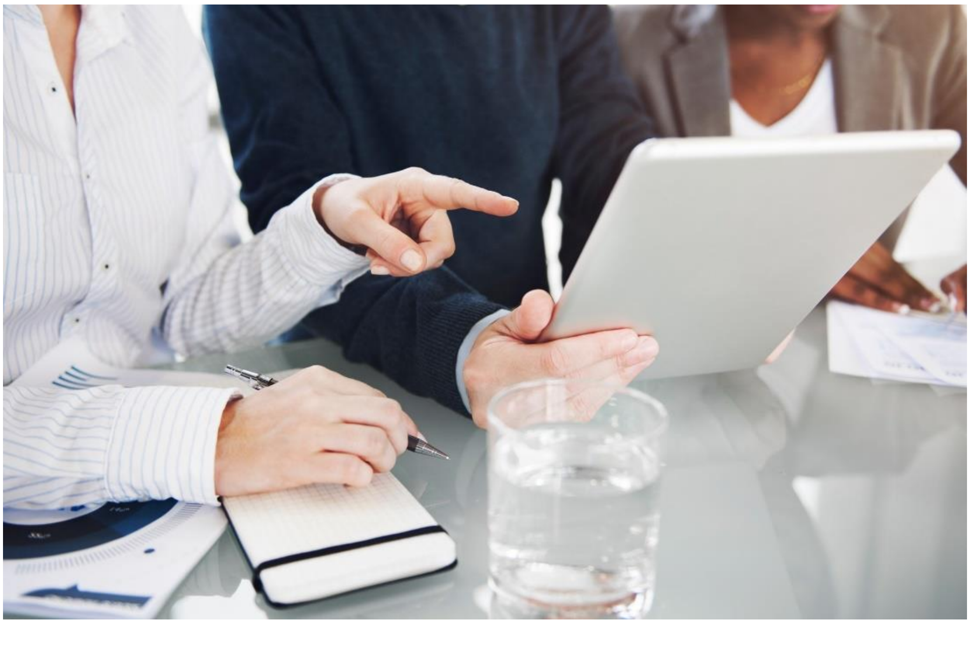
LCP on point

Under-paid state pensions – what have we learned and what should happen next?

August 2020



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Summary

On 26th May 2020 LCP published a paper entitled: "Are thousands of older women being short-changed on their state pension?". In it, we presented estimates, based on Freedom of Information replies and other statistical sources, which suggested that many thousands of older women covered by the 'old' (pre April 2016) state pension system appeared to be getting a lower state pension than they were entitled to receive. On the same day we also launched an interactive 'calculator' which allowed married women to check if their state pension was correct. This can be found at www.lcp.uk.com/underpaid

The response to that paper has been enormous. Key points include:

- More than 160,000 people have visited the website, with around 120,000 of these entering data to check their state pension
- We have been made aware of case-after-case of married women who have discovered that their state pension has been underpaid – in some cases for more than a decade; combining cases notified to LCP with those reported by the 'This is Money' website, we are aware of repayments of around two thirds of a million pounds so far, with the total rising every day
- The topic has been discussed on BBC Moneybox, ITV's 'Money Saving Expert' programme and in most national newspapers
- The issue has been raised in Parliament, both in the House of Commons through oral questions to ministers and in a series of written questions tabled by shadow pensions minister Jack Dromey MP

In the two months since we published our paper, we have heard directly from over 1,000 people with questions and comments. Their experiences plus further investigations have helped to clarify a number of aspects of this issue.

In this paper we summarise what we have learned over the last two months, including areas where there is now greater clarity about the rules. We note in passing that we have also come across multiple cases where individuals are, to this day, still being given misleading or simply incorrect information.

