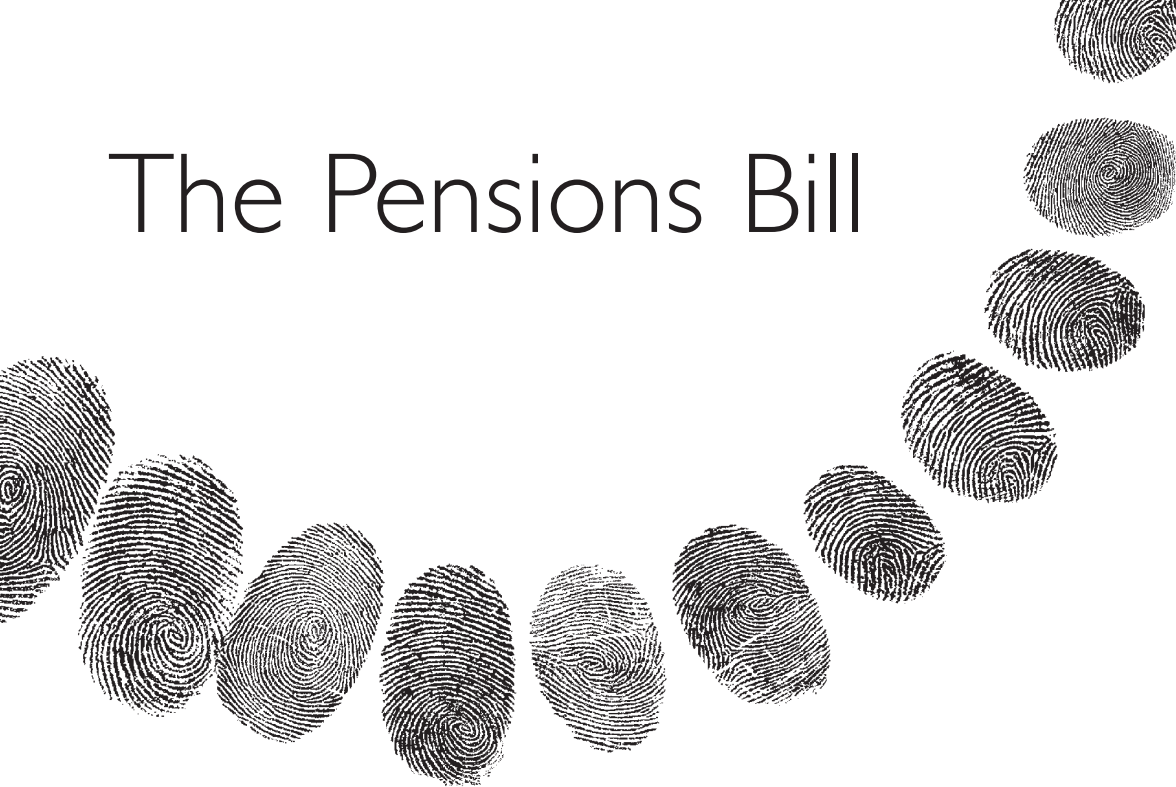


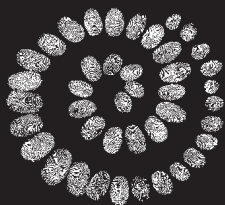
The Pensions Bill



The Impact of Pensions Reform Proposals on the Self-Employed from Black and Minority Ethnic Groups¹

A Runnymede Trust
Briefing Paper
March 2007

RUNNYMEDE



I. Introduction

The Runnymede Trust submitted a response to the proposals set out in the Pensions Reform White Paper, *Security in retirement: towards a new pensions system* in September 2006.² Generally, we welcome the publication of the pensions package that has set out progressive reforms for a new pensions settlement.

In the light of the Government's five tests for reform — promoting personal responsibility, affordability, simplicity, sustainability and fairness — we have focused on issues that particularly concern vulnerable groups in our society today. We have noted that there has been little reflection on the needs of Black and minority ethnic (BME) citizens, despite the fact that they already suffer social and economic exclusion and are more likely to live in poverty.

We are pleased that some important proposals that specifically benefit BME pensioners of the future had been proposed in the White Paper and were then reflected in the Bill, but the full package of proposed reforms still fails to address some of the inequalities that arise specifically from the disadvantaged employment situation and low incomes that many Black and minority ethnic people face.

