



Independent Review of the

State Pension age

Interim Report

October 2016



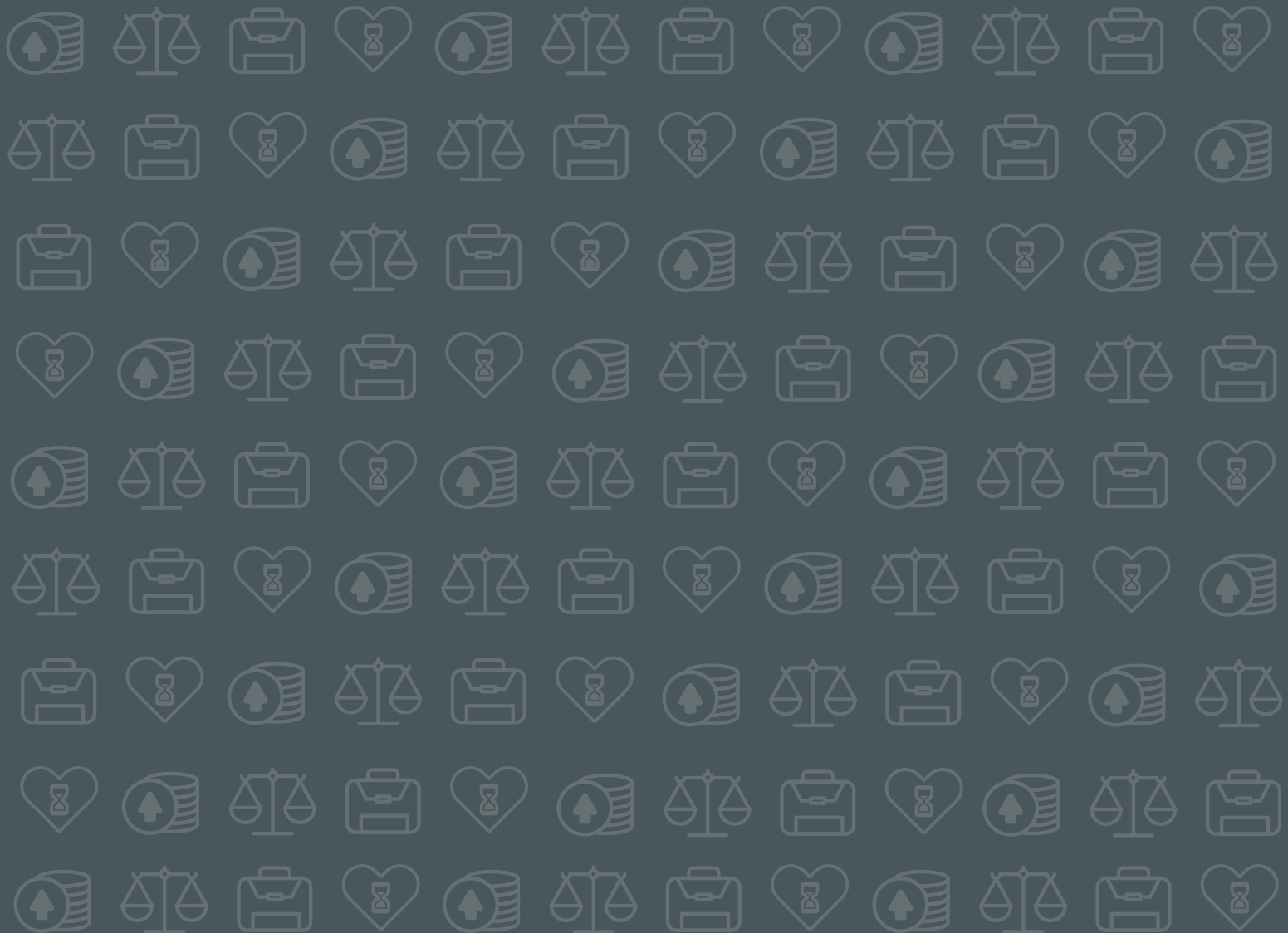


Table of Contents

4		Foreword
6		Executive Summary
12		Introduction
14		Section 01: Setting the Context
28		Section 02: The Three Pillars
52		Section 03: Life Expectancy
68		Section 04: Serious Impacts to Consider
85		Section 05: Smoothing the Transition
92		Annex A: Terms of Reference
93		Annex B: Consultation Questions
96		Annex C: State Pension age legislated

Foreword

I am grateful to the many organisations and individuals who have already been generous with their time, evidence and data. Such welcome contributions have enabled us to publish this Interim Report, which provides an insight into our developing thinking and poses a number of questions. We hope these will stimulate wider discussion and additional engagement.

An assembled team of civil servants seconded to the Review is providing me with support and assistance and I much appreciate their commitment and hard work. I will make recommendations to the Secretary of State and provide my final findings in 2017. These will reflect the valuable insights and objective analysis gathered throughout the Review period.

Being the first Independent State Pension age review, and benefiting from permissive Terms of Reference, we have considerable flexibility and scope when considering the evidence and analysis presented. The Review will take note of existing arrangements already in law, however it will be forward looking and keen to consider the changing demographic, economic and behavioural landscape of the future. These changes, rather than the present context, will be at the heart of my recommendations on setting the right State Pension age.

Please take advantage of our additional consultation period which lasts until the end of December 2016. We welcome all contributions and supporting evidence to ensure that we have considered the widest possible range of available information. Thank you.

Any research or insights that may help inform final findings should be emailed to us at: spa.review@dwp.gsi.gov.uk



John Cridland CBE

Independent Reviewer

A handwritten signature of John Cridland in black ink. The signature is written in a cursive style, with the first letters of 'John' and 'Cridland' being capitalized and prominent.

Executive Summary

Purpose:

This report sets out the evidence we have considered thus far and proposes a series of questions which have been identified as key in shaping any recommendations in the future.

Introduction:

The Review is forward looking and takes note of the existing arrangements before April 2028 which are already law.

At that point State Pension age will be two years higher than when it was first set in its current form 80 years ago. Longevity is changing the pensions landscape, with significant increases in life expectancy seen over the past few decades. The choice of State Pension age is not a decision which can be taken lightly, as it affects when people across society decide to retire and has a significant impact on public finances. It follows that any change in State Pension age can only be considered after a close examination of the evidence and the fullest understanding of the impacts any change will have on individuals, government spending and the overall economy.



Setting the Context:

First, we explore who the people most affected by this Review are and, in identifying them, we define the three generations that feature throughout our analysis: Baby Boomers (born 1945-65), Generation X (born 1966-1979) and Generation Y (born 1980-2000). All these generations may see their State Pension age affected by this Review. Generation X are most likely to need to take account of any changes to State Pension age in their retirement planning.

The State Pension has recently undergone significant reform with the introduction of the new State Pension, while automatic enrolment is predicted to change the value of savings people are likely to have. State Pension age needs to be considered in light of these developments, as they will impact people's ability to plan effectively for retirement.

Looking at the economics of pensions, we see that spending on pensions and pensioner benefits is influenced by a number of factors, including life expectancy and demographics, migration and uprating policy.

Lessons can be drawn from how other countries are dealing with similar demographic challenges. The UK is set to have the highest retirement age of OECD countries by 2060, but there are various policy options designed to incentivise people to work longer.



The Three Pillars:

Our Terms of Reference require us to consider three key pillars of **Affordability, Fairness** and **Fuller Working Lives**. We set out our approach to these here.

Measuring affordability can be achieved in different ways. We explore changes in the dependency ratio, looking at how the ratio of pensioners to working age people is projected to increase over time from 305 pensioners for every thousand working age people today to 357 per thousand working age people when Generation Y are approaching retirement nearing 2050. We also look at spending as a proportion of GDP, which the OBR forecasts to increase to 7.6% of GDP in 2044/5.

A significant aspect in assessing affordability, is the commitment made during the last two parliaments to uprate the State Pension more generously than legislated currently, through the triple lock

In assessing fairness, we focus on intergenerational fairness - whether outcomes are fair between each generation of pensioners - and intragenerational fairness - whether outcomes are fair within each generation of pensioners now and in the future. The gap between working age incomes and pension incomes has narrowed significantly over recent years. Due to changes such as the decline of defined benefit schemes, the introduction of automatic enrolment and the new State Pension, we see a reduction of inequality amongst individuals as we move through the generations. In the Baby Boomer generation there was a smaller number of individuals with high-value defined benefit pensions, whereas in Generation Y more individuals are saving albeit with a relatively less generous pension.

Supporting Fuller Working Lives is key to supporting any changes in State Pension age by giving people the opportunity to work longer. Recent employment trends have been positive for older workers – the number of workers over 50 has increased by 1.4 million over the past five years, and the employment rate gap between people aged 50-64 and those aged 25-49 has decreased by 7.6 percentage points since 1995. There are currently 1.2 million people aged 65+ who are in employment. This is more than double the rate seen around the turn of the twentieth century. However, a significant proportion of people still drop out of the labour market early, often due to issues such as ill health or disability. This is often described as 'burnout'. We need to explore how the labour market can accommodate this.



Life Expectancy:

Life Expectancy has been improving over time – in particular for older people. Since 1970, there has been a rapid decline in mortality rates at older ages, particularly for men. The Cohort Life Expectancy for men born in the UK in 2016 is 90.6 years, and for women 93.5 years.

Although Life Expectancy is still increasing each year, the 2014-based projections show a slower increase in improvements in mortality rates than the 2012-based ones. This is because mortality rates at some ages were higher in 2012 and 2013 than were projected in the 2012-based projections. Based on this finding, the OBR reported that the latest estimates of average Life Expectancy at State Pension age in the UK imply that State Pension age should rise to 68 by 2041; five years later than estimated on the basis of the 2012 projections.

The above indicates that there is uncertainty: for government, for employers and pension providers and most importantly, for individuals and their families when planning for retirement.

There are variations in life expectancy. The issue of differing life expectancy between nations or regions of the UK has received some attention, but evidence from ONS shows variations within geographical areas are larger than national or regional differences.

For example, men in Greater Manchester have a Life Expectancy at birth that is 2.4 years lower than in Greater London (77.2 vs. 79.6) and for women it is 2.6 years lower (81.2 vs. 83.8). However, the variations of Life Expectancy between different local areas within Greater London and Greater Manchester are even wider.

The socio-economic group that people are in also has a significant impact on Life Expectancy. Differences in Life Expectancy at birth between the lowest socio-economic group (Routine) and the highest (Higher, Managerial & Professional) are 5.9 years for men and 4.4 years for women (England and Wales only).

Healthy life expectancy (the proportion of life someone can expect to spend in “good” or “very good” health) appears to be keeping track with rises in overall life expectancy, but again there are quite substantial geographical variations.

Estimates from the 2011 Census show that men born in the UK between 2010 and 2012 could expect to live 63.2 years in “Very good or good” health (or 80.3% of their lives) and women 64.6 years (or 78.2% of their lives) if they experienced the same mortality patterns and rates of good health observed in that period.

If surviving to age 65 and observing the same mortality patterns and rates of good health, men and women could expect to live a further 18.3 years and 20.8 years respectively, of which around half would be in “Very good or good” health (9.1 years and 9.6 years respectively).



Serious impacts to consider:

If any changes are made to State Pension age, this is likely to have a disproportionate impact on certain groups. We consider potential impacts on the following groups: carers, people with disabilities, the self-employed, ethnic minorities and women.

Across all these groups, a recurring theme is that they have difficulty accruing sufficient private pensions savings to provide them with an adequate income in retirement.

Carers are a significant group in the context of the Review – around 1 in 10 adults have some caring responsibilities and some have suggested this is likely to increase in the future. Carers are more likely to have breaks in their work history, leading to an estimated gap between carers' and non-carers' median income in retirement of 4%.

People with disabilities may also face challenges in building up a private pension, particularly for those who are disabled from a young age. For non-disabled people, projected median income in the first year of retirement is around 7% higher than for those with disabilities. Stakeholders report that individuals working in certain professions have a higher risk of having to drop out of work early due to ill health or disability. This is an important group we will be looking to explore further in our final report.

Self-employed people are a diverse group with hugely different incomes and employment experiences. There is evidence to suggest that there is a downwards trend of self-employed people saving into a private pension, which means this group could become over-reliant on State Pension in retirement. We are looking to understand how the nature of self-employment is likely to change in the future and the impact on pension saving.

Evidence from stakeholders suggests ethnic minorities face disadvantage in the labour market which translates into poorer pension provision. We are keen to understand the challenges this group face.

Men and women across all generations are set to receive very similar amounts of State Pension. The discrepancy in pension outcomes for men and women instead reflects different private pension outcomes. On average across all generations, it is projected that just under 30% of women's total pension is made up of private pension, compared to just over 40% of men's.

State Pension age does not only impact individuals, but also interacts with the welfare system and with private pensions. Eligibility for certain benefits is linked to State Pension age, while certain private pension schemes use it to set their retirement age. The Review's focus is on our three key pillars as set out above, but we welcome opinions on whether these impacts should be considered within the Review.



Smoothing the transition:

The nature of work and retirement is changing, as people move from the old model of a fixed retirement age leading to a defined period of retirement to a more flexible approach where people may wish to work part-time or change career in later life.

The current State Pension has a universal age of access and, there is some value in a clear point in time when the state will offer retirement income.

If any changes are to be made to State Pension age, additional support may be required to mitigate the impact on the seriously affected groups discussed above and smooth their transition between work and retirement. Stakeholders have proposed options such as supporting individuals to work longer or increase their private savings. Others have suggested more direct interventions such as early access after a long working life or, granting early access to a reduced pension or enhanced working age benefits for certain groups.

We welcome evidence on how the Government, business and other organisations can support any changes. Finally, we recognise the importance of effective communications. Individuals need to be able to access the right information so they can plan effectively for their own retirement.

Introduction

Since the State Pension age in its current form was initially set in 1948, the UK has seen some significant increases in Life Expectancy. This is a welcome development which will have significant implications for the State Pension system.

The Chancellor of the Exchequer announced the Government's intention to reflect the changes in longevity at the 2013 Autumn Statement, setting out the principle that people should expect to spend, on average, "up to one third of their adult life in receipt of the State Pension".¹ Following on from this, the Pensions Act 2014 introduced a requirement for the Secretary of State of the Department for Work and Pensions to periodically review the rules on State Pension age and report to Parliament.

There are two key components to the legislative requirements. Firstly, the Government Actuary's Department must prepare a report to assess whether the rules about pensionable age mean that, on average, a person who reaches pensionable age within a specified period can be expected to spend a third of his or her adult life in retirement. Secondly, the Secretary of State must appoint someone to report on other relevant factors that need to be considered as part of the overall Government Review.

John Cridland CBE was appointed on 1st March 2016 to carry out the latter review, supported by a team of civil servants seconded to the independent Review. The Review is tasked with making recommendations on a suitable State Pension age, with the key objectives of supporting affordability, fairness and fuller working lives.² The review is forward looking and takes note of the existing arrangements before April 2028 which are already law. However, any recommendations that will alter the legislated timetable pre-2028 would undermine the important principle of allowing significant notice for any State Pension age changes in the future.

Over the past months, we have been gathering evidence and engaging in informal discussions with a range of stakeholders to draw out the key issues relevant to State Pension age in the future. The purpose of this Interim Report is to set out our initial findings and invite further evidence on key themes, which will inform our final report.

We have set out questions we wish to explore over the course of the report (a full list can be found in Annex B). We welcome submissions from interested stakeholders on the questions and/or other relevant issues to the review.

¹ HM Treasury, 2013, Autumn Statement, TSO

² The full Terms of Reference can be found in Annex A.

01 Setting the context





Introduction

Before considering the future policy and implications of changes to the State Pension age, it is important to clarify the role that the State Pension currently has. In the first Chapter, we will define the different generations who will be most affected by any change in State Pension age and attempt to capture the importance that State Pension has in people's plans for retirement. We also provide some analysis on the economics of pensions as they are today, and some international comparisons.

An evolving landscape

An exciting and challenging task for this Review is to attempt to look into the future and understand the demographic, economic and behavioural changes that are yet to come. Life Expectancy has increased significantly over the past few decades, and is projected to continue to increase into the future. These changes, and not the current context, should be at the heart of any recommendations on setting the right State Pension age post-2028.