The DWP has said that it wants individuals to come forward if they think they are being underpaid and we would continue to encourage people to do so. But it has also said publicly that it is 'checking its records' to see who is being underpaid. **A central message of this paper, not least based on the many people who have been in touch with us, is that any such search of records needs to be broad or risks leaving this issue still unresolved. Unless and until that point, we would continue to encourage a broad range of women to check their state pension and to query it with DWP if they are not convinced that it is correct.**

01 The story so far

A Freedom of Information request tabled by LCP partner Steve Webb in February 2020 found that 621,000 women who reached pension age before 6th April 2016 were receiving a state pension below the standard rate payable to a married woman claiming on the basis of her husband's record of NI contributions[1]. We then adjusted this number to exclude:

- *those living in countries where state pensions are 'frozen'*
- *unmarried women*
- *those with husbands under pension age*
- *those with husbands with incomplete NI records*

but still concluded that potentially tens of thousands of women could be receiving a higher state pension than the amount they were currently receiving.

A crucial rule change in 2008

The paper pointed out that a crucial rule change in 2008 affects the amount a married woman can expect to receive today if she believes she is being underpaid. Prior to 17th March 2008, a married woman who wanted to receive a 60% pension based on her husband's contributions had to claim it when he turned 65. From 17th March 2008 onwards, any such uplift should be awarded automatically without the need for a further claim.

For those who make a claim now, the position is:

- **where the husband turned 65 from 17th March 2008 onwards**: if the wife's pension was not automatically increased at the time, she can ask for this to be corrected and any increase will be backdated to her husband's 65th birthday (or her pension age if later); in some cases this involves backdated payments covering a period of more than a decade
- **where the husband turned 65 before 17th March 2008**: any claim by a married woman is treated as a new claim; by law this can only be backdated for 12 months

[1] Further FOI requests on this subject have been tabled but DWP is now operating a blanket refusal to answer on this issue on the basis that it plans to publish its own statistics in due course.

As well as married women missing out on a 60% pension based on their husband's contributions, the paper also highlighted three other groups of concern:

- **widows**, who can potentially receive a 100% basic state pension based on their late husband's contributions, plus inherited additional state pension, and who may be missing out;
- **divorced women**, who can substitute the NI record of an ex-husband for the period up to their divorce. A particular issue seems to surround women who divorce post-retirement;
- **those aged 80 or over** who can claim a *non-contributory* state pension where entitlement depends only on a simple residence test;

A combination of written parliamentary questions, responses to appeals and case studies has shed light on all of these areas. In the next section we set out what we have learned so far.

02 What have we learned – particular groups

The issue of underpaid state pensions affects different groups of women in different ways. In this section we provide an update of the position of each of the key groups.

a) Women whose husband turned 65 on or after 17th March 2008

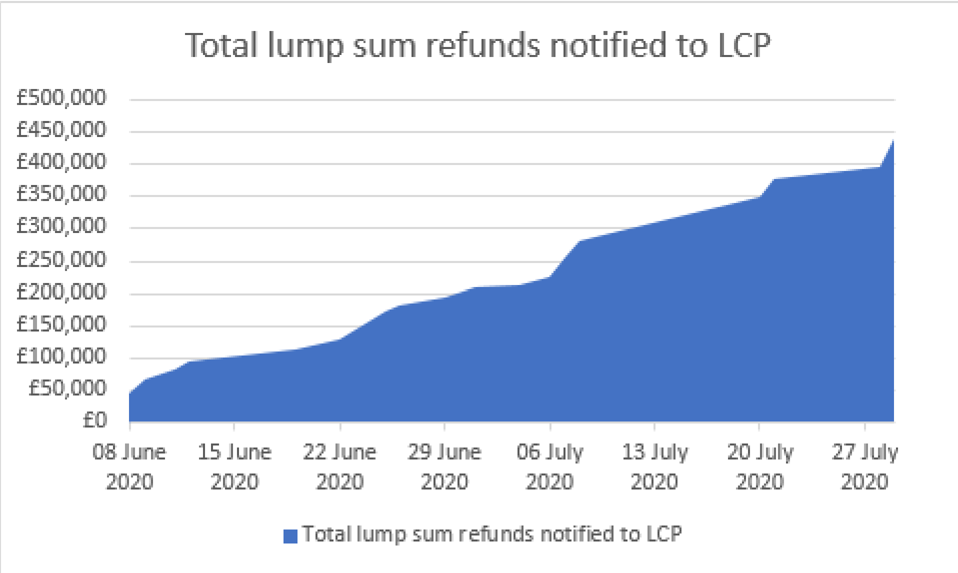
For married women, by far the largest repayments have been to those whose husband turned 65 on or after 17th March 2008. This is because their pension should have been increased automatically at the time, and they are therefore now entitled to full backdating[2].

