Scotland referendum 2014: the impact of independence on pensions

Analysis of the potential impact of a Yes vote in the Scottish independence referendum on pensions.

Part of a collection of articles produced by the House of Commons Library which explore the potential impact of a Yes vote on the UK, aiming to inform the debate from an impartial viewpoint.

There would need to be a system for co-ordinating state pension rights built up in different countries

The existing EU system could provide a ready-made solution to this

The governments of Scotland and the UK would need to apportion responsibility for UK state pension rights built up before independence

Differences in tax and regulatory regimes would add complexity and cost for pension schemes operating across borders

Defined benefit pension schemes operating across borders within the EU could find themselves subject to more stringent funding requirements, although transitional arrangements could mitigate the impact of this

Responsibility for UK state pensions

Perhaps the most important issue would be the allocation of responsibility for UK state pension rights already built up.

Scottish Government position

The Scottish Government's document "Pensions in an Independent Scotland" says it would take responsibility for those of people living in Scotland at the time of independence.

The European Economic Area includes EU countries except Croatia, which will probably shortly join, plus Iceland, Liechtenstein and Norway.

Switzerland has many similar arrangements in the form of bilateral treaties

UK Government position

The UK Government's document "Scotland analysis: Work and pensions" (PDF) argues that the untangling of past records would be a complex exercise and that the government of an independent Scotland would also need to contribute to the state pension costs of people living overseas, some of whom would have worked in Scotland.

In the event of independence, there would need to be a system to co-ordinate the state pension entitlements of people who had lived and worked in different countries.

Overseas pensions

Scotland within the EU

If an independent Scotland joins the EU, there are arrangements under the co-ordination rules to enable individuals to make an application in their country of residence to an agency that arranges for each Member State where they were insured for at least a year to pay a pension.

In the UK, this is the International Pension Centre.

The pension received from each country corresponds to the length of the individual's social security coverage in that country. Further advice is available from the DWP State Pension in EEA countries website.

Uprating overseas pensions

Scottish Membership of the EU would resolve the issue of annual uprating.

The European Economic Area includes EU countries except Croatia, which will probably shortly join, plus Iceland, Liechtenstein and Norway.

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The UK State Pension is payable overseas but is only uprated in an EEA country, or one with which the UK has an agreement requiring this.

The UK has not made a new commitment to uprate pensions in a non-EEA country since 1981. The House of Commons Library has produced a briefing on frozen overseas pensions which gives further details.

Public service pensions

It is generally accepted that legal responsibilities exist towards those with accrued public service pension rights. However, responsibility for existing liabilities would have to be apportioned between the two new states.

In the case of those schemes which are fully or executively devolved, the Scottish Government says all accrued rights and entitlements would "continue to be fully protected and accessible."

The question of how to deal with those schemes which operate on a GB- or UK-wide basis, like the civil service and armed forces schemes, is more complex.

Scottish Government’s position

The Scottish Government’s “Public Service Pensions” says it would take responsibility for the pensions of those staff in the current civil service and armed forces who work in Scotland’s public service, and for those pensioners living in Scotland.

UK Government position

The UK Government’s document “Scotland analysis: Work and pensions” (PDF), on the other hand, argues that any apportionment should depend on the approach of an independent Scotland to public services more broadly, and the extent to which any services would continue to be shared.

Private pensions

Private pension schemes in the UK operate within a complex legal framework. Pension tax legislation, for example, places restrictions on the contributions individuals may make to a pension scheme, and the payments they can receive, without attracting additional tax charges.

Some pension providers have expressed concern that in the event of Scottish independence, having to deal with two regulatory systems would add to the complexity and cost of running pensions.

Pensions framework in the EU

Although the design of pension schemes is largely the responsibility of individual countries, the European Commission’s 2012 White Paper - para 2.4 (PDF) highlights an EU regulatory framework which applies to EU Member States. This:

- establishes an internal market for funded occupational schemes and the necessary minimum standards on prudential rules to protect scheme members and beneficiaries
- requires minimum guarantees concerning occupational pensions and accrued rights in case of the insolvency of the sponsoring employer
- applies anti-discrimination rules, although with some differentiation, to both statutory and private pension schemes.

Scottish Government position

The Scottish Government’s regulatory framework for pensions sets out that private pensions in an independent Scotland should be closely aligned with the UK. In particular:

- The body of law governing pensions would continue to apply in Scotland until amended, replaced or repealed by the Scottish Parliament
- A Scottish Pensions Regulator would work to maintain a pan-GB approach to the regulation of private pensions
- The current arrangements for the protection of individual’s pensions by the Pension Protection Fund should continue, although it would be for future governments to determine future arrangements
- It would develop a compensation scheme which would mirror the protection provided in the Financial Services Compensation Scheme
- The Pensions in an Independent Scotland: Supporting Pension Saving indicates that the Scottish government would continue with the roll-out of automatic enrolment into a workplace pension

Cross-border schemes

If an independent Scotland joined the EU, there would be implications for cross-border schemes (which are located in one EU country but accept contributions from an employer in another).

Under the European Occupational Pensions Directive (PDF), such schemes are required to be 'fully funded' at all times. This is in contrast to schemes operating within borders which, in the UK at least, may put in place 'recovery plans' to achieve full funding over a period of around ten years.

The Scottish Government's "Regulatory Framework for Pensions" page says that the EU rules allow a degree of flexibility and that it would be possible to agree transitional arrangements.

However, organisations such as the National Association of Pension Funds are concerned that if an independent Scotland became a member of the EU "a significant number of UK pension schemes would become cross-border schemes, and as such would be required to fill any funding gap."

Pension tax rules

The Scottish Government says it plans no immediate changes to the tax treatment of private pensions (PDF) at the point of independence (although future Scottish governments would wish to consider whether reforms could improve incentives to save). It is awaiting the outcome of consultation on radical reforms, announced in The Budget 2014 (PDF), to the tax rules for how people can access defined contribution pension savings.

From April 2015, people aged 55 and over will be able to choose when and how to draw income from their pension pot, subject to their marginal rate of income tax. This has proved controversial with some welcoming the freedom of choice but others concerned that it will place a significant burden of responsibility on individuals. The Scottish Government has said it agrees in principle with the greater flexibility but that much will depend on the detail.