State Pension age is currently a subject of national interest and captures public attention both as a good news story, when looking at the improving longevity statistics, and equally as an issue of discontent, for groups that feel disadvantaged by recent policy developments. Women born in the 1950s are currently a significant group in the latter category.

In the report we have tried to separate these current issues from our focus on the future. For the purposes of making our recommendations, the people whose lives we need to understand are not current pensioners or those nearing pension age right now. They are the working age population of today that will start retiring or start considering their retirement mainly in the 2030s. With this in mind, we will not be looking to comment on the pre-2028 State Pension age arrangements unless we expect them to be relevant to our timeframe.

Generations of Pensioners

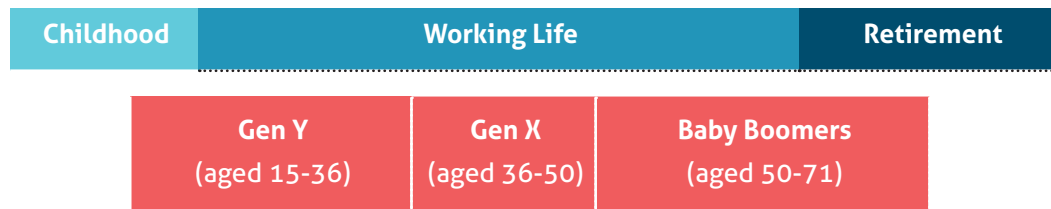
Given the long-term nature of the Review, we have attempted to define and better understand the generations that our recommendations may impact. The Pensions Act 2014 increased the State Pension age to 67 by April 2028. The next increase to 68 was legislated in the Pensions Act 2007 and is due to commence in April 2044. This was based on a programme of change recommended by the Pensions Commission over 10 years ago.

In this Review we will look at, in particular, State Pension age arrangements from May 2028, including the currently legislated changes to 68 in the mid-40s as far as it is reasonable to project so far into the future.

Given these time periods, this Review is considering three key generations, defined by their birth year:

Baby Boomers	1945-1965
Generation X	1966-1979
Generation Y	1980-2000

This chart shows where the three generations are now:



Baby Boomers are the oldest of the generations considered. Many will now be retired, although the youngest will be reaching their State Pension age in 2032, aged 67. Most older workers in this group will receive a new State Pension based on their pre-2016 National Insurance contributions or credits record.³ The majority of Baby Boomer workers retiring in the 2030s will receive at least the full rate of new State Pension when they get to State Pension age. Only around a quarter of people in the Baby Boomer generation remained in full-time education beyond the age of 18, suggesting many began their working lives before or at 18.

Generation X are now well into their working lives, ranging in age from 36 to 50. Many of them may be already planning for retirement, whilst for others retirement planning may seem too remote. Most will be covered in the system through National Insurance contributions or credits. This period of their lives will be key to building both their entitlement to new State Pension (most will get the full amount when they reach State Pension age) and private pension savings. Around a third of people in Generation X remained in education beyond the age of 18, which represents a slightly higher proportion than the Baby Boomers before them.

³ National Insurance credits are designed to recognise and protect the State Pension position of people who have caring responsibilities or who have interrupted working lives.

Generation Y are the youngest generation we are considering, ranging in age from 15 to 36. As is evident from this age range, some of those in this generation will not have even begun their working lives.⁴ Most are predicted to gain full entitlement to the new State Pension. Many younger members will see the benefit of automatic enrolment across their working lives, but even some of the oldest should see the benefit of automatic enrolment for over 35 years of their working lives. Of those in Generation Y who have begun their working lives, around half remained in full-time education beyond the age of 18.

All the generations may see their State Pension age affected by this Review. However, it is worth noting that Baby Boomers born before April 1961 are not likely to be affected as their arrangements are beyond the scope of this review. There is also the potential for Generations X and Y to be affected by future State Pension age reviews as they are legislated to occur at least once in every Parliament. Generation X are most likely to need to take account of any changes to State Pension age in their retirement planning. For Generation Y the shaping of the State Pension age policy may influence the plans they will need to make and it will set the tone for their key retirement planning decades.

In the context of State Pension age changes it is important to estimate how the generations will prosper across their working lives and what their income in retirement is likely to be.

The new State Pension – design and objectives

The new State Pension was introduced on 6 April 2016. It was designed to deliver a “single flat-rate state pension set above the basic level of the means test for future pensioners [which] will simplify the state pension and better support saving for retirement”.⁵ Maintaining the value of the full new State Pension above the means-test level is fundamental so that individuals, with even a minimal level of private savings for retirement, are less likely to need any means-tested welfare support. Consequently, most recipients of the State Pension will avoid seeing any private pension saving that they have means-tested by the Standard Minimum Guarantee element of Pension Credit.⁶ In this way the new State Pension is intended to provide a foundation for private saving and give people clarity about what they can expect in retirement from the state.

Under 2016/17 rates, the full new State Pension will provide a weekly income of £155.65 per week. In steady state this will be after 35 National Insurance qualifying years whether these are comprised of contributions or credits or, as is often the case, a combination of both. A transitional element will be in place for some years to ensure that the old system National Insurance contributions are recognised.

⁴ Automatic enrolment reforms require employers to automatically enrol eligible workers into a qualifying workplace pension scheme and pay a contribution, in addition to a government contribution in the form of tax relief.

⁵ Department for Work and Pensions, 2013, The single-tier pension: A simple foundation for saving, CM8528, TSO

⁶ The Pension Credit Standard Minimum Guarantee sets out the minimum weekly amount which recipients of Pension Credit are entitled to.

This new system replaced the basic State Pension and additional State Pension. The old system was already in a process of reform to implement the recommendations of the Pensions Commission, who had recognised the crucial role that state pension has in underpinning private pensions.⁷ The April 2016 changes retain the objectives of the Commission but introduce a radically reformed structure designed to be simple and to get as many new pensioners over the means test as possible.

The new State Pension should be seen in partnership with increased coverage of workplace pensions through automatic enrolment. The Government advocates that this arrangement, where the state delivers a basis for retirement while promoting opportunities to save privately, provides better chances for adequacy of income in later life.

The Policy Role of the State Pension

State Pensions policy has changed significantly in the 70 years since the Beveridge scheme was introduced in 1948. The State Pension started as a flat rate pension funded by flat rate National Insurance contributions. The objective was to deliver a weekly income above the poverty level but at a value that for most people meant that further private saving or other provision would be needed to achieve adequacy of income in retirement.

It changed to a two-tier pension with the introduction of the additional State Pension in 1978, where people received an earnings-related pension, based on earnings-related National Insurance contributions. In its original 1978 form it was supported by the basic State Pension which was uprated by earnings, so it would provide a form of an occupational pension for people not covered by employer schemes. This meant the state would take responsibility for their income (and in effect some of the adequacy of that income) in retirement. The adequacy of this new arrangement was quickly pared back. A series of changes to the policy meant that for many, low earners in particular, the additional State Pension did little more than make up for the fact that their basic State Pension was uprated by prices instead of earnings from 1980. A further key feature during this period was reform aimed at protecting the state pension position of women in their own right rather than as dependants of their husbands.

From 2016 the new State Pension delivers a flat rate pension based on earnings-related National Insurance. The value of the full new State Pension has been set just above the weekly means test. At the same time, automatic enrolment should ensure easier access to private saving for many working people. The policy objective appears to have returned to the 1948 model, where individuals take responsibility for adequacy of income in retirement to suit their own needs and aspirations, with the Government providing a basis that intends to protect most from poverty.

⁷ The Pensions Commission, 2005, *A New Pension Settlement for the Twenty-First Century: The Second Report of the Pensions Commission*, TSO

All post-1948 State Pension provision has been supported through the pay-as-you-go National Insurance system, where each generation of workers pays for each generation of pensioners. This is organised through the National Insurance Fund with expenditure smoothed from time to time by Treasury supplements from the consolidated fund.

The system has been regulated over time to ensure that each generation of workers can afford to support each generation of pensioners. Pressures like longer durations of entitlement because of increased Life Expectancy have been met in the past by reducing the value of the basic State Pension. This in turn led to an increase in the number of people who slipped into poverty, became entitled to means-tested benefits and were comparatively penalised financially for any private saving, eroding further the perceived rewards of private saving for retirement.

Despite rapid increases in Life Expectancy from the 1970s onwards, the first change to State Pension age from the 1948 system did not start until 2010, when State Pension age for women was set to equalise with men's at age 65 in 2020.

Further changes proposed by the Pensions Commission were put in place in the Pensions Act 2007 so that State Pension age would increase to ages 66, 67 and 68 starting from 2024, 2034 and 2044 respectively.

Further reforms in the Pensions Act 2011 and Pensions Act 2014 increased the speed of the changes above. The current timetable that sets the context for this Review is:

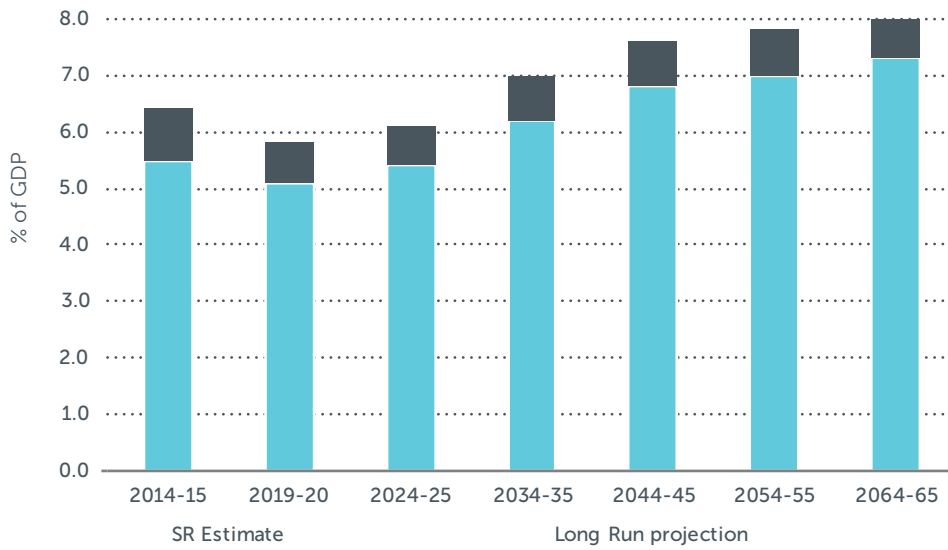
- **Age 66** – from December 2018 – October 2020
- **Age 67** – from April 2026 – April 2028
- **Age 68** – from April 2044 – April 2046⁸

Historically, the overall cost of state pensions has been controlled mainly by favouring a prices uprating policy over earnings, while other scheme design changes were introduced to control the cost of the additional State Pension. These same type of controls would be less effective in controlling expenditure in the new system because of its simplicity of structure and the need to retain the value above the means-testing level. The role of State Pension age is a more significant lever than ever before in maintaining control over the public cost and keeping up with societal changes, such as Life Expectancy. We explore this point in more detail in Chapter 2.

The chart below illustrates long-term pensioner spending as a proportion of Gross Domestic Product (GDP) and shows that this is projected to increase over the coming years.

⁸ Full legislated State Pension age timetable can be found in Annex C.

Figure 1: Long – run projections on pensioner spending (% of GDP) (2014-15 to 2064-65)



● Pensioner benefits ● State pensions

Figure 1: Long – run projections on pensioner spending (% of GDP) (2014/15 to 2064-65)

Question:

Is our interpretation of the policy intent for the State Pension correct?

The economics of pensions

Key concepts

To assess the overall impact of State Pension age changes and the affordability of the state pension system we need to know about the future population (how many people of working age and how many pensioners) and we need to know how much money might be available (the size of the economy). The Office for National Statistics (ONS) produces projections of the UK population and Life Expectancy as far ahead as the 2060s while the Office for Budget Responsibility (OBR) runs its estimates of the UK economy through a similar period. The most recent Fiscal Sustainability report by the OBR was published in June 2015. It is based on the 2012 population projections.

This review covers the period after 2028, and projecting estimates of the population and the economy this far into the future is of course uncertain. Beyond the medium term, estimates of population and the economy become a combination of projecting existing trends and modeling key assumptions (eg Life Expectancy, migration, productivity, earnings growth) based on the best available evidence. Forecasters therefore often present a range of different scenarios, showing the impact of uncertainty around key assumptions, and examine how their forecasts change over time, in order to improve their models.

The State Pension age review will need to make judgments based on a range of projections. We need to assess the impact of changes in those projections, and, given that we know projections will change over time, what contingencies any recommendations should have. A separate section in Chapter 3 looks specifically at changing projections for Life Expectancy and how this might affect what State Pension age should be.

Projections of population and the economy

Obviously there is some uncertainty over the state of the economy in the short term, but this is always the case. In the long term, uncertainty increases. The OBR (like other forecasters) estimates the likely average or trend growth for key economic variables, such as productivity and earnings growth, employment rates and so on. These assumptions determine how we expect the size of the economy as a whole, and the average income each person has, to change in future.

Population projections, economic forecasts, and fiscal sustainability estimates are closely linked. The ONS makes a range of assumptions when making projections of the UK's future population and these are then combined under different scenarios. In the long term, differences in assumptions on Life Expectancy, fertility and migration can have a substantial effect on the size and age of the population. The OBR takes the ONS's "principal" estimate of the UK population to underpin its own "central" projection of the economy and to create a range of economic projections.⁹

The OBR uses a range of economic assumptions, along with those on population, when assessing the sustainability of the UK fiscal position – or in simple terms, how much of the UK's income is being spent by the government and on what. Usually this is shown as government spending as a proportion of GDP.

Probably the most important economic assumptions for State Pension age review purposes are population (working age vs pension age) and productivity growth (which in turn determines growth in average earnings and therefore the triple lock uprating on basic State Pension and new State Pension).¹⁰ Both will affect the size of the economy, spending on pensions, and therefore "affordability" and the government's fiscal position, as measured by spending as a proportion of GDP.

Assumptions about productivity growth (which the OBR assumes matches earnings growth) and prices are important for determining the cost of triple lock uprating, as lower earnings growth increases the relative cost of the triple lock. The link to earnings means that upward changes in (labour) productivity growth in the economy will (at least in OBR projections) automatically feed through to state pensions.

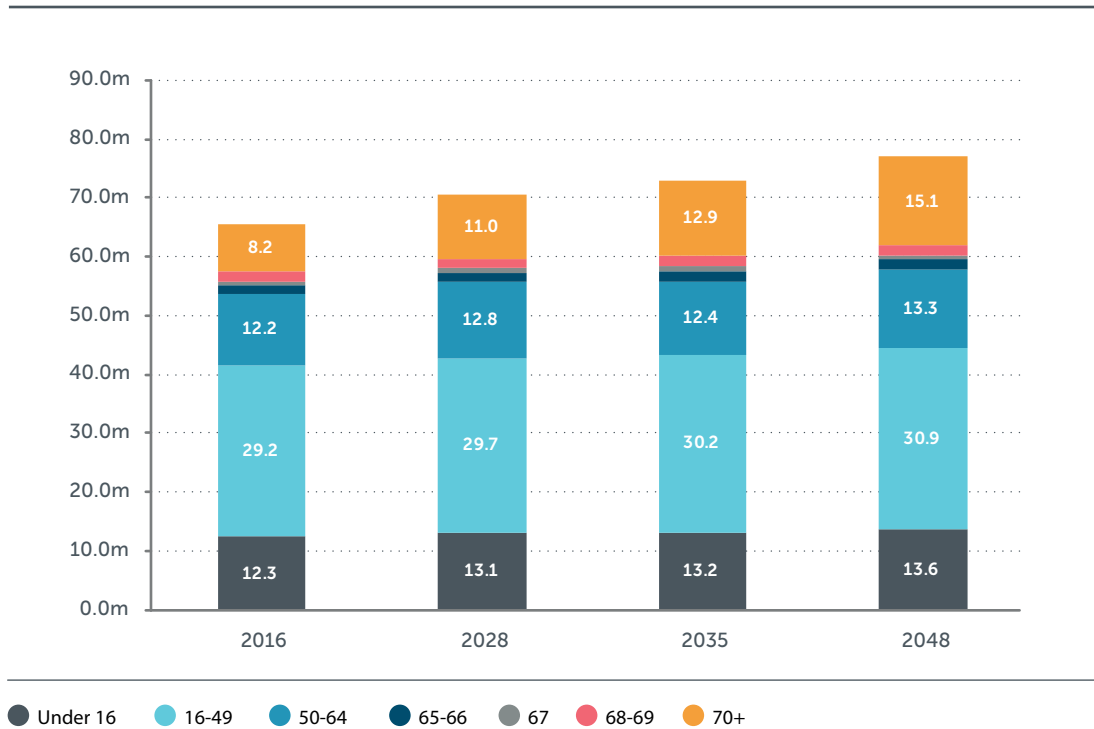
Changes to population, especially the ratio of working age to pension age people (if we ignore those who work past State Pension age for now) can change the measure of spending on state pension as a proportion of GDP. Similarly changes to the proportion of people in work could also affect the fiscal position – if there are more people working and paying taxes that would mean a larger economy to pay a given number of pensioners. We would need to see substantial changes in the number of people working to completely offset the likely increases in number of people living past State Pension age. The section on Fuller Working Lives examines this in more detail.