The following case study gives an example:

Case Study 1 – large lump sum from backdating

Mrs A is currently receiving a basic state pension of just £24 per week. The standard 60% rate for a married woman with a husband on a full basic pension is £80.45 per week. Mrs A's husband turned 65 in late 2008 and her pension should have been increased to the 60% rate at the time but this did not happen. She contacted DWP and has received a lump sum repayment of over £33,000, covering roughly 12 years of underpayment.

Most of the cases reported to LCP have been of 'post 2008' cases where a pension increase should have happened automatically. The Chart below shows how the total amounts repaid have steadily increased since the paper was published:



[2] We consider the issue of interest or 'special payments' on these backdated amounts later.

At time of writing, the total amount in lump sums repaid in cases notified to LCP stands at £439,000 in respect of forty six claims. The average lump sum is therefore just under £10,000.

In addition to cases notified directly to LCP, we have continued to work with the ‘This is Money’ website and the Daily Mail who have continued to investigate this issue and hear from more readers who have secured repayments. The total figure from this source stands at around £340,000, giving a combined figure of more than three quarters of a million pounds in repayments to date.

On the assumption that many people who claim a refund do not notify LCP or ‘This is Money’, we are confident that DWP will already have paid out several million pounds in refunds even before it undertakes its own check of records.

b) women whose husband turned 65 before 17th March 2008

With one major exception, where a woman’s husband turned 65 before 17th March 2008, she had to make a separate claim for a 60% pension. If she did not do so at the time, she can claim now, but only receives 12 months of backdating, as in the following case study:

Case Study 2 – modest lump sum because of 12 month time limit on backdating

Mrs B was receiving around £69 per week rather than the full £80.45 she could have received if she had claimed on her husband’s record. Mr B turned 65 in 2007 and at the time it was necessary to make a claim for an uplift. Mrs B’s claim in 2020 has been successful and her pension has been uplifted by over £11 per week. She has received a lump sum payment of just over £700 for the last 12 months, but has missed out on an improved pension for the whole period from 2007 to 2019.

The one exception to the pre 2008 rule is cases where there is a larger age gap between husband and wife so that when the wife reached state pension age of sixty her husband was *already* drawing a state pension. In these cases, the wife’s claim for her own state pension is treated as a claim for a pension on her husband’s record as well, and the 60% rate can be put into payment immediately. In a small number of cases this does not seem to have happened correctly and some women have therefore been able to get backdated payments stretching back before 2008.

A key issue is the extent to which married women understood the need for the ‘second claim’ that was usually needed when her husband turned 65. The government’s position is that the law at the time was clear and that women needed to claim their 60% pension before it could be put into payment. In general, the onus is on the individual to claim what they are entitled to, and if the individual fails to claim (for whatever reason) it is the individual who loses out.

However, there are several reasons why it could be argued that the DWP should have done more to alert married women of their entitlement:

a) 2008 rule change a recognition of problems

The fact that the rules were changed in March 2008 to make uplifts automatic for married women is a recognition that the system was not working properly until that point. Yet when the rules were changed nothing was done to track down the women who came under the old system and still needed to make a claim. Such women who claim now can get 12 months of backdating but have missed out on 12 years or more of enhanced pension. DWP should arguably have done more at the point of the rule change to alert these ‘pre 2008’ women.