These issues are discussed below in more detail. For the purposes of this paper we focus on what the pensions reform proposals presented in the Bill might imply for Black and minority ethnic self-employed people with a special regard to the low-income self-employed who are over-represented among BME communities. We also consider the potential implications of the proposals on personal accounts on Black and minority ethnic self-employed people. A more detailed consideration of the possible impact of personal accounts on BME groups will be submitted in due course.



In this paper we argue that low-income Black and minority ethnic self-employed people will not benefit equally from the reforms proposed in the Pensions Bill and Personal Accounts White Paper. Therefore we are using this opportunity of the passage of the Bill through Parliament to:

- draw the attention of all political parties and of Government to the existing differences and inequalities BME self-employed groups face in entrepreneurship;
- highlight the related important implications for pension provision; and
- call for the reconsideration of the extension of

2. Background to this paper

To address the lack of focus on the needs of Black and minority ethnic groups in the Pensions Commission's second and final report of November 2005, Runnymede undertook a small programme of work to introduce the pensions needs and experiences of BME communities into public and policy debates, suggesting areas for further research and encouraging better policymaking that includes all sections of our society. This culminated in our formal response to the Pensions Reform White Paper, *Security in Retirement: towards a new pensions system*, which included: (1) a research/discussion paper, *Proposals for Pensions Reform – Implications for Black and Minority Ethnic Communities* commissioned by Runnymede and authored by Dr. Helen Barnes of the Policy Studies Institute; and, (2) a set of case studies produced by the Pensions Policy Institute for Runnymede, which illustrated the potential impact of the reforms on the amount of state pension income received by individuals with characteristics similar to those seen in many BME households.

Current pension provision among BME groups shows significant differences compared to White pensioners.³ Minority ethnic pensioners have, on average, lower incomes than White pensioners.^{iv} Research on the extent of current pension provision among minority ethnic people of working age also suggests that they are significantly less likely than the White population to have access to private pensions. According to a survey by the Pensions Policy Institute, only 44% of non-White people have private pensions compared to 56% of White people, and, that among those aged 25-34, this difference is even larger than among older age groups (39% compared to 57%).⁴ These differences are attributed to the widely acknowledged fact that minority ethnic groups continue to face labour market disadvantage in the form of lower employment rates, lower earnings, early exits from the labour market and segmentation into particular sectors.

The ability of BME groups to make adequate provision for their retirement is further constrained by other factors particularly prevalent among minority ethnic groups: high rates of poverty, poor health, and lack of access to information. The factors that have the greatest impact on future capacity to save for pensions or to have access to job-related pensions provision are those that already marginalise certain BME communities in society today:

- low earnings;
- larger families for whose long-term financial support a (single) relatively low earner is responsible;
- late entry into the labour market so full pension entitlement cannot be built up;
- low skills and lack of language capacity;
- health problems, increasing the risk of redundancy and reducing the ability to save for pensions, and potentially having a long-term effect on employment prospects and earnings;
- restricted access for women to the labour market due to family commitments and/or lack of skills;
- although qualified for Basic State Pension, the self-employed are not eligible for State Second Pension and thus tend to be on the margins of provision unless very financially successful with a private pension and asset to dispose of on retirement;
- where migration is seen to be temporary in nature, this can militate against making and maintaining long-term pension commitments;
- BME groups are overall more likely to be qualified for means-testing but evidence shows they are less likely to take up the means-tested benefits to which they are entitled; and
- in addition to these factors affecting individual savings, BME groups also are more likely to have reduced access to Basic State Pension because of broken contributions records, e.g. because of caring activities, migration during working life, unrecorded periods of unemployment, and jobs paying less than the earning threshold for National Insurance.

Taking into account these factors, the key findings of our research/discussion paper demonstrated that the White Paper's proposed reforms offering improved coverage for those with interrupted work histories (particularly for those involved in child-rearing and other forms of care-giving), and reducing the spread of means-testing, would benefit BME groups (although perhaps not to the degree suggested). However, we also noted that the expectation that people will work longer may prove problematic for those in poor health and those facing multiple disadvantage in the labour market, who may still leave the labour market in their 50s and would therefore face the prospect of a longer wait before being allowed to claim retirement benefits. This is likely to have a disproportionate impact on certain BME groups.