⁹ For details, see Office for Budget Responsibility, 2015, Fiscal sustainability report – June 2015, TSO, p61, Table 3.3

¹⁰ Under the triple lock, the State Pension is increased each year by the highest of price inflation, growth in earnings or 2.5 per cent.

The chart below shows how the UK population is currently projected to change over time (ONS 2014 based population projections).

Figure 2: UK Population projections by age group, over time (2016 – 2048)



Source: ONS, 2014-based National Population Projections, UK¹¹

OBR Fiscal Sustainability Report

In its annual Fiscal Sustainability Report the OBR produces Pensioner Spending projections which cover the period which the Review is focusing on (2028 onwards). The latest full published projections are from June 2015 using 2012 population estimates.

In 2028, the point at which State Pension age reaches 67, State Pension expenditure is projected to be 5.5% of GDP (roughly the current level). If State Pension age is linked to longevity, spending rises to 6.7% in the early 2040s – or 7.1% if State Pension age follows existing legislated rises. Different assumptions about the cost of the triple lock have an increasing impact over time, while the low and high migration scenarios also affect pension spending as a proportion of GDP. In OBR projections lower net migration has a higher proportion of GDP spent on all pensioner benefits as lower GDP offsets the slightly lower number of pensioners. The reverse is true for high net migration. We discuss costs in more depth in Chapter 2, looking at affordability.

¹¹ The 2014-based national population projections are based on the estimated population at the middle of 2014 and a set of demographic assumptions about future fertility, mortality and migration based on analysis of trends and expert advice.

International Lessons

This Review is keen to look at how the UK compares internationally and whether we can draw on any examples to inform our thinking over the next few months. Of course there are difficulties in drawing direct comparisons – other countries will have different socio-economic conditions, different pension systems, and different demographics – but the commonality of core elements of other systems makes comparisons worthwhile.

What are retirement ages across OECD countries?

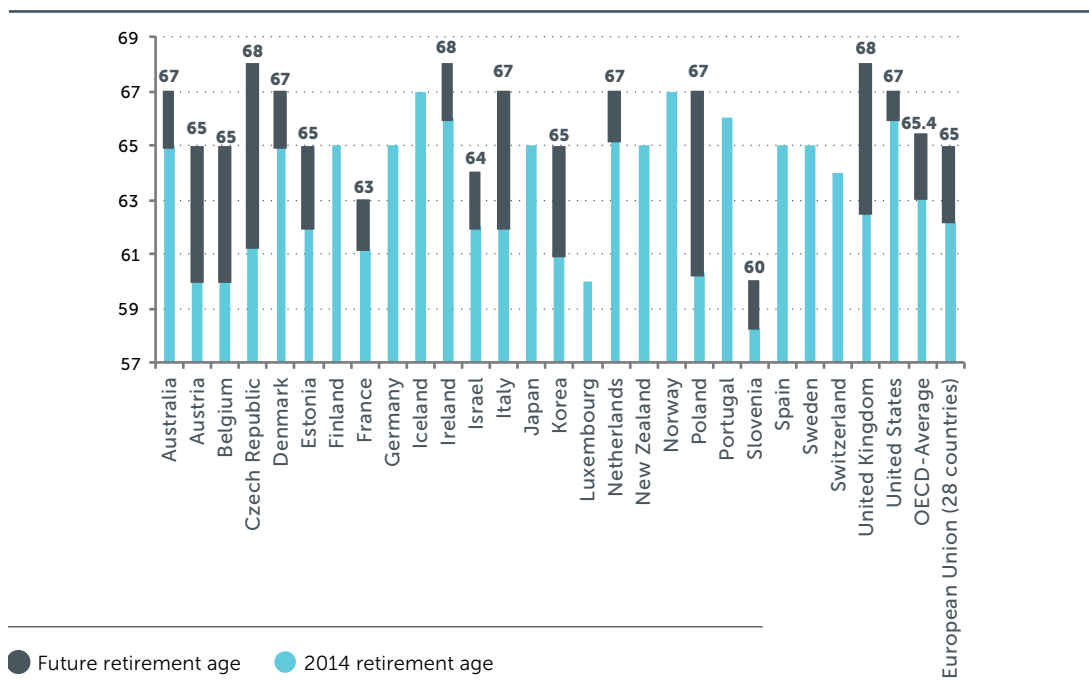
Looking across all OECD countries, the average retirement age¹² is set to rise from 64 years to 65.5 years by 2060¹³.

Currently, Iceland, Israel, and Norway have the highest retirement age set at 67. Examining current legislation, they are set to be overtaken by the UK, Ireland and the Czech Republic whose retirement age will rise to 68.

Slovenia maintains its position at the other end of the scale for the foreseeable future. It has the lowest current retirement age of 58.7 and this will only rise to 60 by the late 2050s. Luxembourg will also have a retirement age of 60 in the late 2050s.

Although the UK will have the highest retirement age of all OECD countries in the late 2050s, it is not the most aggressive rise in age. Italy for instance will increase its retirement age from 62.5 now to 67. Many countries will also have retirement ages near to that of the UK. By 2054, 15 out of 34 OECD countries will have a retirement age above 65.

Figure 3: Current (2014) and future retirement ages in OECD countries



¹² For comparative purposes, taken as of males entering the labour market at age 20.

¹³ OECD, 2015, Pensions at a Glance: 2015 OECD and G20 indicators, OECD Publishing, p13

Gender equalisation of pension age

The vast majority of OECD countries have equalised or are set to equalise their retirement ages. Thirteen countries currently have different retirement ages according to gender but only Chile, Switzerland, and Israel have no legislation to achieve equalisation.¹⁴

Early Retirement

The general trend across OECD countries is to limit the ability to take early retirement. This is being done through a variety of means, but mostly through either increasing the years related to eligibility, increasing the age one can take early retirement from, or a combination of both. Denmark and Spain are both increasing the age at which people can take early retirement. Belgium, Austria and Portugal are doing this as well as increasing the years related to eligibility. Both the Netherlands and Finland are abolishing early retirement, although in Finland this is for private sector workers only.¹⁵

In France and Germany, there are also possibilities for early access to state pension if someone entered the labour market early. In France, if people entered the labour market before age 18 they can access their pension at 60 (provided they worked at least 41.5 years). In Germany currently, those with at least 45 years of contributions can access their pension at 63. However, it is interesting to note that Germany is also limiting this in future and from this year will increase the age of early access by two months every year until it realigns with the standard retirement age of 65.¹⁶



“We have not identified, from the OECD work, any countries operating variable SPAs between different sub-groups of the population, except that some retain sex-based differences and some may allow particular professions (e.g. Army, Police, Fire-fighters, Trawlermen) to retire earlier than others.”

IFoA Submission to the Review



Institute
and Faculty
of Actuaries

Affordability, sustainability, and reforms

The increasing challenge of an ageing society is of concern across the OECD countries. Particular care has been taken to consider balancing adequacy in retirement with financial sustainability. Similarly to many of the policy suggestions we have heard from stakeholders, the key four areas where reforms have been focused are as follows:

1. Increases to retirement age
2. Decreasing the ability to take early retirement, or at least higher penalties for early pension
3. Financial incentives to work beyond normal retirement age

¹⁴ OECD, 2015, Pensions at a Glance: 2015 OECD and G20 indicators, OECD Publishing, p23

¹⁵ OECD, 2015, Pensions at a Glance: 2015 OECD and G20 indicators, OECD Publishing, p25

¹⁶ OECD, 2015, Pensions at a Glance: 2015 OECD and G20 indicators, OECD Publishing, p26

4. Greater ability to combine working and receiving some pension

Points 1 and 2 have been discussed in relation to other countries above, but points 3 and 4 merit some further consideration. Canada and Spain are two of the countries who have been encouraging older citizens to consider taking part of their pension whilst working by increasing the flexibility to access their pension whilst also remaining in employment.

Norway has also increased pension flexibilities to enable longer working by requiring private schemes to allow partial draw-down. Switzerland has focused on this issue but taken a slightly different approach, by increasing the age limits for contributing into a pension so that citizens can continue to benefit from paying into a pension in their later working lives.

Canada, Australia, and Sweden have made some provision of financial incentives to work beyond normal retirement age. In Australia, this has focused on employers who are given financial incentives to employ older workers. In Sweden, the incentives are focused on employees, who from 2014 have been granted more generous earned income tax credits if they are working after 65.

In Canada, financial incentives are also directed at workers, although through retirement income rather than working income. There it is possible to defer both an earnings-related pension and the flat-rate Old Age Security (OAS) pension for increased returns. For the OAS pension, the increment is 7.2% per year and for the earnings-related pension the increment was 8.4% as of 2014. However, there is an age limit to this system, and once a person reaches 70 there is no financial benefit to deferring their pension.

Conclusions

Of the OECD countries the UK is one of the most advanced in policies directed at the pension age. According to planned legislation, it will have the highest retirement age of all OECD countries by 2060. It must however also be recognised that it has one of the smoothest rises in pension age and that many countries may well raise their pension ages with less notice between now and 2060 to join the UK at 68 or go further.

Looking at other OECD countries' approaches to working longer, the trend is clearly to limit support, or in some cases access, to early retirement but instead focus on encouraging working longer through a mixture of financial incentives and pension flexibilities.

Question:

How successful are other international policies? Are there any other policies that we could consider? How should the UK policy on State Pension age take these examples into account?

02 The Three Pillars





Defining the Scope

This Chapter discusses how we will approach our Terms of Reference and how we understand the three pillars of Fairness, Affordability and Fuller Working Lives. We will set out what we understand by the State Pension age arrangements being affordable in the long term, fair to current and future generations of pensioners and consistent with supporting fuller working lives.

In the first part of the chapter we look at affordability. We look at current spending on state pension and estimated expenditure in the future. We also look at how the state pension is funded and the dependency ratio, followed by the main drivers of expenditure - the increasing numbers of pensioners who are living longer and the design of the State Pension itself.

We then consider fairness, asking whether outcomes are fair within each generation of pensioners now and in the future, and also whether they are fair between each generation.

Finally, we consider Fuller Working Lives and, in particular, the importance of the labour market for pension policy and for older workers.



Affordability

The costs of the current system over time

In Chapter 1, we described that the Government's objective for the new State Pension is to deliver a weekly benefit to most people that is set above the limit of the weekly means test. This is achieved by:

- A full amount of new State Pension set at £155.65 compared to the Standard Minimum Guarantee in Pension Credit of £155.60. Both amounts are required by primary legislation to be increased each year to reflect the growth of earnings. This means that the poorest pensioners still share in the prosperity of the nation and people who have a full new State Pension always have an income above the basic means test.
- Setting the conditions for building the new State Pension in such a way that most people can achieve the full amount. The full amount requires 35 National Insurance qualifying years of contributions or credits and by 2028, negating for the effects of contracting-out¹⁷, around 90% of people will reach State Pension age with a full new State Pension.

To achieve the Government's objectives this is the system that must be afforded at any one time. It follows therefore that pensions policy has to be able to respond to an increasing caseload because more people are living longer.

The Pension Commission recognised these dynamics of longer Life Expectancy in an ageing society, saying that it was "essential to keep the increase in public expenditure within limits which are fair within generations and sustainable in the long term"¹⁸ and for this reason recommended at the time that State Pension age should be increased in line with increases in Life Expectancy.

Furthermore, the Government announced the principle that State Pension age should be set in such a way that people could expect to receive the State Pension for, on average, "up to a third" of their adult lives.¹⁹

Meeting the costs of the state pension

As we mention in Chapter 1, the State Pension depends on "pay as you go" funding which is organised through National Insurance contributions, meaning that pensioners depend directly on working age people to achieve a retirement income. So for all pension systems, affordability is first determined by the number of people capable of work who can support those not in work. One way of measuring this is the dependency ratio: defined as the number of pension age people per thousand working age people.

¹⁷ Including the effects of contracting-out, by 2028 83% of people will reach State Pension age with a full new State Pension, increasing to around 85% by the mid-2040's (after the last contracted out people have reached SPa).

¹⁸ The Pensions Commission, 2005, A New Pension Settlement for the Twenty-First Century: The Second Report of the Pensions Commission, TSO

¹⁹ HM Treasury, 2013, Autumn Statement, TSO

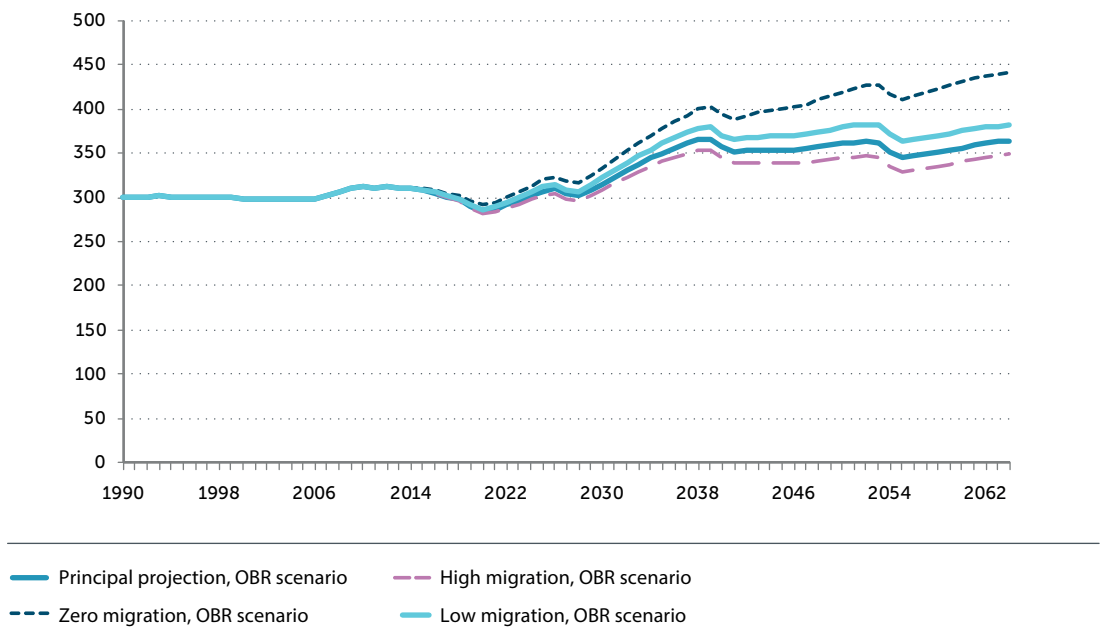
The ONS population estimates allow us to look at projections of the dependency ratio over the next 50 years. The ONS use a range of assumptions on life expectancy, fertility, and migration, so we can see what happens under different scenarios.

The chart below shows how the dependency ratio changes over time. The estimates, like those for future spending, assume that State Pension age changes in line with the Government objective that people spend up to one third of their adult life with entitlement to state pension.

The ratio of people at State Pension age and above to those of “working age” rises over time, although increases to State Pension age have the effect of delaying when this rise happens. This means, other things being equal, as a nation we will be asking a progressively smaller number of people to pay for an increasing number of pensions in payment. The chart also shows the impact of migration. Clearly the higher the working age population (either through migration or higher birth rates) the easier it is for those workers to meet the costs of the pension population.