b) Complexity of the system

Whilst it is a general presumption that citizens need to claim their entitlements and be generally aware of how things work, there must come a point where the complexity of the system is such that the onus is on government departments to do more to help people make claims. In the case of the married woman's claim to a pension, she is moving from a Category A pension in her own right to a category ABL pension based on her husband's contributions, or perhaps from no basic pension in her own right to a Category BL pension based on her husband's contributions. And to become entitled can require a woman who has already claimed her state pension and is already receiving regular payments to make a second claim. All of this may be baffling to some and is far from intuitive. Many people would assume that once they are claiming a pension they will be paid the 'correct' amount without the need for further action on their part.

c) Old-fashioned approach to alerting women

Under the old (pre 2008) rules, a woman would usually face a two-stage process when claiming her pension. At her own pension age (then age 60), she would receive a claim pack ahead of pension age and would be invited to make a claim. This would be for a pension based on her own contributions. This would be accompanied by a booklet which explained more about how pensions worked including the fact that some married people can make a claim based on the record of a spouse. But assuming her husband was not yet 65, this information would not be directly relevant at this point.

Subsequently, and possibly several years after reaching her own pension age, her husband would reach 65. The wife would then need to make a fresh claim for a pension based on her husband's record.

In response to an appeal on this point, DWP have said in writing that when the husband turned 65 he would be sent an information leaflet (with a reminder that married people may be able to claim on the basis of a spouse's contributions) plus *two* claim forms – one for him and one for his wife.

Today, this looks pretty astonishing. DWP are recognising that the wife may have a claim and are going as far as to 'nudge' the claim by sending out two claim forms. But rather than send a claim form to the wife – who has to actually make the claim – they relied on the husband to pass it on. In cases where a husband failed to pass the form on (or understand the system), it seems hard for the wife to lose out as a result.

Potential challenges by 'pre 2008' women

Whilst the legal position of these 'pre 2008' women is clear in terms of the need for a claim before a pension uplift can be paid, it could be argued that DWP was guilty of 'maladministration' in the way that it went about making sure that women were aware of their ability to claim an uplift. DWP clearly hold data that would enable them to identify all the women entitled to an uplift, but still waited for women to make a claim. They also sent claim forms not to the person who needed to put in the claim but to the potential claimant's husband.

The Parliamentary Ombudsman is able to investigate cases where maladministration by a government department has led to financial or other loss to a citizen. We understand that several 'pre 2008' women will be complaining that DWP was guilty of maladministration by failing to ensure effectively that they were aware of their entitlement to claim an uplift, with the result that they have been living on a lower pension than necessary for more than a decade. It will be up to the Ombudsman to make a decision as to whether this is a case of maladministration and, if so, what compensation might be in order.

c) Widows

Some of the largest lump sum refunds we have seen in the last two months have been in respect of widows. There are two reasons for this:

- Whereas a married woman can claim a '60%' pension based on her husband's contributions, at a rate of £80.45 in 2020/21, a widow can claim a '100%' pension based on her late husband's contributions, at a rate of up to £134.25 in 2020/21; if a married woman's pension was not recalculated when her husband died, the shortfall can be very considerable;

- On top of the basic state pension, a widow can inherit between 50% and 100% of her late husband's additional state pension (also known as SERPS or state second pension), depending on his date of birth; if a married woman's basic pension was not adjusted when her husband died, it is highly likely that no account was taken of his additional state pension either.

Although the number of cases where widows have not been uplifted appears to be small relative to the wider group of married women, the amounts underpaid are truly shocking and in some cases have exceeded £100,000. The following is a case study of a widow who received a lump sum of over £30,000.

Case study 3 – widow underpaid for several years

Mrs C was widowed in 2013 but her state pension was not adjusted at the time. Had correct procedures been followed, she would have received a full basic state pension based on her late husband's contributions, and she would have inherited around £50 per week of earnings-related additional pension. When this case was drawn to the attention of DWP they eventually doubled Mrs C's state pension and paid arrears for the last seven years of over £30,000.