On the positive side, among the reforms proposed in the White Paper and reflected in the Bill, there are several that would specifically benefit future BME pensioners:

- Reducing the contributions base from its current level of 44 years for men (39 for women) to 30 for all, and abolishing the minimum requirement for engagement in paid work would make a significant difference both to carers and to others with an interrupted work record, however it will not ensure complete pensions coverage.
- Changing the Home Responsibilities Protection (HRP) to a system of weekly tax credits for Basic State Pension and State Second Pension is welcome, the changes of HRP would considerably improve the position of those women who spend many years raising families or caring for elderly relatives.
- Linking increases in state pensions with average earnings rather than prices would also help to alleviate poverty and reduce reliance on means-testing.⁵
- Individualisation of benefit in place of dependency on 'breadwinner' entitlement would significantly improve the financial autonomy of retired BME women in the future, by providing them with an independent source of income.

Other proposals rejected in the White Paper and not included in the Bill but which could have potentially benefited future BME pensioners were fewer, and our comments on these can be found in our September 2006 research/discussion paper. But we feel strongly that access to State Second Pension for the self-employed is one reform proposal that deserves greater consideration and inclusion into the pensions reform package. This point is our major concern at the present time. **The implications of the continued exclusion of the self-employed from State Second Pension, particularly for BME people, are discussed in detail below.**

3. What the pensions proposals imply for Black and minority ethnic self-employed people

For the purposes of this paper, we focus on a consideration of Black and minority ethnic self-employed people, a group for which improved state pensions provision would be highly important given the high percentage of self-employed people overall who are not saving in private provision – 2 million out of the 3 million self-employed people in the UK are not saving in private provision.⁶ We argue that the decision not to extend the State Second Pension to the self-employed, a group where people from minority ethnic communities are over-represented

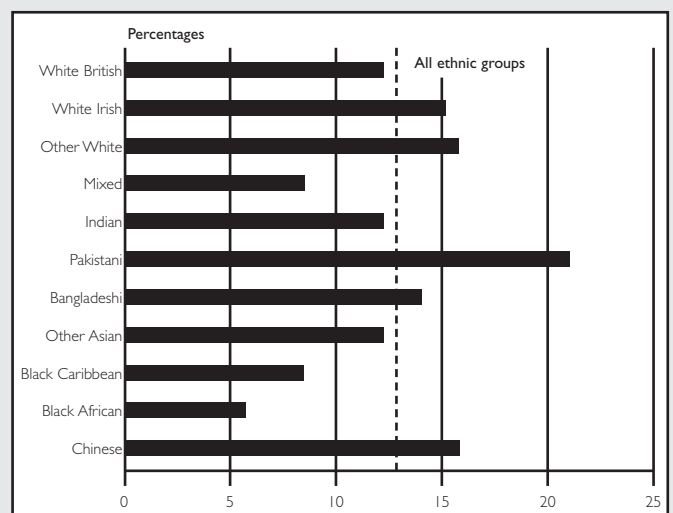
and which generally lacks the incentive to take up personal accounts, means that there is likely to be little improvement in their pension position based on the proposed reforms. **We therefore call on all political parties and Government to reconsider its position on this element of possible pensions reform and extend access of State Second Pension to self-employed people, especially those on low incomes.**

Personal accounts will be a major development in the UK pensions system. We encourage some reflection on the implications that the proposed scheme could have on the low-income self-employed. We believe that, while it is intended to make it easier for more people to save money for their retirement, **the proposed personal accounts scheme is likely to have a limited impact on a significant proportion of Black and minority ethnic low-income self-employed people.** This is because their disadvantaged economic position allows them to save only a modest amount, if anything, from their earnings. We address this in more detail below and will also be responding separately to the White Paper *Personal Accounts: a new way to save* (December 2006).

3.1. BME groups are over-represented among the self-employed

The over-representation of certain Black and minority ethnic groups in self-employment is a significant feature of the UK labour market. Across ethnic groups, however, this over-representation is not consistent. As Figure 1 shows, self-employment is particularly prevalent among Pakistani, Chinese and Bangladeshi groups. Pakistani and Chinese people have much higher rates: 23% and 18% of all those in employment respectively, compared to the White British population at 12%. Rates for other ethnic groups are either at the level of those of the White British population, as is the case of those of Indian background at around 12%, or lower, for example those from Mixed or Black Caribbean backgrounds at under 10%, and Black Africans at around 6%.