This is a challenge the UK shares with most developed countries which are facing significant rises in the dependency ratio.

Figure 4: Old age dependency ratio projections under different migration scenarios, 1990 -2062, People above SPa per 1000 working age

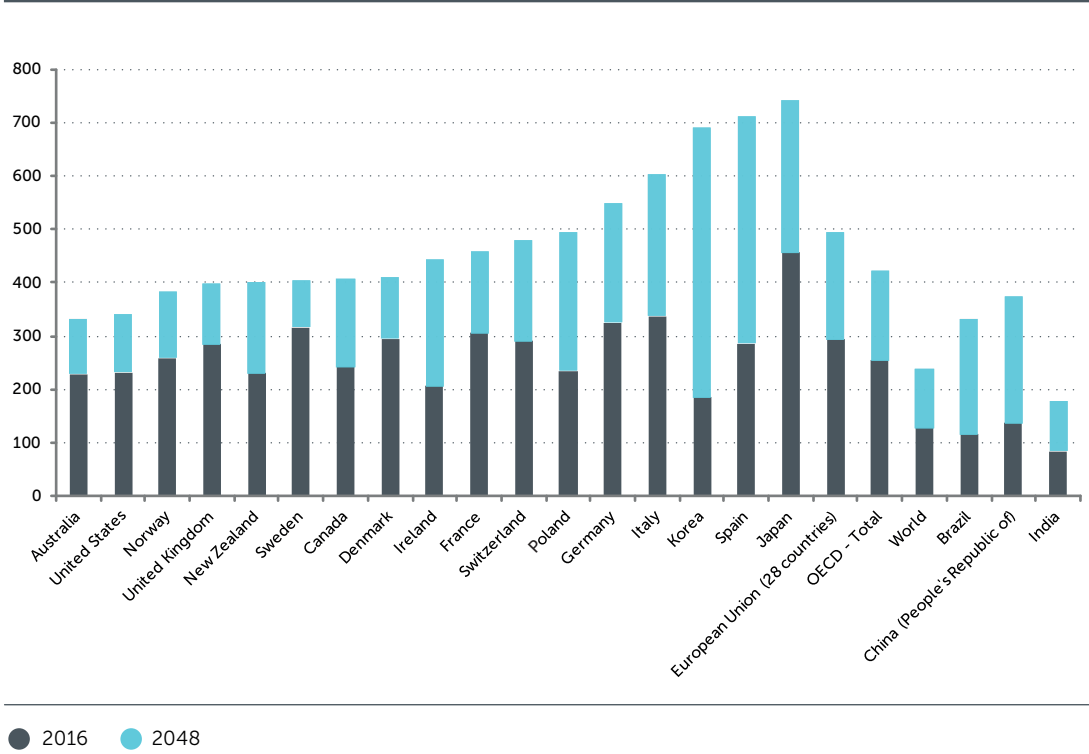


Source: ONS Old – age Dependency ratio data based on 2014 Population Projections and OBR Scenarios

Migration (and fertility) don't affect SPa – but do affect dependency ratio, and affordability as a % of GDP

2014 Population projections see a slightly slower rise in Life Expectancy – this pushes back rise in SPa to 68 based on the “1/3 rule”

Figure 5: Old age dependency ratio projections (2016 vs. 2048) - People aged 65+ per 1000 working-age



Source: OECD statistics

Other Drivers of Affordability

We have shown that to a large extent the costs of the system are pre-determined by: 1) the policy intention for the State Pension to provide an income above the means-tested level; 2) the increase in Life Expectancy; and 3) the principle that people should spend up to a third of their adult life receiving the State Pension.

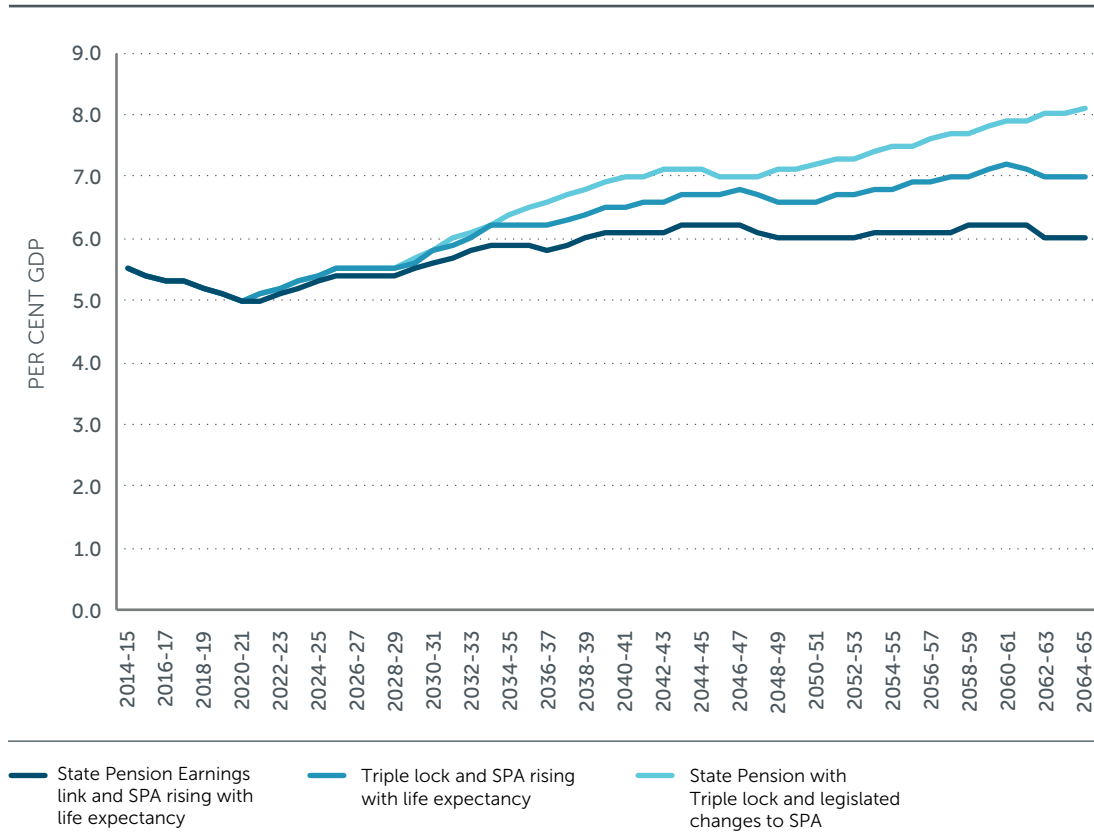
A significant aspect in assessing affordability is the commitment made during the last two Parliaments to uprate the State Pension more generously than legislated currently, through the triple lock.

The triple lock was introduced in the last Parliament and provides that the basic State Pension and new State Pension is increased each year by the higher of prices or earnings, but if prices and earnings growth are less than 2.5% then the State Pension will increase by 2.5%. The triple lock is not a legal requirement (the legal requirement is to increase basic State Pension and new State Pension by earnings growth) but the OBR includes the triple lock in its estimates of long-term state pension spending.

The triple lock uprating has meant that the basic State Pension recovers some of the value it lost in the last two to three decades when uprating did not keep up with the growth of the UK economy. The triple lock benefits better off pensioners who have had poor returns on their savings over recent years. It also means that the income of some less well-off pensioners has been lifted over the Standard Minimum Guarantee.

On the other hand, the impact of the triple lock over time is significant. Each time it is activated, pension payments increase by the highest of the triple lock factors, adding more each time to the consolidated amount to be uprated in the future. The chart below shows the costs of the system using alternative policy scenarios.

Figure 6: State Pension spending projections under different uprating scenarios (% of GDP), 2014-15 to 2064-65



Source: Office of Budget Responsibility, Fiscal Sustainability Report 2015

There appears to be a consensus on the Government’s objectives that the new State Pension should be a robust and durable underpin for private saving. However, we have repeatedly heard that ending the triple lock uprating of the State Pension from 2028 could delay further increases in State Pension age; so that pensioners in the future could receive less weekly income but have it paid from an earlier date. So the overall proposition is trading how much pension an individual can get with when they are eligible to get it.

Under the scenario above, where state pension is linked to earnings, the policy objective of delivering a pension above the means test would be met – in earnings terms the new State Pension will still be the equivalent of £155.65 when Generations X and Y reach State Pension age. It is worth noting that while the triple lock is of benefit to all pensioners, it is particularly important, as described in Chapter 4, to disadvantaged groups.

As mentioned above, withdrawing the triple lock has been identified by some people as a way of mitigating the impact of State Pension age changes. The other lever in play is the number of people who are covered by the full amount of new State Pension.

The coverage arrangements, where people build National Insurance Qualifying Years on both contributions and a range of credits and where full entitlement is achieved in 35 years of a 50 plus years working life, means that by 2028 some 90% of people qualify for the full new State Pension, negating for the effects of contracting out.²⁰ It is possible to reform these arrangements by increasing the number of years required for a full new State Pension so that savings could be reinvested in State Pension age mitigation. However, this may undermine the Government's overall objective, because more people would see less state pension than the Standard Minimum Guarantee at State Pension age.

There are other areas of benefit spending on pensioners, such as Winter Fuel Payments, which do not contribute to the Government's core State Pension objectives. However, these are discretionary amounts and we have discounted them in our considerations.

Question:

Considering the main drivers of State Pension expenditure, which ones are more important to the policy intent, if they were presented as a trade-off? Maintaining early access, a generous increase annually or ensuring that most people can achieve the full rate of the new State Pension? Which of these delivers fairer outcomes?

Conclusions

There are 13 million pensioners now. By the time Generation X get to State Pension age in the mid 2030s there will be 15.5 million people over 67 (17.2 million over 65) and by the time Generation Y gets to the current legislated State Pension age (68) in 2048 there will be around 16.6 million pensioners (19.1 million people will be over 65).

Today there are 305 pensioners for every thousand people of working age. By the time Generation X are approaching retirement in the mid-2030s there will be 350 pensioners aged 67+ per thousand people of working age, and 357 pensioners per thousand people of working age when Generation Y approach retirement nearing 2050 (68+). Over the same time period the state pension itself will become less generous for some pensioners while more generous for others. Overall, spending on the new State Pension is much the same as the scheme implemented in response to the Pensions Commission until the 2040s. After that, the post-2016 system starts to cost less than the old system. However, costs are still increasing due to the increasing number of pensioners.

The Pensions Commission estimated that overall expenditure on State Pension and pensioner benefits would reach 7.6% of GDP in 2050. This is broadly in line with the current OBR projections that State Pension and pensioner benefits expenditure, including the triple-lock and adjusting for Life Expectancy based on the 2012 projections, is going to reach 7.6% of GDP in 2044/45.²² This falls within the Pension Commission's proposed

²⁰ Including the effects of contracting-out, by 2028 83% of people will reach State Pension age with a full new State Pension, increasing to around 85% by the mid-2040's (after the last contracted out people have reached SPa).

²² This includes benefits pensioners receive such as Disability Living Allowance and Housing Benefit.

²³ The Pensions Commission, 2005, A New Pension Settlement for the Twenty-First Century: The Second Report of the Pensions Commission, TSO, p13

“envelope” of 7.5%-8%.^{23[1]} On the position post-2045, the Pensions Commission said of the 7.5% to 8% range that “fairness between the generations suggests that public expenditure on pensions as a percentage of GDP should stay roughly constant. If Life Expectancy goes on rising this will require further rises of State Pension age in proportion to Life Expectancy, allowing each generation to enjoy the same proportion of life contributing and receiving state pensions.”

Question:

Is the Pensions Commission’s assessment of the proportion of GDP expenditure on pensioner benefits, over time, still valid, when considering State Pension age affordability post-2028? Is State Pension age the best tool to maintain a steady GDP proportion for pensioner benefits?



Fairness

All groups have an interest in ensuring the Government’s investment in pensions is fair. If at any point the gain from the state pension is not enough for pensioners or costs too much for workers, there is a danger that the financial and social contract between the two groups will break down.

As many stakeholders have acknowledged, measuring fairness is complex, as there are a range of perspectives on what constitutes fairness in the context of State Pension age. In considering fairness of any changes, we will be looking to explore two main aspects. Firstly, we will explore whether the Government is distributing its investment in pension provision fairly between generations and within generations. Secondly, focusing on groups who are likely to be disadvantaged in terms of pensions outcomes, does the system treat those individuals fairly? Are there specific barriers for certain groups which will significantly affect their opportunity to build an adequate income in retirement?

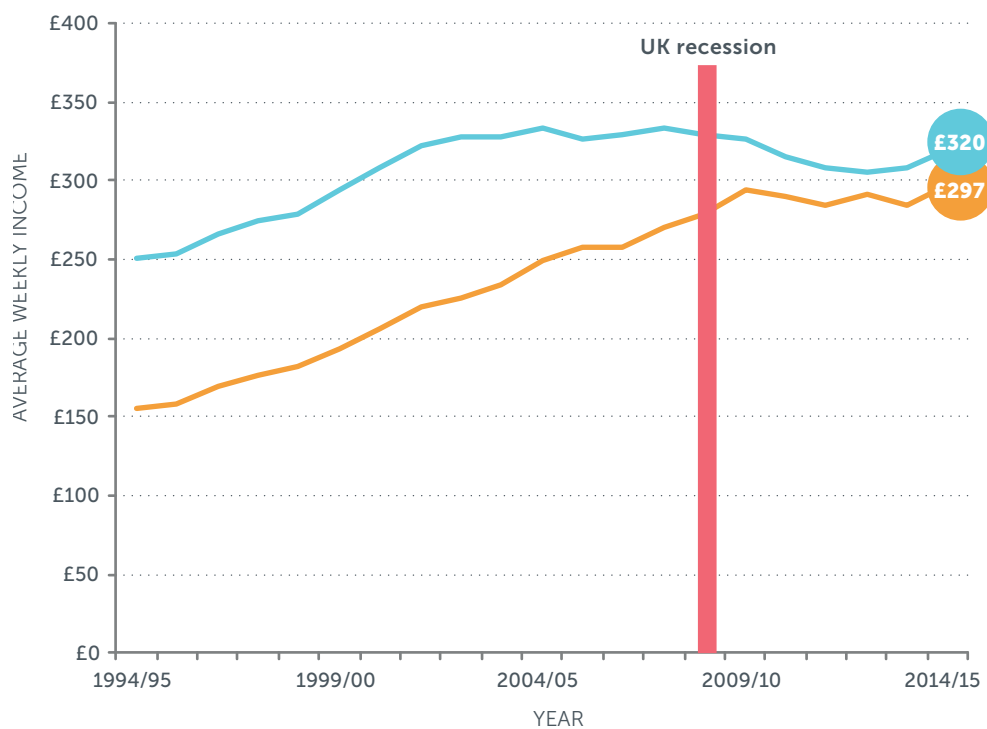
It is inevitable that some people will fare less well than average when it comes to pension access and provision, regardless of how State Pension age is fixed. This happens now and will continue to happen in the future. It may be that their opportunity to save privately, or in some cases their ability to build a full new State Pension, has been restricted because they have had an interrupted working life or have had to restrict their earnings potential through no fault of their own. It may also be that their income is limited immediately before State Pension age and waiting longer for a relatively higher pension will cause them hardship. We discuss disadvantaged groups in more detail in Chapter 4.

Intergenerational fairness

The current balance between generations

In recent years, there has been a considerable levelling of working age and pensioner income, as can be seen in the chart.²⁴ In 2014/15, the average weekly pensioner income was 7% lower (around £23 in 2014/15 prices) than that of working age people. In contrast the position 20 years earlier was that pensioner income was 38% lower (around £96 in 2014/15 prices) than working age income. Research from the Institute of Fiscal Studies shows that the over-60s cohort are the only age group to have become better off since 2007-08²⁵.