Another group of widows who we are keen should get what they are owed are those who may be getting the correct pension now, but who, <u>when they were still married</u>, were not on the correct rate Given that we think that thousands of married women are currently being underpaid, it seems inconceivable that there are not thousands more who are now widows but who were being underpaid when their husband was still alive. Any search of records by DWP must include this group.

d) People aged 80 or over

A group which has received relatively little attention is those aged 80 or over. A little-known corner of the benefit system is the 'Category D' pension which is payable at the rate of £80.45 per week on a non-contributory basis. Unlike other elements of the state pension system, a Category D pension can be paid regardless of the NI record of the claimant or a spouse and depends only on satisfying a simple residence test at the point of claiming. Our previous report identified thousands of women over 80 who were not receiving the full rate, and we have since heard from several who are apparently missing out and have encouraged them to make a claim.

One issue which was unclear was whether it is necessary to make a claim at age 80 (and therefore it was up to the woman to make a claim when she turned 80) or whether any uplift at age 80 was automatic. The following written Parliamentary answer sheds light on this question:

Asked by Jack Dromey (Birmingham, Erdington) Asked on: 29 June 2020 **Department for Work and Pensions** **State Retirement Pensions** 66004 To ask the Secretary of State for Work and Pensions, whether entitlement to a Category D pension requires a person to make a claim. **A** Answered by: Guy Opperman on 07 July 2020 *A claim for a Category D State Pension is required (under section 1 of the Social Security Administration Act 1992), unless the individual is resident in Great Britain at age 80 and is already getting another category of State Pension (Section 1 and Social Security (Claims and Payments) Regulations 1987, Regulation 3(1)(b)).*

This written answer indicates that provided that the person concerned was already receiving a state pension of some sort and met the residency rules, then no further claim would be required. On this basis, it is especially puzzling that so many UK based over 80s are not receiving the full category D rate. Again, if DWP is checking its records for underpaid state pension, it should be checking for those who may be missing out on Category D payments.

e) Divorced women, including post retirement divorcees

The position of divorced women is complex and diverse and it is therefore difficult to say to what extent the issues affecting married women are also affecting divorced women. In brief, a woman who is married once, divorces and reaches state pension age without divorcing can substitute the NI record of her ex-husband for her own up to the date of their divorce. What this means in practice is that a woman who divorces later in her working life can potentially derive a basic pension of up to 100% of the full rate, though a woman who divorces at a younger age may get less benefit from these rules.

Our previous report indicated a worrying number of divorced women not even receiving the £80.45 rate, let alone the £134.25 full basic pension which they might receive if they were married for a long time.

The application form at pension age for a state pension does ask the applicant about previous marriages and so in principle, most divorced women should be picked up at that point. However, what is not clear is how the system is working for the growing number who divorce post-retirement[3]. In principle, they can still substitute the contribution record of their ex-husband and potentially benefit from a significantly enhanced basic state pension. But if the DWP is not notified of the divorce, it is unlikely that such a recalculation would happen automatically.

Based on the cases brought to our attention, we believe DWP should do more to research the position of post-retirement divorcees to see if there is a significant issue of underpaid state pensions.

[3] According to the Office for National Statistics, the number of women aged 65 or over who divorced during the course of a year rose by 38% between 2005 and 2015. See: https://www.ons.gov.uk/peoplepopulationandcommunity/birthsdeathsandmarriages/marriagecohabitationandcivilpartnerships/articles/marriageanddivorceontheriseat65andover/2017-07-18

03 What have we learned – the rules

The diversity of individual circumstances inevitably throws up a range of questions as to how the rules on women's state pensions apply in particular circumstances. It can often be hard to find a definitive answer to some of these questions, but recent Parliamentary answers and individual case studies have helped to provide some clarity. We cover some of these issues below.

a) If I get a lump sum repayment of state pension, do I have to pay tax?

Regular payments of state pension are taxable and lump sum backpayments are also taxable. However, a concern has arisen as to how a large lump sum would be taxed. In some cases back payments have exceeded £50,000 and therefore could even take the recipient into higher tax bands if the lump sum was taxed in a single tax year. This would be especially unfair given that many of these women are on relatively low incomes and might have paid no tax at all if the correct pension had been paid at the correct time.