Figure 1: Self-employment as a percentage of all in employment: by ethnic group, 2002/03, GB



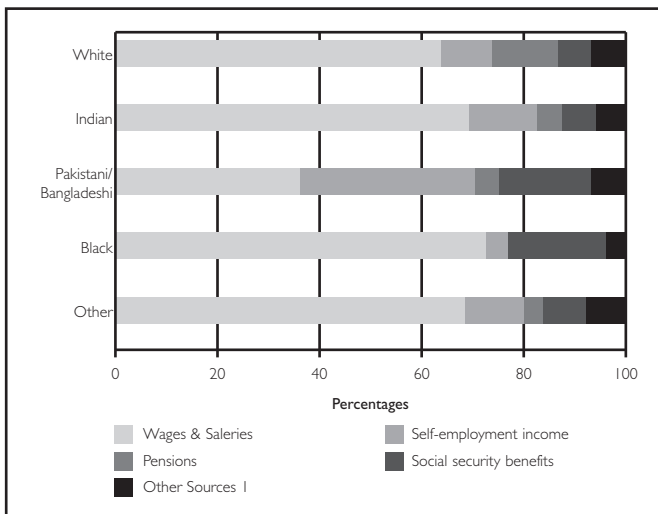
Source: Annual local area Labour Force Survey, 2002/03. ONS



Self-employment among ethnic groups is an important contributor for household income.

Figure 2 indicates income sources across Black and minority ethnic groups. Self-employment as a source of income among Bangladeshi and Pakistani groups accounts for a third of the total weekly gross household income. This is a far higher proportion compared to other BME groups. In the Pakistani and Bangladeshi group, income from self-employment is as important as paid work. This trend, however, is anomalous to other Black and minority ethnic groups where self-employment contributes on average 8% of total income.

Figure 2: Sources of total weekly gross household income: by ethnic group of head of household, 2000/01



Source: Family Resources Survey, Department for Work and Pensions 2000/01

Trends in self-employment among ethnic minority groups have changed over the last decades, showing a substantial growth in self-employment in the 1980s and a decline during the 1990s.⁷ A number of factors affect the choice of Black and minority ethnic communities between self-employment and paid-employment ranging from better job satisfaction to fear from discrimination in the paid labour market.

There are some important and persistent implications of entrepreneurship which affect BME groups' pensions planning and provision needs as set out below:

3.2. BME groups are over-represented among the low income self-employed, individually and by household income

It has been shown that full-time self-employed people are disproportionately over-represented among those with low incomes.⁸ Research using data from the British Household Panel Survey found that when other factors such as age, occupation, employment sector etc. were controlled for, a self-employed person had over three-times the chance of

falling into the poorest tenth of the overall household income distribution than did an employee. Data also shows that BME entrepreneurs earn substantially less than White entrepreneurs.⁹

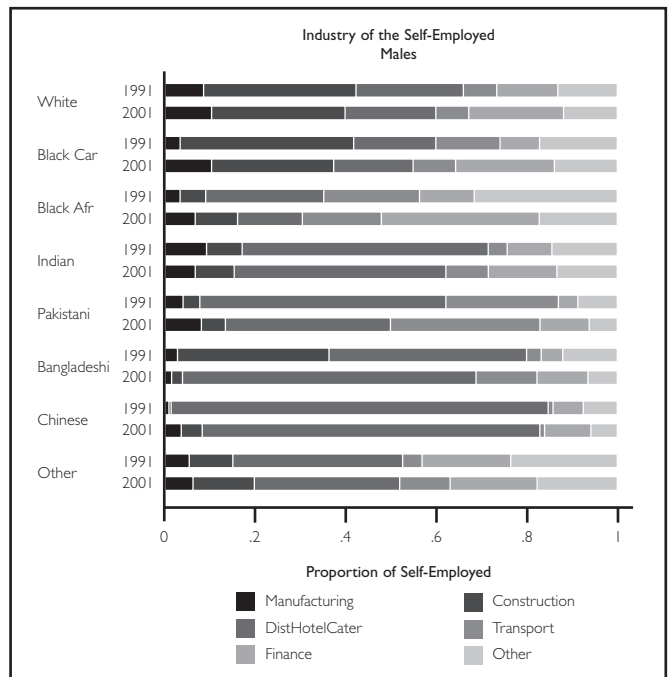
Those who are self-employed are also over-represented among low-income homeowners.¹⁰

According to the Family Resources Survey 2002/2003, in a quarter of households where only one adult is in employment, 39% of those are self-employed. One in ten self-employed low-income homeowner households are of Asian origin.

3.3. BME self-employed people are found in the industry sectors with highest levels of business failure

As noted by the Bank of England,¹¹ Black and minority ethnic groups in Britain tend to work in sectors where business failure rates are high. As Figure 3 shows, a large proportion of BME self-employed males are concentrated in the distribution, hotels and catering and transport sectors — the industry sectors with the highest level of failures. This is particularly acute for Pakistani, Chinese and Bangladeshi groups.