Figure 7: Average weekly income of pensioner units and working-age population benefit units (After Housing Costs) in 2014/15 prices (£), using unequivalised income



— Working age population — Pensioners

Source: Pensioners’ Incomes Series: An analysis of trends in Pensioner Incomes: 1994/95-2014/15

Working age incomes were flat ahead of the financial crisis, and have declined since then. Combined with relatively strong private pensions (and earnings) for younger pensioners, the gap between the two groups has closed. In addition, the triple lock has meant that those pensioners with a full basic State Pension are around £11 a week better off than if their pensions had been increased by earnings growth. A further consequence of this has been

²⁴ Department for Work and Pensions, 2016, Pensioners’ Incomes Series: An analysis of trends in Pensioner Incomes: 1994/95-2014/15

²⁵ C. Belfield et al, 2016, Living standards, poverty and inequality in the UK: 2016, IFS Report (R117)

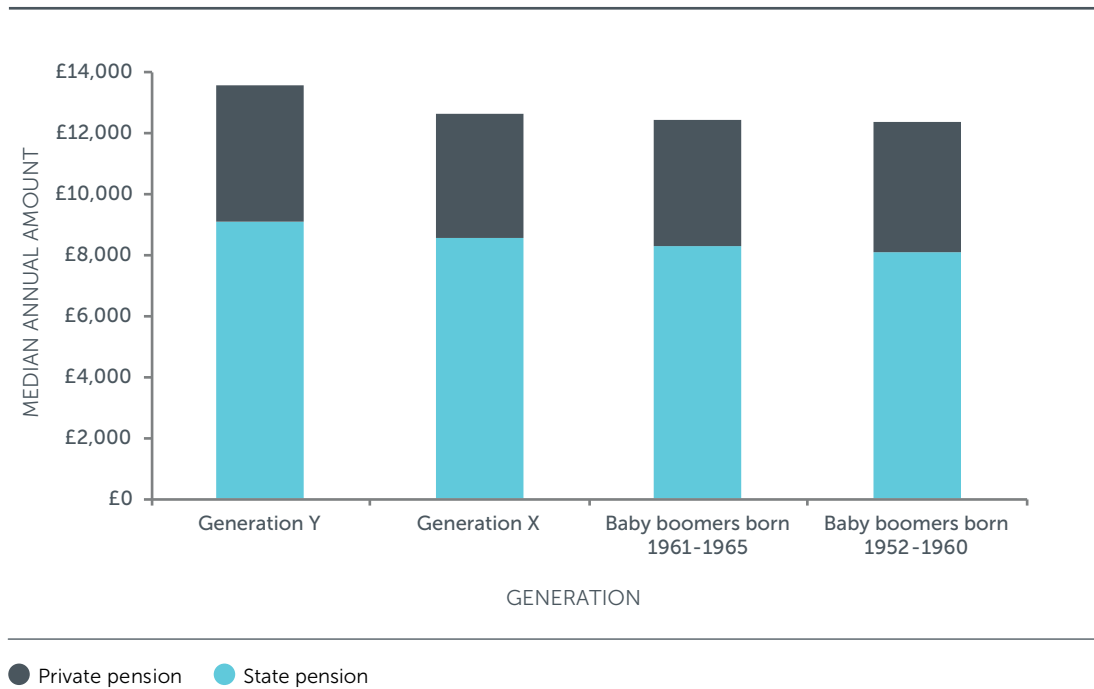
the higher than earnings increase in the Standard Minimum Guarantee, which combined with other factors now means that pensioners are less likely to live in poverty than other groups.

Comparison of pension outcomes

When considering the pension outcomes across generations we will look both at the projected adequacy likely to be achieved by future generations compared to current pensioners and a more direct comparison of what future generations are likely to get out of the State Pension compared to their predecessors. This latter comparison is key when considering the value of State Pension payments in the context of likely longevity for each generation.

Looking forward to pension value across the generations, the chart below shows projected median average state and private pension incomes in a person’s first year of retirement for Baby Boomers, Generation X and Generation Y (note that the median amounts include those with zero pension)²⁶:

Figure 8: Projected median average amounts of State Pension and private pension in 1st year of retirement, by generation



Source: PENSIM2

The chart shows that over time, total median pension values are projected to increase. Median State Pension amounts increase relative to earnings as more people in the future receive the full amount of State Pension and those in the younger age cohorts benefit for longer from the triple locking of the State Pension.

²⁶ All figures are expressed in 2016 earnings terms and the generations shown in the charts are based on current ages as at 2016. Unless stated otherwise, zero amounts are included within the median state and private pension incomes. Median private and state pension amounts should not be added together to gain a median total pension amount.

The chart appears to indicate that the value and widespread coverage of defined contribution incomes for younger generations is replacing the value of defined benefit incomes in older generations. More detailed analysis of the data suggests that over time increasing numbers of pensioners have some defined contribution income from their workplace pension. In the future more people receive a private pension income, but the average pension in payment is relatively lower compared to current levels, which are higher for those who have access to a defined benefit scheme.

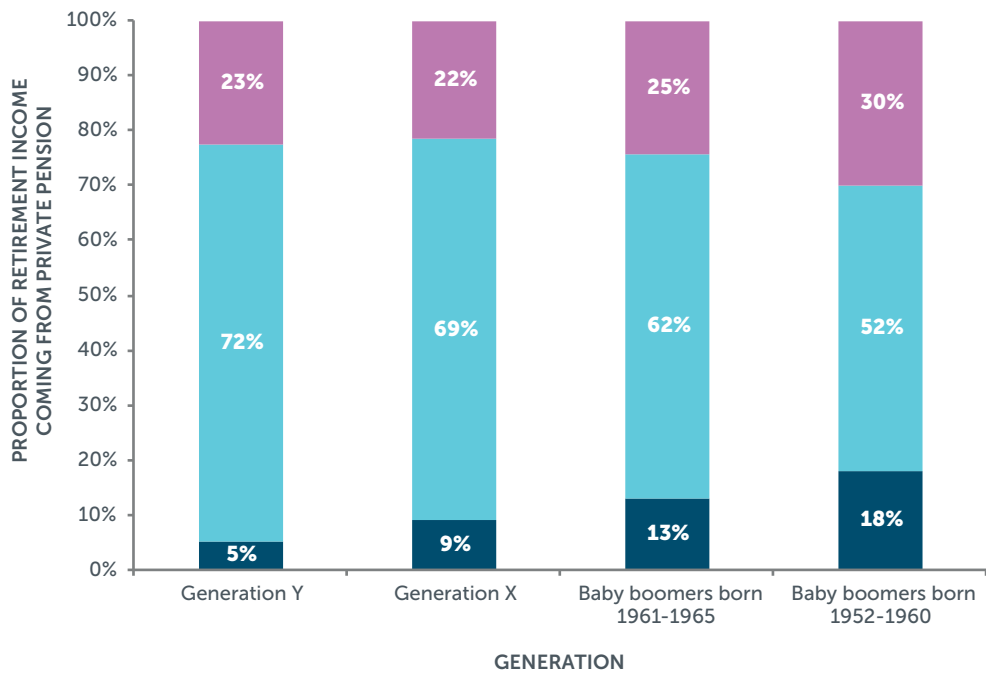
The proportion of people without a private pension in retirement is projected to fall over time. As an example, 95% of those in generation Y are projected to have a private pension income in retirement because of automatic enrolment take-up.

When attempting to compare generational outcomes, it is important to consider not only monetary values but also to what extent individuals are likely to be reliant on their State Pension. Looking at the chart below, the proportion of people with at least 50% of their total pension income coming from private pension is projected to increase between Generations X and Y. However, only around a quarter of Generation Y (equivalent to around 3.9m people) have at least 50% of their total pension income coming from private pension. This is still lower than that of the baby boomer generation (projected to be 28%), reinforcing the value of defined benefit schemes to past generations.

The number of people who will receive income from defined benefit schemes is projected to fall from the baby boomer generation levels. Between Generations X and Y, the proportion of people receiving any defined benefit income is expected to fall from 66% to 39%. At the same time, there is an increasing proportion within each generation receiving income from defined contribution schemes (83% in Generation X up to 91% in Generation Y).

The following chart breaks the figures down further by generation:

Figure 9: Projected proportion of income in 1st year of retirement coming from private pension, by generation



● No Private pension ● Less than 50% ● 50% and over

Source: PENSIM2

The charts reiterate the point made above that private pension income will, over time, cover more people, but with declining access to more generous defined benefit pension income. Many commentators make the point that the 8% statutory minimum investment in automatically enrolled pensions is not enough to deliver people the pension income they aspire to, and some commentators expect a shift upwards of savings levels. However, the prospects for some in the disadvantaged groups discussed in chapter 4 are likely to be limited because of affordability.

Some of the representations which we have received also look at the wider economy in determining fairness, especially across generations. For instance, some look at the distribution of wealth and assets, particularly housing wealth.

Housing costs, and how these have changed and may change over the next 20 years, may affect the adequacy of individuals' pension outcomes. The English Housing Survey shows that the age of first time buyers increased over the past 20 years²⁷. In particular:

- The average age of first time buyers increased from 30 to 33 over the past 20 years. In 2014-15, the majority of first time buyers were aged 25-34 years (61%), similar to 1994-95.

²⁷ Department for Communities and Local Government, 2016, English Housing Survey First Time Buyers and Potential Home Owners Report 2014-15

- Between 1994-95 and 2014-15, the proportion of first time buyers aged 16-24 years declined from 23% to 10%, while the proportion aged 35-44 years increased from 11% to 20%.

We have seen a move to extend mortgages for customers until their 70s or even 80s by a number of high-street banks, so it appears that this trend is not likely to be a temporary occurrence.

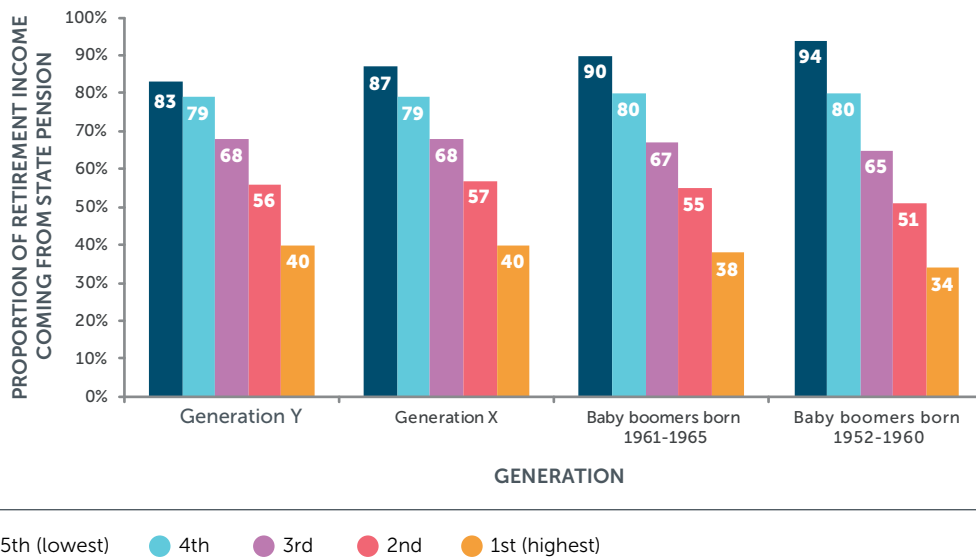
Question:

Are there any other issues around the opportunity to achieve adequacy for future generations that we need to consider? How can we best take into account wider economic impacts, for example, the likelihood of low interest rates in pension outcomes or the changes in housing costs and overall wealth distribution?

The value of the state pension to each generation

In considering intergenerational fairness, we also want to understand the value that the State Pension has for all generations of pensioners. The chart below uses PENSIM2²⁸ to estimate the mean average value of the state pension by income quintile²⁹ as a proportion of overall pension income for each generation.

Figure 10: Projected proportion of income in 1st year of retirement coming from State Pension, by generation and income quintile in 1st year of retirement



Source: PENSIM2

²⁸ PENSIM2 is a micro-simulation model which allows us to project forward using current pension’s policy, to estimate future pensioner incomes, based on modelled private pension savings and coverage.

²⁹ Income quintile defined by sorting the population by total pension income, then dividing into five equally sized groups.

In the lowest income quintile, the State Pension makes up the vast majority of a person’s total pension income (over 80%), though this reliance is decreasing with each successive generation (due to the introduction of automatic enrolment).

In the top two income quintiles, the lessening effect over time of higher value defined benefit schemes can be seen, as the State Pension makes up a greater proportion of total pension income for those in Generations X and Y (when compared to Baby Boomers).

Question:

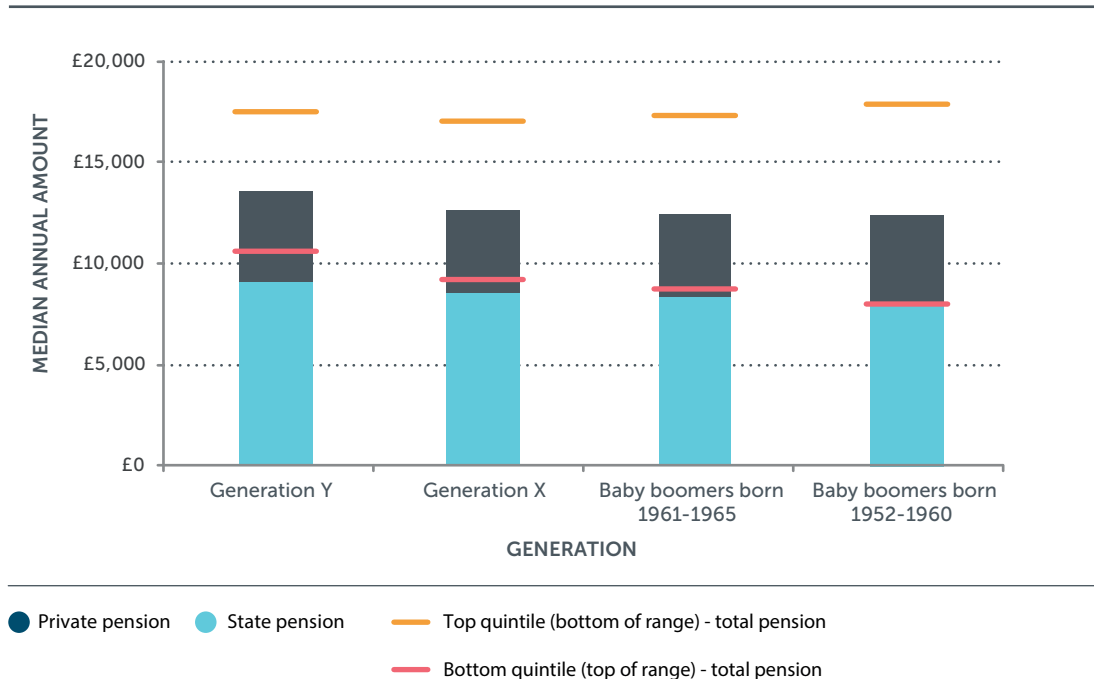
Are there any other factors that may impact the value of the State Pension for each generation?

Intragenerational adequacy outcomes

Turning to fairness within generations, there can be wide variation in individual pension outcomes which will affect the adequacy of individuals’ retirement income. To fully assess whether any changes are fair, we want to take into account the barriers to adequacy faced by specific groups within the future pensioner cohorts and assess whether these groups will have to shoulder a disproportionate impact from any State Pension age change.

On this measure of income pensioner income inequality is forecast to continue to reduce over time, as seen in the chart below.

Figure 11: Projected median average amounts of State Pension and private pension in 1st year of retirement (also shows upper and lower quintile amounts of projected total pension income), by generation



Source: PENSIM2

In terms of pension outcomes, the analysis here shows that income inequality is narrowing across the pensioner income distribution and that this continues across the generations. This is likely to be due to the flattening in value of the new State Pension. It also shows that workplace pension saving will increasingly give more people on average more pension in retirement, as opposed to a higher defined benefit income for a narrower range of people in the current pensioner generation.

The information here reflects our general findings across Chapter 2 – that the levelling and broadening of the new State Pension delivers a foundation income for Generation X and Y, but that the withdrawal of defined benefit membership, and with it a significant amount of employer subsidy, means that future generations are unlikely to see overall pension outcomes to equal the Baby Boomers.

Our initial analysis of private savings suggests significant reliance on the State Pension as a proportion of retirement income, especially for low earners.

If we work through some simple case studies using the DWP iPen model: low earners, with full or interrupted working lives, get less private saving as a proportion of overall income than other groups. For example, Generation X low earning women receive only 4% of their total income from private pensions (£8 a week after 34 years of saving into a private pension) while Baby Boomers receive around 2% (£3 a week after 16 years of private pension saving). This increases to 6% of overall income for Generation Y (£12 a week after 46 years of saving into a private pension). Generation X low earning females who spend some 35% of their working lives caring will derive less than 2% of their pension income from private saving.