The following written answer provides helpful clarity:

Q
Asked by Jack Dromey (Birmingham, Erdington)

Asked on: 26 June 2020
Treasury
State Retirement Pensions: Females
65108
To ask the Chancellor of the Exchequer, what the tax liability is for women who receive back payments of underpaid state pension in a single financial year; and if he will make a statement.
A
Answered by: John Glen
Answered on: 01 July 2020
Income tax is calculated on arrears of state pension for the tax year in which the pensioner was entitled to receive it, and not in the year in which a lump sum is paid.
Where arrears of state pension are paid, income tax will only be due on any income that exceeds the personal allowance for the respective tax year.
In addition, HM Revenue and Customs can only collect income tax for the current tax year and the four preceding tax years. Any arrears of state pension relating to earlier years will not be subject to income tax.

The good news for recipients of lump sums is that they will not be treated as if the lump sum had all fallen within the current tax year. For older tax years (beyond four years before the current year), no additional tax will be paid, and for other tax years it will only be the share of the lump sum that would have fallen in the year in question which is potentially taxable. As noted above, for many married women this could mean that no tax at all is payable despite receipt of a large lump sum.

b) If I get a lump sum backpayment because of official error, will I get interest?

In the case of 'post 2008' women, their state pension should have been uplifted automatically when their husband turned 65. The fact that this did not happen is down to error on the part of the DWP, and arrears are therefore backdated all the way to the husband's 65th birthday.

Some of those who have received lump sums have also received interest payments, sometimes running to several hundred pounds, but others have received nothing. The following written answer sets out the government's position:

> **Q** Asked by **Jack Dromey** (Birmingham, Erdington)
>
> Asked on: 29 June 2020
> **Department for Work and Pensions**
> **State Retirement Pensions**
> 66003
> To ask the Secretary of State for Work and Pensions, what criteria her Department uses to determine the circumstances in which interest is added to back payments of a state pension.
> **A**
> Answered by: **Guy Opperman**
> Answered on: 07 July 2020
>
> The DWP has a discretionary special payment scheme and the current criteria has been in place since 2012. If a benefit payment has been delayed DWP can consider a payment to recognise any erosion in the value of the money. Special payments for 'interest' are calculated using HMRC's repayment interest rate.

DWP are adamant that interest is payable on a discretionary basis, but apart from 'de minimis' rules to avoid payment of trivial sums, it is hard to see why all post 2008 cases should not receive interest automatically and without having to request it. Our experience has been that too many people are awarded large lump sum repayments with no offer of interest and then have to make a further request for an interest payment to be made.

We believe that DWP should ensure that all such cases receive interest automatically.

c) If my husband didn't take his pension at 65, do I have to wait until he draws his pension before I can claim my 60% rate?

Although it is possible to claim a state pension when you reach state pension age, it is not mandatory to do so. Many people, especially those who plan to continue working past pension age, choose to defer taking their state pension. This can reduce their overall tax bill and brings entitlement to a higher rate of state pension when they do finally draw their pension.

The question then arises as to whether a married woman who is dependent on her husband's contributions can make a claim for a 60% pension as soon as he reaches pension age or whether she has to wait until he starts drawing a pension.

Different people appear to have been given different advice by DWP, but we have established that a woman's entitlement to a derived pension starts at her husband's pension age, **regardless of whether or not he is taking his own pension**. A written Parliamentary answer confirms that this provision has applied since 6th April 2010.

This does raise an interesting issue about what triggers an uplift in a married woman's pension when her husband reaches pension age if he does not actually make a claim for a state pension.

For post 2008 cases, any such uplift should be automatic, but it does seem clear that in some cases this has not happened.

We believe that DWP should ensure that a married woman whose husband defers taking his state pension does not lose out as a result.

d) If my late wife / late mother was underpaid, can I still put things right?