Figure 3: Industry of the Self-Employed (Males)



Source: Changing Patterns of Ethnic Minority Self-Employment in Britain, Clark & Drinkwater, 2006

3.4. BME self-employed people face a greater degree of uncertainty of income and financial security

The uncertainty of work and incomes, which stems from the fear of business failure, are compensated for by longer

working hours. It is well-established that the self-employed work longer hours than paid-employees in order to provide for some sort of financial security in case of 'random shocks', while receiving lower income returns.¹²

This greater degree of uncertainty of income and financial security among low-income Black and minority ethnic entrepreneurs determines future financial and pensions planning, as shown by the Department for Work and Pensions Research Report No 395 on '*Self-employment and retirement*'. The research report points out that men and women who are the sole or main earner in the household are more occupied with financial anxieties and concerns. Fluctuations in income, business start-up loans, mortgage payments and family needs, contribute to the factors affecting pensions savings and attitudes towards life after the State Pension Age. Over the life cycle of a self-employed individual, the propensity to save more depends on earnings improvements, paid-up mortgages and children becoming financially independent.

3.5. Language and cultural differences affect savings behaviour

Varying cultural attitudes towards saving for retirement is an important factor influencing savings behaviour. Nesbitt and Neary's qualitative study of retirement decisions¹³ suggests a strong preference for support from adult children among Pakistani and Bangladeshi men. Where strong norms of family support do exist, commitment to such an ideal may lead people in the prime of their working life to invest more heavily in their children's welfare than in their own future; remittances to the extended family overseas may also reduce disposable income for saving. Moreover, larger family sizes, longer periods in education, and higher rates of unemployment among young Black and minority ethnic people mean that some parents will still be providing financial support to their children at the time they retire.

The lower level of understanding and knowledge about pensions and related financial products by the self-employed in comparison to paid-employees¹⁴ is even more prevalent among BME self-employed with English language needs, as they have a particular reliance on clear and accessible information in community languages. In the absence of such information, self-employed individuals from Black and minority ethnic groups are likely to rely heavily on the advice and services of community intermediaries, who may not be providing them with the most appropriate advice and services.

The information deficit about the pensions system, coupled with low-income and an uncertain economic situation, leads to highly insecure financial statuses among Black and minority ethnic self-employed people. While a number of self-employed people have come from paid-employment and therefore may have accrued some savings as part of an occupational scheme, many self-employed are

in personal schemes. Attitudes research suggests that personal schemes are perceived to be risky.¹⁵ This leads to individuals opting out of personal schemes and relying solely on the future sale of business or home assets for pension income. Sale of business assets or property is an obvious yet highly insecure contribution to future income due to fluctuations in value or changing family situations.

In summary:

- BME groups are over-represented among the self-employed and in particular among the low-income self-employed individually and by household income;
- BME self-employed people tend to work in sectors where business failure rates are high;
- There is high uncertainty of income and financial security among low-income BME entrepreneurs which is particularly determinant of future financial and pensions planning;
- The information deficit about the pensions system and related financial products combined with uncertain economic situations among BME entrepreneurs is manifested in highly insecure financial behaviour leading to reliance primarily on the future sale of business or home assets;
- The self-employed do not have access to State Second Pension and do not benefit from 'matched' employer contributions, which means that they would need to save more, make higher contributions or accept lower retirement income than paid-employees in a personal account scheme;
- Given the variable cash flow and income uncertainty that great numbers of BME self-employed people experience, it is unlikely that their savings in personal accounts will build up an appropriate retirement income.

4. Conclusion

The pathways to saving for the future among self-employed people contain risk, instability and a high level of uncertainty. Dips in income, lack of information about financial products, and the absorption of risk contribute to this among the self-employed¹⁶; especially among Black and minority ethnic self-employed people. There are many more obstacles to saving in comparison to paid-employees.

Self-employed people do not benefit from employer contributions. Further, under current proposals, people who move from working as paid-employees into self-employment would receive a lower overall income from



Basic State Pension, State Second Pension and personal accounts than if they had been a life-long paid-employee.

Voluntary access to personal accounts is welcome; however self-employed people will not be able to benefit from 'matched' contributions in the same way as those working for an employer. It is also likely that the self-employed, particularly those engaged in low-income self-employment, where Black and minority ethnic groups are over-represented, will be less likely to take up personal accounts compared to paid-employees who are automatically enrolled. The self-employed will be required to make even higher contributions, save for longer or accept a lower retirement income.