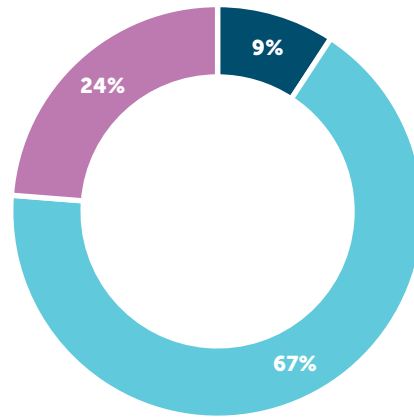
Median earners receive a far higher proportion of their income from private pensions. A Generation X man receives 32% of his pension from private pension compared to the 4% proportion received by a low earning woman of the same age. A Generation Y man, with lower private provision because of the increasing withdrawal of defined benefit coverage, still receives nearly 30% of his income from private provision compared to a woman of the same age on low earnings who sees 6% of her income from private provision. Even if a Generation X median earning man withdrew from private saving at age 50, he would still receive almost 23% of his pension from his private scheme.

Private pensions for low paid workers can only be a small proportion of overall pension outcomes because they have less to invest. However, in contrast the replacement rates of low earners are comparatively high. The iPEN examples show Generation X low earners achieve replacement rates of 130%, Baby Boomers 117% and Generation Y women see replacement rates of over 145% of last earnings. These replacement rates reflect the fact that most workers receive the full rate of the new State Pension (including the benefits of the triple lock) and that most had low working age incomes.

These case studies help explain the projected picture for the whole population. The chart below looks at the projected percentage of total pension income which comes from private pension in the first year of retirement across all current working age people. Note that this analysis looks at income in the first year of retirement, so this will exclude people who

accrued rights to a private pension which they then converted into a lump sum payment:

Figure 12: Projected proportion of income in 1st year of retirement coming from Private Pension



● No private pension ● Less than 50% ● 50% and over

Source: PENSIM2

3.4m (9%)

are projected to have no private pension income

25.0m (67%)

are projected to have less than 50% of their total pension income coming from private pension

8.9m (24%)

are projected to have at least 50% of their total pension income coming from private pension

On average across all generations, just over a third of a person's total pension is made up of private pension. This figure is fairly static across each generation, and shows significant reliance on the State Pension as a source of income.

Looking to the future we see a projected increase in median pension outcomes and a reduction of pension income inequality. As discussed above, more people in lower income brackets can (and are expected to) access private pension savings, while people in higher income brackets see a reduction in private incomes due to the withdrawal of defined benefit schemes. In addition, there has been a narrowing between working age and pensioner incomes in recent years.

In looking at fairness, we need to consider what impact any State Pension age changes would have on different groups. We also need to consider whether our current methods of measuring fairness are still appropriate in a changing labour and housing market.

We discuss the potential impact of State Pension age changes on specific impacted groups in more detail in Chapter 4.

Measuring Adequacy

The Pensions Commission used a tool that is most commonly used and most widely recognised for measuring adequacy for current pensioners. This is based on Replacement Rates that compare an individual’s retirement income against their average earnings in the last decade prior to retirement. The Commission then recommended different replacement rates for different earnings bands.

2016/17 income band Target replacement rate	Target replacement rate
Up to £12,600	80%
£12,600-£23,300	70%
£23,300-£33,200	67%
£33,200-£53,200	60%
Over £53,200	50%

30

However, in looking at the relevance of Replacement Rates for pensions policy in the future, a number of issues arise:

- Pension Flexibilities: Is it possible to accurately measure the income likely to be generated by a Defined Contribution pension pot when annuities are no longer obligatory?
- Costs in Retirement: The Replacement Rates assume that certain costs will no longer be relevant in retirement, such as housing costs or the care of children, and that is how pensioners can scale down their earnings without compromising their household wealth. However, there are increasing suggestions that mortgages and responsibility for children will apply until much later in life for future generations. Is the suggested reduction of income in retirement still a good measure of adequacy when these costs are likely to decrease less proportionately than in the past?
- Changing retirement behaviours: using the decade preceding the retirement point as part of the adequacy measure implies that retirement will continue to be treated as a fixed point in time. In the future we may need to disengage more slowly from the labour market so defining pre-retirement income might become more difficult. We may also see different approaches to retirement where more people return to work (for example after a period of caring) around retirement or even post-retirement.

30 Department for Work and Pensions, 2012, Estimates of the number of people facing inadequate retirement incomes, DWP

There are some alternative suggestions to replacement rates as a way of measuring pensions policies. Some research suggests a range of incomes that are linked to achieving happiness in retirement. Other approaches suggest an overall size of pension pot as a measure for retirement. We are keen to understand better how adequacy should be measured for people retiring post-2028.

Question:

Are replacement rates linked to pre-retirement income a good measure of adequacy for the future? What would be the most relevant alternatives?



Fuller Working Lives

Introduction

The labour market affects what happens to individuals' pensions in several ways. Most qualification for State Pension is through National Insurance contributions which are linked to earnings; the type of employment affects the type of private or occupational pension available to an individual; while the level of pay affects how much people feel they can afford to save, and what kind of income they might look to achieve in retirement. National Insurance credits are in place as a contingency when people cannot work.

As discussed in Chapter 1 on the economics of pensions, people working today contribute to State Pension current payments through their National Insurance contributions, and provide the goods and services that pensioners buy with their pensions. Since older people make up a large and increasing share of the population, their decisions on when to retire and whether to take on responsibilities such as caring can have a significant impact on their personal circumstances, as well as to the pension system and wider economy as a whole.

The labour market can influence how people respond to changes in State Pension age. In some circumstances the opportunity to remain or re-enter employment might not be available. If people do keep working it might need to be in a different job and/or a different working pattern.

Looking at the UK labour market now, the overall (age 16-64) employment rate reached a record 73.5% in summer 2016. However, it is worth noting that even Generation Y has already experienced one recession and the younger Baby Boomers have been participating in the labour market through at least three major recessions.

The position of Older Workers

The UK, alongside most developed countries, has an ageing population.

Between 2014 and 2028, the number of people aged between 16 and 49 will rise by 0.5m while the number of people aged between 50 to 67 (SPa) will rise by 1.2 million. By the mid-2030s, people aged over 50 will comprise half the adult population in the UK.³¹

Figures for 2016 (Apr-Jun) show that there are currently 9.8 million workers aged over 50. This represents an increase of 1.4 million over the last 5 years, and an increase of over 2.0 million over the last 10 years. Both the number of people in work and the employment rate of men and women above State Pension age has increased over the past years. There are currently 1.2 million people – 742,000 men and 465,000 women - aged 65+ who are in employment: 14.2% and 7.5% of male and female 65+ population³². This is more than double the rate seen around the turn of the century respectively.

So older people are already playing an increasingly significant role in the labour market. Enabling older workers to remain in or return to the workforce is important as it allows people to supplement or top up their pensions, and manage the transition to retirement. The opposite to this, taking early retirement, can have a significant impact on people's income. Analysis of the English Longitudinal Study of Ageing suggests that around a third of people who stopped work between the age of 50 and State Pension age between 2008 and 2010 saw their household income drop by more than half.³³

Estimates by the National Institute for Economic and Social Research, show that adding 1 year to working lives could increase GDP by 1% per year after 5 years, and adding 3 years would increase GDP by 3.25% per year by the early 2030s³⁴. What this means in practice is that people working longer boosts the whole economy as well as their own financial situation, and this in turn can help make the state pension system more sustainable.

The trends in this area are positive, with a consistent increase in labour market participation for workers over 50 in the last two decades for both men and women. It should be noted however, that employment rates for older men are still lower than in the 1970s -80% of men aged 60–64 were in paid work in 1968, compared to just 43% in 1993³⁵. There are also other countries (such as Sweden and Canada) with higher employment rates for older workers than the UK. It is also worth noting that younger generations appear to start work later overall than their preceding generations. The participation rates by age are provided in the Figure 13.

31 Department for Work and Pensions, 2014 Fuller Working Lives: a framework for action

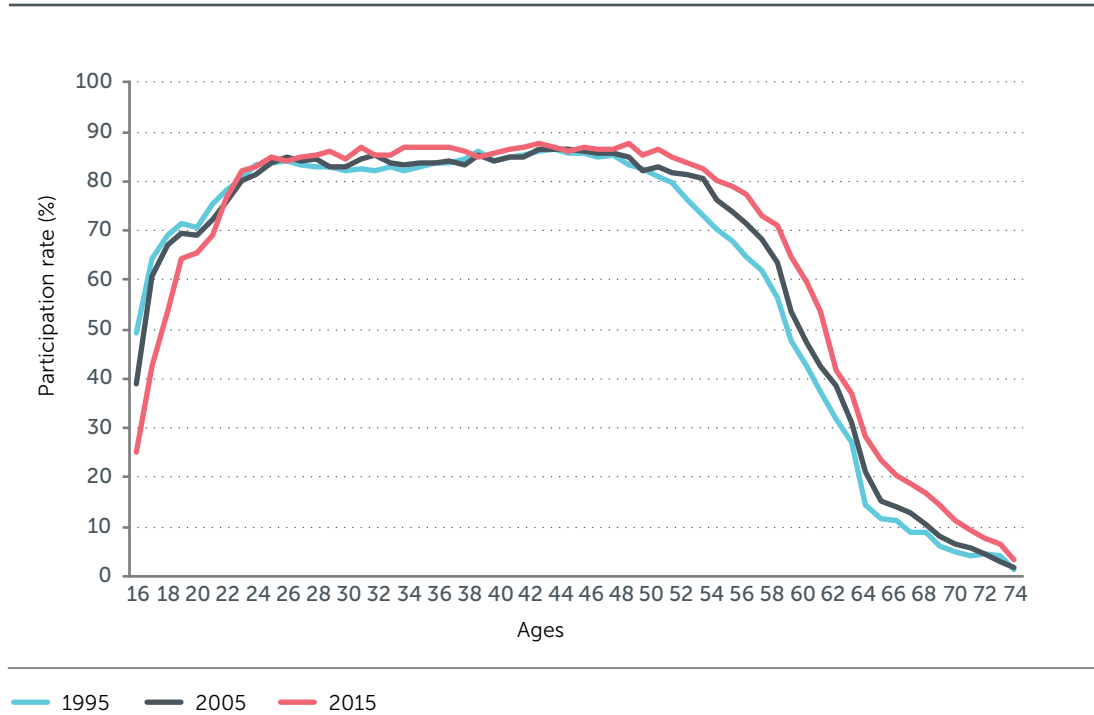
32 ONS August 2016 Labour Market Statistics 2nd Quarter (April-June) 2016

33 Department for Work and Pensions, 2014, Fuller working lives – background evidence, DWP

34 Department for Work and Pensions, 2011, The macroeconomic impact from extending working lives Working Paper No. 95

35 D. Chandler, G. Tetlow 2014 Retirement in the 21st Century, IFS

Figure 13: Labour market participation rates (%) of people by individual age (4th quarter average 1995, 2005, 2015)



Source: ONS Data from Labour Force Survey

Older workers have also been closing the gap in employment rates with young workers. The employment rate gap between people aged 50 – 64 and those aged 25 – 49 has decreased in the last twenty years from 20.5 percentage points in 1995 (25 – 49 employment rate of 77.7%, 50 – 64 employment rate of 57.2%) to 12.9 percentage points in 2015 (25 – 49 employment rate of 82.3%, 50 – 64 employment rate of 69.4%)³⁶.

The participation rate for women has also been positive. Between 1995 and 2015, the largest absolute increases in participation and employment came from women aged 55 – 59 and 60 – 64 (those women approaching and passing State Pension age). In the last 20 years, employment of women aged 55 – 59 rose from 52.5% to 68.8% in 2015, up 16.3 percentage points. For women aged 60 – 64 employment rates rose from 25.2% to 40.2% in 2015, mainly driven by the recent equalisation process of State Pension age. For men, the largest increase was for those aged 60 – 64 from 45.5% in 1995 to 58.5% in 2015³⁷.

³⁶ Department for Work and Pension, 2016, Economic Labour Market Status of Individuals Aged 50 and Over Since 1984: Data for 1984 to 2015. Participation rate includes those in employment and ILO unemployed.

³⁷ See above

Flexibility in employment is a key characteristic of the employment patterns of older workers. As an example, self-employment has historically been dominated by older age groups. Similarly, while part-time employment is dominated by women, there is an increasing proportion of men working part-time. In 2015, of people aged over 50, 4.137 million men were in full-time employment compared with 2.258 million women. However, the proportion of men in part-time employment has increased overall and especially for those aged 60-64 since 1995 (7.7% in 1995 vs. 13.9% in 2015)³⁸.

On an individual level, the increase in employment rate is mainly associated with factors such as education, socio-economic class, health, household type and region. In particular men and women aged 50+ are more likely to be employed if they still have a mortgage, dependent children (for men), have a degree or equivalent compared to no qualifications, or report a very good or good health status.

Of those working past State Pension age, further work by the ONS for the Review shows that 25% of men and 32% of women report a financial reason for doing so (such as boosting a pension pot, or the purchase of necessary or desirable goods). The largest single reason was that they are “not ready to stop work”. We will need to unpick this rather broad response in the course of the review.

We know from analysis by the IFS³⁹ that changing State Pension age for women so far has an impact on people’s decisions as individuals as part of a household, with both men and women staying longer in the labour market as a result. It will be important to monitor level of response for older age groups as State Pension age rises to 67 by 2028.

Triggers for early exit from the labour market

Some people may be able to achieve a financially stable retirement ahead of State Pension age; but ill health, difficulty in returning to work after redundancy and caring responsibilities stand amongst the main reasons why people choose to leave the workforce before State Pension age, whether permanently or not.

Analysis conducted by the ONS using Annual Population survey data for March – April 2016, shows that the most common reason why people leave work before State Pension age, is taking early retirement (27.6%), followed by health reasons (25.7%). The graph below illustrates the position

³⁸ See above

³⁹ J. Cribb et al, 2014, Labour supply effects of increasing the female state pension age in the UK from age 60 to 62, IFS Working Paper (W14/19)

Figure 14: Reasons for leaving last job before State Pension age (people aged 50 – Spa)(%)



Source: ONS data from Annual Population Survey, March – April 2016

Similar evidence from the Wealth and Assets survey 2012-14 indicate that retirement before pensionable age due to ill health stands as the key driver of early retirement, followed by being offered reasonable terms to take voluntary or early redundancy.



“Nearly half of people leave the workplace by State Pension age, many a long time before. This is often due to illness or disability, particularly for those in manual occupations.”

TUC Submission to the Review



As a supplement to the above, analysis from the NatCen’s British Social Attitudes Survey, looking at people (of all ages) who were already retired, concludes that:

39%

of retired people say that they retired because they wanted to;

20%

retired due to ill health (this was the same for men and women);

11%

retired because of their employer’s policy on retirement age; and

11%

retired due to losing their job/being made redundant/their firm closing down.

Overall, it appears that people who are likely to be more financially secure (eg they are mortgage free or in a professional or managerial occupation) are more likely to retire early compared to their peers. For example, analysis conducted for this Review by the ONS indicates that men and women age 60-64 who are owner-occupiers are more likely to be retired compared with the general population of the same age group (29.1% vs. 21.2% of men, in 2015).

Men age 60-64 with a degree or higher education are more likely to be retired than those with lower qualifications (29.2% of men aged 60 to 64 with higher education vs. 14.6% of men with no qualifications). There is not a clear pattern for women approaching State Pension age. However, past age 65 men and women with a degree or higher education are less likely to be retired and more likely to still be in employment.

It has been suggested to us that the type of profession might also be a significant factor for early retirement, whether it is accompanied by ill health or financial incentives or both. This is often labelled as “burnout” and it is most commonly observed in manual workers (eg in the construction industry), knowledge workers (eg teachers) and perhaps frontline crisis professions (eg ambulance drivers). There may be some professions in these categories where the transition to an alternative career might be more difficult than other professions.