We have been contacted by widowers and by the adult sons and daughters of women who have now died to ask what happens if it turns out that a woman who died was not getting the right amount of state pension.

Some clarity on this point is provided by another written Parliamentary answer.

Asked by Jack Dromey (Birmingham, Erdington)

Asked on: 26 June 2020

Department for Work and Pensions

State Retirement Pensions: Females

65109

To ask the Secretary of State for Work and Pensions, whether the underpayments of state pension to women who have not received their full state pension will be passed on to the (a) surviving spouse and (b) beneficiaries of a will where a female pensioner is deceased.

A

Answered by: Guy Opperman

Answered on: 02 July 2020

Where arrears of Cat BL pension are payable, they will be distributed to those who have a legitimate claim to the monies. This could include the surviving spouse and the beneficiaries of a will.

From this answer is would seem that a widower and/or others with an interest in the estate of a married woman should be able to receive any arrears of state pension that are due. It is important to note that this is likely to be primarily in the 'post 2008' cases where an uplift should have been applied but was not.

We recommend that any search by DWP of its records should include cases where a woman who is now deceased was previously underpaid the state pension to which she was entitled.

04 The government's response – and what needs to happen next

In addition to the various written Parliamentary Questions which we have quoted in this report, this issue has been discussed briefly in Parliament on 29th June, and the DWP Press Office have also issued various statements setting out their position.

The Pensions Minister, Guy Opperman MP, set out the government's position to the House of Commons as follows:

> *"The Department for Work and Pensions is looking into the matter, and we invite any individual who feels that they are affected to claim a state pension increase by contacting the Pension Service helpline"*
>
> *(Source: Hansard, 29th June 2020)*

In response to inquiries, the DWP press office says:

> *"We are aware of a number of cases where individuals have been underpaid state pension. We corrected our records and reimbursed those affected as soon as errors were identified. We are checking for further cases, and if any are found awards will also be reviewed and any arrears paid".*
>
> *(Source: Statement, DWP Press Office)*

a) The DWP's check of its records

A central issue therefore is what DWP means by 'checking for further cases', and the scope of that check. DWP makes a clear distinction in written answers and elsewhere between 'pre 2008' and 'post 2008' cases.

For post-2008 cases where any uplift should have been automatic, the approach is generally comprehensive. The correct rate of pension is put into payment, backdating can go back for many years to when the husband reached pension age, and interest can be paid on request.

By contrast, for pre-2008 cases, the DWP's view is simply that claims will be dealt with when received and that until a claim is received there is no 'underpayment'.

On this basis, we assume that any DWP check of records is restricted exclusively to married women who did not automatically receive a post 2008 uplift.

As we have indicated throughout this report, we believe that any such check of records would be far too narrow.

In summary, we believe that DWP should also use its records to:

- Check for 'pre 2008' cases of women who could be getting a higher pension and notify them of their entitlement;
- Check that all widows are now receiving the correct pension based on the contribution record of their late husband;
- Check that pensioners over 80 are receiving the Category D state pension where applicable;
- Check that those who are now widows were receiving the correct rate of state pension when their husband was still alive;
- Check that women who have now died were receiving the correct rate of pension and pay any arrears to their heirs

Unless and until such a check is undertaken by DWP of its own records, we would continue to urge individuals who are in any doubt as to their entitlement to contact the Pension Service directly to ask for it to be reviewed.

b) Other issues

To fully resolve this issue and to ensure that people are treated fairly, we also believe that the DWP should:

- Investigate the position of divorced women and in particular post-retirement divorcees, to see if the system is correctly calculating their pensions
- Ensure that when people are paid lump sums they are given information about the tax treatment of those lump sums
- Ensure that interest is paid automatically on all arrears cases, without the need for a separate application.

We can also confirm that we will share our findings with the Parliamentary Ombudsman and hope that women affected by the 'pre 2008' cut-off will raise their concerns with him about potential maladministration by the DWP.

Contact us

If you would like more information please contact your usual LCP adviser or one of our specialists below.

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