

Topping up state pensions – is this a good time to buy ?

A combination of the Pensions Act 2007 and the Pre Budget report last year means that anyone with an incomplete National Insurance Contribution (NIC) record could potentially benefit by buying extra 'years' before 6 April 2009 to boost their basic state pension.

As ever with state pensions, the actual terms and how they might apply on an individual basis are complicated. However we have attempted to summarise the headline issues below.

Qualifying years

NICs entitle an individual to 'qualifying years' in the state pension scheme. At the moment, to achieve a full state pension of £4,953 a year (2009/10), an individual needs to have credit for about 90% of the normal 'working life' (working life deemed to be 40-44 years).

Anyone reaching State Pension Age (SPA) after 5 April 2010 benefits from a reduction to a minimum of 30 'qualifying years' for entitlement to a full basic state pension.

Buying Class 3 NICs

There are 2 main issues to be aware of:

1. Normally, back payments can be back dated for up to 6 earlier tax years, i.e. the 5 April 2009 is the last day for paying 2002/03 Class 3 contributions. Normally, Class 3 contributions are based on current year costs (£421.20), not the actual year being purchased. But see point 2 below.
2. Exceptionally, if earlier contributions have been missed for the years 1996/97-2001/02 Class 3 contributions can be made at historic rates due to an earlier error by the then Inland Revenue. These rates range from £309.40 (1996/97) to £351 (2001/02).

Importantly, two changes to Class 3 contributions take effect from 6 April 2009:

1. The Class 3 rate will rise by almost 50% from £8.10 a week to £12.05 a week
2. The option to pay for 1996/97-2001/02 missed years will lapse.

So, who should act on this?

Those most likely to benefit from purchasing additional years before 6 April 2009 are:

- Women who maybe ceased work when they had children
- Anyone who has had a patchy work history

What does it cost and what are the benefits?

For those falling short it is possible to purchase Class 3 voluntary NICs before 6 April 2009. The table below shows the costs to purchase one years additional contributions or the full six years allowable based on current NIC rates. We have also shown the costs and benefit of sweeping up lost NIC for the 1996/97-2001/02 tax years (shown in full in this example):

Years purchased	Benefit purchased *	Cost to buy	Equivalent annuity cost male/female**
One year (between the yers 2002/03-2008/09)	£165 a year	£421.20	£3,600/£4,700
Six years (between the years 2002/03-2008/09)	£990 a year	£2,572.20	£21,500/£28,000
OR			
1996/97-2001/02	£990	£1,977	£21,500/£28,000

* Annual index linked pension

** based on a male aged 65, female aged 60 and prevailing index linked annuity rates, single life only.

In summary, Class 3 contributions are very good value when compared to the corresponding cost to buy such an annuity in the open market but until 5 April 2009 they are exceptionally good value! If you think that you or your partner may have missed NIC contributions over the years please do speak with Gareth or I at the earliest opportunity as the 5 April 2009 deadline looms close. We can then provide individual guidance on this (complicated!) matter.

Ruth Sturkey
The Red House
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