Because of their limited propensity to make additional savings, whether into private pensions or personal accounts, **low-income Black and minority ethnic self-employed people would not benefit equally from the reforms proposed in the Pensions Bill and Personal Accounts White Paper.**

Changes to government policy on pensions need to take note of the existing differences and inequalities that exist between disadvantaged Black and minority ethnic groups and White Britons. Developing a new pensions settlement provides an opportunity to explore the experiences that BME self-employed people face in order to reduce inequalities and future pensioner poverty among BME communities.

We strongly urge all political parties and the Government to reconsider its position on the extension of access to State Second Pension for self-employed people, especially those on low incomes. Pensions reform should not work to worsen the already marginal financial situation people with this work/life pattern experience.

To discuss this paper and/or our views and concerns further, contact Michelynn Lafèche, Director of the Runnymede Trust on the contact details noted below.

Endnotes

- ¹ This briefing paper was drafted by Katalin Halasz with Michelynn Lafèche and Mehul Doshi. Thanks also to Dr Helen Barnes for her comments on our early drafts of this paper. We would also like to acknowledge and thank Friends Provident Foundation who provided the funding for our work on pensions reform, which has enabled us to produce this briefing paper.
- ² The Runnymede Trust's response to Security in Retirement: towards a new pensions system (DWP 2006), September 2006
<http://www.runnymedetrust.org/about/policyResponses.html>
- ³ Pensions Commission (2004) *Pensions: Challenges and Choices. The First Report of the Pensions Commission*. London: The Stationery Office
- ⁴ Pensions Policy Institute (2003) *The Under-Pensioned – Ethnic Minorities*. London: PPI
- ⁵ Yet the rejection of a flat-rate universal state pension would mean that many minority ethnic pensioners are likely to continue to rely on means-tested benefits. This is of particular concern given the over-representation of BME groups in low-paid work, including low-income self-employment. Any element of pension provision tied to individual earnings perpetuates the disadvantages that Black and minority ethnic groups face in the labour market and fails to appropriately address economic inequalities. For as long as BME groups continue to experience disadvantage in the labour market, contributory pensions will reflect this disadvantage.
- ⁶ Department for Work and Pension (2006) *Personal accounts: a new way to save*. London: The Stationery Office
- ⁷ Clark, K. and S. Drinkwater (2006) *IZA Discussion Paper No. 2495: Changing Patterns of Ethnic Minority Self-Employment in Britain: Evidence from Census Microdata*. Germany: IZA.
- ⁸ Using the basic definition of low-income: the lowest quintile and 60% of the median income
- ⁹ Clark, K., S. Drinkwater and D. Leslie (1998) 'Ethnicity and self-employment earnings in Britain, 1973-95' in *Applied Economics Letters*, 5, 631-634.
- ¹⁰ *Low-income Homeowners in Britain: Descriptive Analysis*, DWP Report 251
- ¹¹ Bank of England (1999), *The Financing of Ethnic Minority Firms in the United Kingdom*. Bank of England, London.
- ¹² Parker, S., Y. Belghitar and T. Barmby (2005) 'Wage uncertainty and the labour supply of self-employed workers' in *The Economic Journal*, 115, C190-C207.
- ¹³ Nesbitt, S. and D. Neary (2001) *Ethnic Minorities and Their Pensions Decisions: A Study of Pakistani, Bangladeshi and White Men in Oldham*, York: Joseph Rowntree Foundation
- ¹⁴ *Self-employment and retirement*, DWP Report 395
- ¹⁵ *Ibid*, pp. 41
- ¹⁶ *Self-employment and retirement*, DWP Report 395

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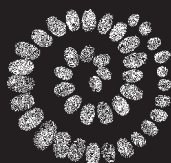
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ABOUT RUNNYMEDE

Runnymede is an independent policy research organisation focusing on equality and justice through the promotion of a successful multi-ethnic society. Founded as a Charitable Education Trust, Runnymede has a long track record in policy research, working in collaboration with eminent thinkers and policymakers in the public, private and voluntary sectors. Since 1968, the date of Runnymede's foundation, we have worked to establish and maintain a positive image of what it means to live affirmatively within a society that is both multi-ethnic and culturally diverse. Runnymede continues to speak with a thoughtful and independent voice on these issues today.

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