week (being £221.20 divided by 35) which is a total of £328.64 per year. It would take under 3 years to recoup that additional investment. An extra year of contributions if you can pay at Class 2 rate would be £179.40 for a year which is less than the extra state pension you would obtain which would seem to be a less difficult decision.

Retiring overseas

You can claim the state pension even if you are going to retire overseas. However, the state pension will only increase each year if you live in the EEA, Gibraltar, Switzerland and some countries which the UK has a social security agreement with (being Barbados, Bermuda, Bosnia-Herzegovina, Guernsey, IOM, Israel, Jamaica, Jersey, Kosovo, Mauritius, Montenegro, North Macedonia, Philippines, Serbia, Turkey and USA).

Deferring the state pension

If you reach the state pension age, you can get an increase in weekly pension rates if you defer the date at which you receive the state pension. You have to defer for at least 9 weeks. It increases by around 1% for every nine weeks that you defer, so around 5.8% for every 52 weeks.

If you are entitled to the full state pension of £221.20 per week, you would get an extra £12.83 per week or £667 a year if you deferred for 52 weeks (assuming no increase in the state pension which is not going to happen). However, the pension foregone for a full year was £11,502 (assuming he is retiring now at the age of 66), and he would have to live for a further 17 years to make this worthwhile.

Contributed by Ros Martin