Question:

What evidence is there to suggest “burnout” is a feature of certain professions and what are the alternatives for workers in those roles? How can FWL strategy support best the transition required, if that is the case?

Conclusions

Access to and participation in the labour market for older people is crucial for State Pension age policy. If people disengage from the labour market too early, many will have to live either on private resources (eg drawing down from the private pensions income thus converting an income for life into a short-term financial source of support) or, on working age benefits.

Question:

To what extent can a delay in State Pension age act as a direct mechanism to enable Fuller Working Lives? What factors would increase the likelihood that people remain in gainful employment during any such delay?

03 Life Expectancy





Introduction

In this Chapter we discuss the main determinant in setting State Pension age – Life Expectancy. We describe how Life Expectancy is measured, summarise the latest data and describe how the different socio-economic and lifestyle factors that prevail in various parts of the country can influence Life Expectancy. We also discuss Healthy Life Expectancy.

Life Expectancy has been improving over time – in particular for older people. Since 1970, there has been a rapid decline in mortality rates at older ages, particularly for men. The Cohort Life Expectancy for men born in the UK in 2016 is 90.6 years, and for women 93.5 years.

One of the main drivers of this may be the different historical patterns in cigarette smoking between men and women - peak consumption for men was earlier (1940 to 1960) and higher than for women (around 1960)⁴⁰. Improvements will also have been driven by health care, diet and lifestyle which have risen alongside levels of income and education.

These are projections and not forecasts, and the ONS who has provided us with these projections, has to make assumptions about how mortality rates will change in the future. Information on how mortality rates have changed in the past, is used to estimate the current rate of mortality improvement by age and sex, and to make assumptions about improvements in mortality rates in the future.

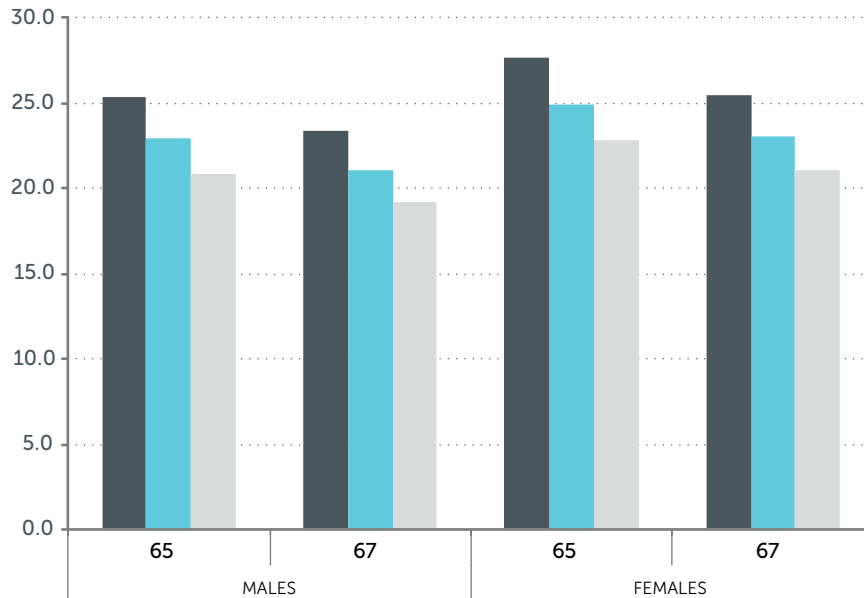
ONS consults a range of demographic and health experts to decide how long historic trends will continue into the future. It is possible (as some demographers argue) that future improvements in mortality rates, will not be as rapid as historic improvements, partly as no more than a minority of the population will adopt a truly healthy lifestyle. External factors, such as the emergence of new diseases, or antibiotic resistance, could also affect future mortality improvements. Alternatively, technological and medical improvements may maintain or increase the rate of improvement⁴¹.

To reflect this uncertainty ONS produces a range of Life Expectancy projections which by their assessment are within the bounds of plausibility: the chart below shows Life Expectancy for someone aged 65 (current State Pension age for men) and 67 (the legislated State Pension age at that time) in 2028 under the ONS “high”, “low” and “Principal” Life Expectancy scenarios.

⁴⁰ ONS, 2016, National Population Projections: 2014-based reference volume, series PP2

⁴¹ See above

Figure 15: Cohort Life Expectancy principal projections and high & low Life Expectancy variants for a person aged 65 & 67 in 2028, UK



● High Life Expectancy ● Principal Life Expectancy ● Low Life Expectancy

Source: ONS 2014 – based Life Expectancy projections

Life Expectancy

How is Life Expectancy measured?

There are two measures of Life Expectancy:

Period Life Expectancy (which estimates how long people live) is based on mortality rates for a fixed point in time, and does not take into account improvements in mortality rates beyond that point. Cohort Life Expectancy includes estimates of expected improvements in life expectancy. The cohort approach, is used by financial companies to determine things like annuity rates and life insurance, and is what will be used to decide on an appropriate State Pension age.

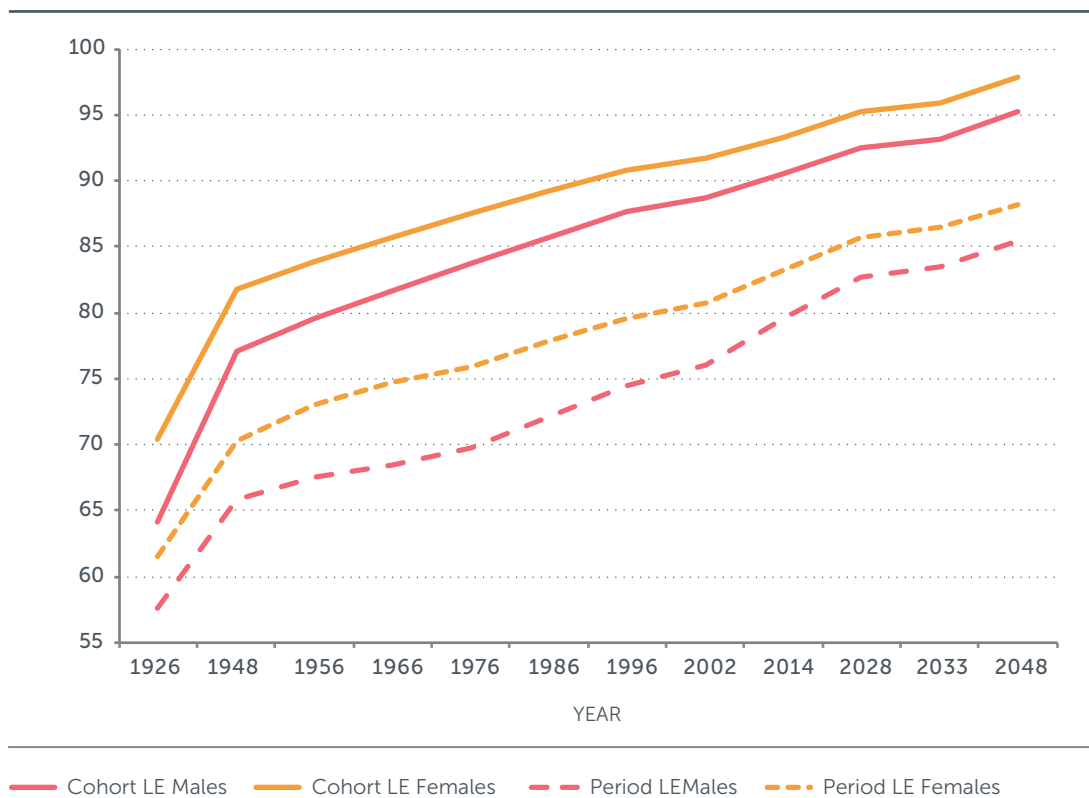
Latest information on Life Expectancy

Cohort Life Expectancy at birth and at 65 has increased since 1926 when the first contributory state pension was introduced. Historic figures for England and Wales show that in 1948, when the basic State Pension was introduced, the Cohort Life Expectancy of a 65 year old man was around 12 years compared with 21.3 in 2014.

The latest set of estimates from the ONS report that women’s Cohort Life Expectancy at age 65 has risen 4.6 years from 18.9 in 1989 to 23.5 in 2014. Men’s Cohort Life Expectancy at age 65 has risen 5.9 years from 15.3 in 1989 to 21.2 in 2014.

These rises are expected to continue: UK Cohort Life Expectancy for men/women at age 65 is projected to rise from 21.5/23.7 in 2016 to 22.9/24.9 in 2028 and 24.8/26.8 in 2046 (when the State Pension age increase to 68 was timetabled in the 2007 Pensions Act).

Figure 16: Period and Cohort Life Expectancy (Males & Females) (1926-2048), England & Wales



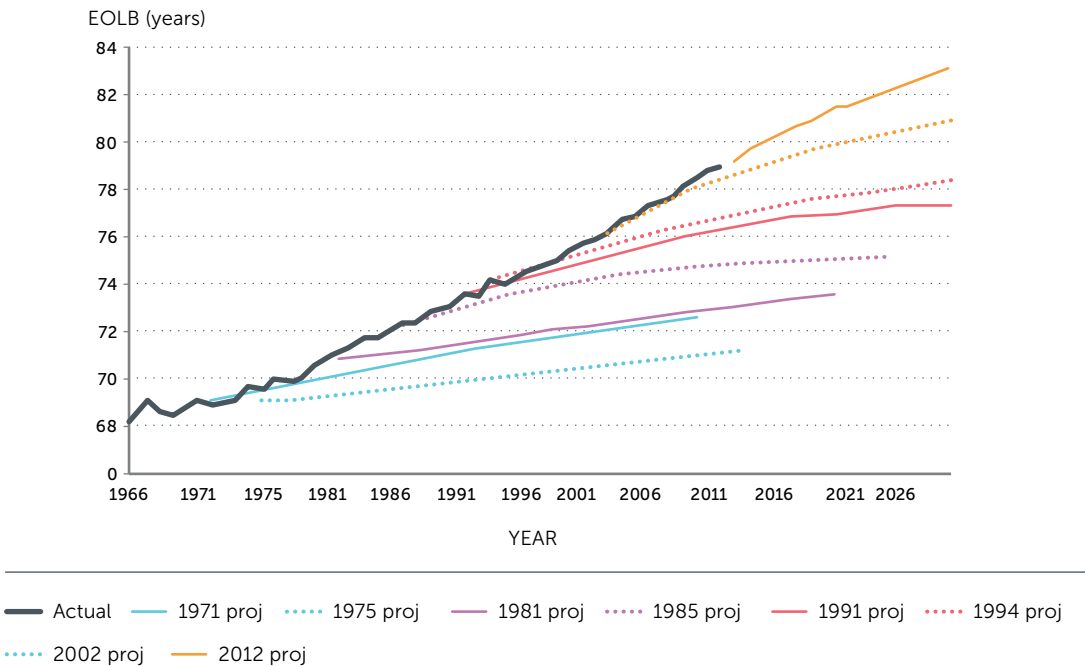
Source: ONS National Life tables 2011-2013 England & Wales

It is important to note that although the gap in Life Expectancy between regions has closed over 1991-2014, there remain substantial differences between and within the regions and nations of the UK, implying that changes to State Pension age will have a varying geographical impact.

Sensitivity of Projections of Life Expectancy at State Pension age

Period Life Expectancy has increased at a fairly steady rate for both men and women over the last 50 years. In the past, projections have consistently assumed that the rate of improvement in Life Expectancy would slow, meaning that Life Expectancy has been consistently underestimated. Projections from the mid-1970s in particular underestimated actual improvements in Life Expectancy. More recent projections have made increasingly optimistic mortality assumptions but have still consistently under-projected Life Expectancy.

Figure 17: Actual and projected period expectation of life at birth males, United Kingdom 1966-2030, selected projections



Source: ONS 2015 National Population Projections Accuracy Report

Although Life Expectancy is still increasing each year, the 2014-based projections show a slower increase in improvements in mortality rates than the 2012-based ones. This is because mortality rates for some ages were higher in 2012 and 2013 than were projected in the 2012-based projections. Based on this finding, the OBR reported that the latest estimates of average Life Expectancy at State Pension age in the UK, imply that State Pension age should rise to 68 by 2041; five years later than estimated on the basis of the 2012 projections.

The above indicates that there is uncertainty: for government, for employers and pension providers and most importantly, for individuals and their families when planning for retirement.

It is unclear whether individuals themselves account for uncertainty over life expectancy (and therefore State Pension age) when planning for later life. The implications of longer living introduce new considerations for people; such as when to retire, the likelihood of being a carer (or needing care) and how best to utilise their private savings (against a background of the decline in defined benefit pension coverage).

Question:

How can we best take into account the sensitivity of the Life Expectancy projections when considering an appropriate State Pension age for the future?

Relevant factors in Life Expectancy

a. Geographical Differences in Life Expectancy

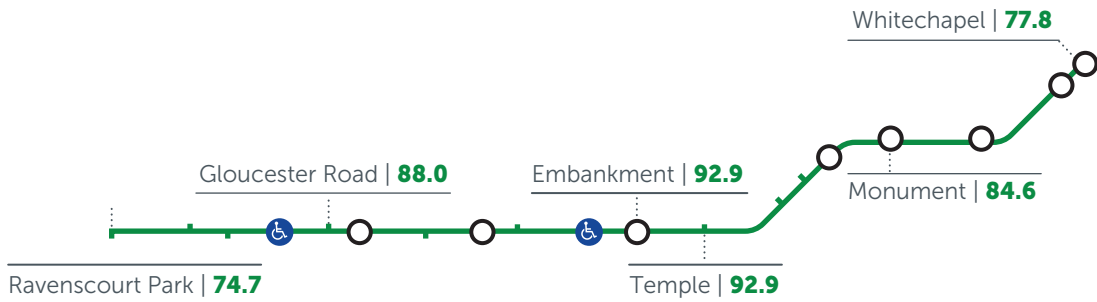
We have had several representations from stakeholders suggesting that regional differences in Life Expectancy will significantly affect the impact of changes to State Pension age, particularly looking at the constituent nations of the UK.

ONS produces “Period” Life Expectancy estimates (using existing mortality rates by age, rather than projecting further changes) at regional and local authority level. While these suggest that there are variations amongst the UK’s constituent countries and English regions, they also suggest that significant disparities exist even at a more local level.

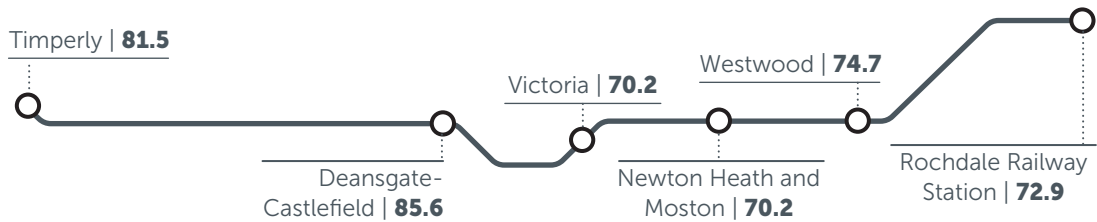
For example, men in Greater Manchester⁴² have a life expectancy at birth that is 2.4 years lower than in Greater London (77.2 vs. 79.6). There is a corresponding difference for women of 2.6 years (81.2 vs. 83.8). However, the variations of life expectancy between different local areas within the areas of Greater London and Greater Manchester are even wider.

The Life Expectancy by public transport maps here illustrate this point.

LONDON | District Line



MANCHESTER | Tram Network



⁴² Life Expectancy estimates for Greater Manchester calculated by the ONS and derived from the aggregation of boroughs that encompass Greater Manchester.

Using ONS life expectancy data⁴³, incorporated into London’s District Line tube and Manchester’s Tram Network maps, we capture the extent of variation from cross-sections of the two transport systems.

In London, if you travel from the Temple and Embankment tube stations in Westminster to Ravenscourt Park station in Hammersmith there is a fall of more than 18 (92.9 to 74.7) years in life expectancy at birth for men. In Manchester, if you take the tram from Deansgate - Castlefield to Victoria there is a drop of around 15 years (85.6 to 70.2) in men’s life expectancy at birth. So it appears that life expectancy inequalities within Greater London and Greater Manchester are significantly higher than inequality between the two city regions.

An alternative measure is to look at Life Expectancy by splitting up the population by area measure of social deprivation in a given area. This is based on “neighbourhoods” of roughly the same population (so 10% of neighbourhoods is roughly 10% of the population) ranked by a range of measures which determine relative deprivation.

ONS analysis from the census data shows that while there are differences between the nations of the UK, the differences within those nations are larger. The table below, shows Life Expectancy across the UK nations, and the difference between the top 10% least and top 10% most deprived areas. The difference between Life Expectancy at age 65 for men was less than a year between England and Wales, but within Wales there is a difference of 4.4 years between the top and bottom decile of area deprivation.

Table 1: Life Expectancy at 65 overall, and by national deciles of area deprivation, 2010-12

	LE (years)	Least deprived	Most deprived	Difference	
Males	England	18.4	20.4	15.7	4.8
	Wales	17.9	19.9	15.5	4.4
	Scotland	17.1	19.8	14.1	5.6
	Northern Ireland	17.8	19.4	17.1	2.3
Females	England	20.9	22.8	18.6	4.2
	Wales	20.5	22.6	17.9	4.7
	Scotland	19.4	21.9	16.9	5.0
	Northern Ireland	20.5	21.3	19.7	1.6

Source: ONS, 2016, Health state Life Expectancy (general health) and Life Expectancy, 2010-12

⁴³ ONS, 2015, Life Expectancy at birth by Sex for Middle Layer Super Output Areas (MSOAs) in England, 2009-2013

⁴⁴ ONS 2015 Trend in life expectancy at birth and at age 65 by socioeconomic position based on the National Statistics Socio-economic Classification, England and Wales, 1982—1986 to 2007—2011.

Differences in the spread of socio-economic groups (occupations) across the country may explain some regional differences. The National Statistics Socio-economic Classification (NS-SEC) distribution is not uniform across the country. ONS also find that areas with higher Life Expectancy (or Healthy Life Expectancy) have a higher proportion of people in advantaged socio-economic groups and areas with lower Life Expectancy (or healthy life expectancy) have a higher proportion of people in disadvantaged socio-economic groups in comparison to overall average across England.

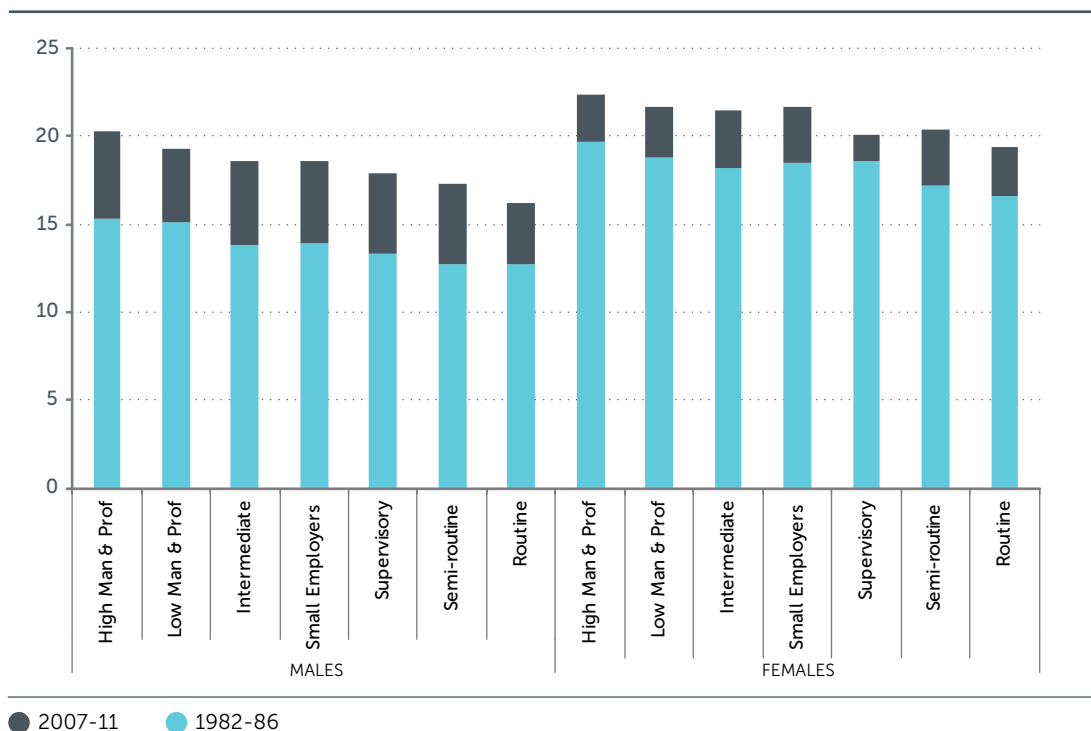
As measured by each country’s index of deprivation, a man in the most deprived decile of England will have a Life Expectancy which is 3.7 years lower than a man in the least deprived decile in Northern Ireland. However, the extent of relative deprivation exposure of these two populations may not be comparable.

The data above suggests that regional differences cannot be considered in isolation. Building on this, there is a range of evidence to suggest that socio-economic factors are a key driver of geographical disparities in life expectancy⁴⁴. The next part of the chapter looks at how life expectancy varies for different socio-economic groups.

b. Socio economic group [Period]

ONS can also look at period Life Expectancy by socio-economic group which is broadly described as people’s occupation. This measure incorporates a number of factors - whether a person’s job is physically demanding or risky and with health implications, but is also a broad measure of their income and education levels. Life expectancy has increased in the past across all socio-economic groups, although not evenly, and there are still differences.

Figure 18: Changes in period Life Expectancy at age 65 by occupational group between 1982-86 and 2007-11 (Male and female).



Source: ONS 2015, Trends in Life Expectancy at birth and at age 65 by socio-economic position based on the National Statistics Socio-economic Classification, England and Wales: 1982—1986 to 2007—2011

Period life expectancy has risen for both genders and all socio-economic groups - ONS use people's occupation to assign socio-economic groups.

For men, groups ranging from the semi-routine to managerial and professional class saw rises in Life Expectancy of between 4-5 years between 1982-6 and 2007-11. The group who had the lowest increase in Life Expectancy at age 65 between 1982-6 and 2007-11 was the routine group for men (just 3.5 years increase) and the supervisory group (an increase of merely 1.4 years) for women. Yet, the group with the lowest Life Expectancy for both women and men is still the routine group (16.4/19.4).

Depending on what measure is used, this could be interpreted as showing inequalities in male Life Expectancy have worsened or improved – the group with the lowest Life Expectancy has seen the smallest improvement, but other groups (eg in semi-routine occupations with lower Life Expectancy) saw equal or better improvements than the top groups. For women it does appear as though groups with higher Life Expectancy have seen larger improvements in their Life Expectancy.

Question:

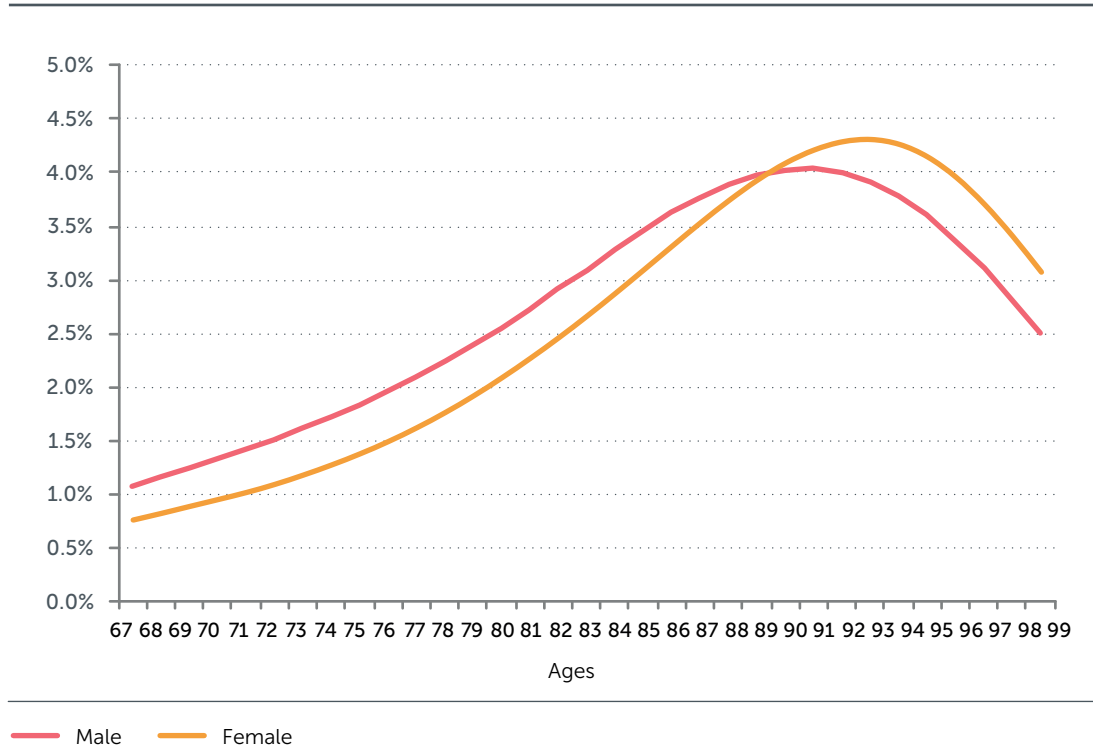
Do you think that regional factors have an impact on Life Expectancy and how? How should the Government factor in the combination of regional and socio-economic factors?

Life Expectancy of generations covered in this Review

As we explained in Chapter 1 there are three key generations this Review is considering: Baby Boomers (born between 1945 and 1965), Generation X (born between 1966 and 1979) and Generation Y (born between 1980 and 2000). Analysis of ONS projections shows that for a man born in 1961 who will have survived to reach 67 in 2028, the mean life expectancy at 67 is 88 years, the median is almost 89 years and the mode is 91 years. Similarly for a woman born in 1961 who will have reached 67 by 2028, the mean Life Expectancy at this age is 90 years, the median is 91 years and the mode is 93 years.

Looking at the distribution of Life Expectancy, of those people reaching age 67 in 2028 around 9 in 10 women will live beyond 77 while 9 in 10 men are expected to live beyond 74; while 1 in 10 men and 1 in 7 women can expect to live to 100.

Figure 19: Distribution of Life Expectancy: Probability of death by year of age for a person who reaches 67 in 2028



Source: 2014-based National Population Projections Life table template, UK

Healthy Life Expectancy

Introduction

We have frequently heard in the first half of this review, that Healthy Life Expectancy, the number of years people live in good health, should be assessed alongside Life Expectancy when considering State Pension age. The most common question asked in our engagement with stakeholders was if Healthy Life Expectancy was improving at a similar rate to Life Expectancy or whether people live longer periods in poor health and disability.

We have seen evidence that Healthy Life Expectancy has improved almost proportionately to Life Expectancy but there is still a substantial gap in healthy life years across areas within the UK. Gaps are most pronounced between the least and most deprived areas within each constituent country.

What does Healthy Life Expectancy stand for and how is it measured?

Health expectancies add a quality of life dimension to estimates of Life Expectancy by dividing expected lifespan into time spent in different states of health. They are, in part, subjective and, for ONS estimates, based upon the following survey question:

“How is your health in general; would you say it was... very good/ good/fair/bad/very bad?”

This type of self-reported data is comparatively easy to collect (in comparison with actual medical data) – and academic research ((WU et al, 2013)⁴⁵ and (Doiron et al, 2015)⁴⁶) find poor reported health is associated with objective health problems, and are predictive of more serious chronic illnesses.

The 2011 Census enables self-reported health to be linked to how much it limits day to day activity. Of the group aged 65+ reporting fair health, almost 78% reported either no or “a little” activity limitation, compared to only 21% of those reporting “bad” or “very bad” health.

The latest information on Healthy Life Expectancy

Estimates from the 2011 Census show that men born in the UK between 2010 and 2012 could expect to live 63.2 years in “Very good or good” health (or 80.3% of their lives) and women 64.6 years (or 78.2% of their lives) if they experienced the same mortality patterns and rates of good health observed in that period.

If surviving to age 65 and observing the same mortality patterns and rates of good health, men and women could expect to live a further 18.3 years and 20.8 years respectively, of which around half would be in “Very good or good” health (9.1 years and 9.6 years respectively).

Healthy Life Expectancy over time

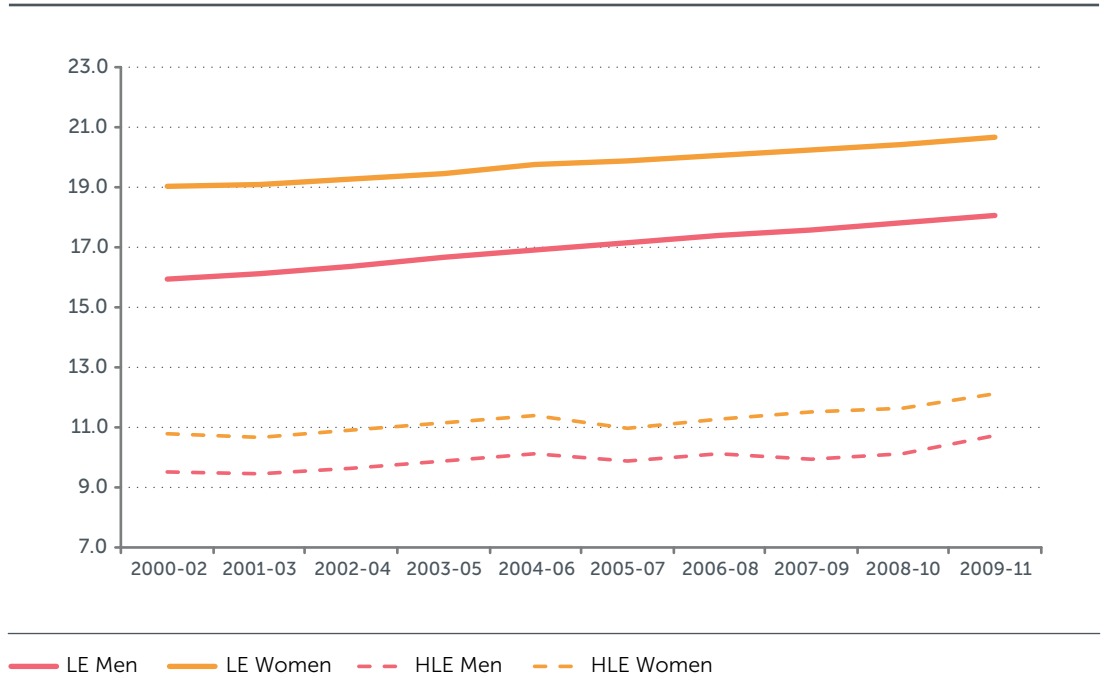
Comparing census data with survey data is problematic because of differences in data collection method and population coverage, which often results in different percentages of people reporting their health as “Good”. Thus, for the purpose of drawing the picture of how Healthy Life Expectancy has changed in relation to Life Expectancy over time we can use the time series based on the General Lifestyle Survey.

While the General Lifestyle Survey has been shown to slightly overestimate good general health compared to the Census, it is useful for tracking Healthy Life Expectancy with Life Expectancy over time.

⁴⁵ Wu et al, 2013, The relationship between self-rated health and objective health status: a population-based study, BMC Public Health

⁴⁶ Doiron et al, 2015, Does self-assessed health measure health, Applied Economics vol.47

Figure 20: Life Expectancy and Healthy Life Expectancy at age 65 for men and women over time, UK (2000-02 to 2009-11)



Source: ONS 2014 General Lifestyle Survey

For both men and women at birth, Healthy Life Expectancy rose over the decade faster than Life Expectancy, suggesting people were living more of their lives in good health. The same is true for women at age 65, but for men, there was no evidence supporting a meaningful increase.

Question:

Are Healthy Life Expectancy and Life Expectancy improving sufficiently for the majority of the population? Are there specific aspects of Healthy Life Expectancy that would directly interact with State Pension age and how?

Other factors to consider when testing Healthy Life Expectancy

Country level Healthy Life Expectancy

Like Life Expectancy, Healthy Life Expectancy varies across the UK constituent countries. Based on observed mortality between 2010 and 2012, at age 65, men in England could expect to live another 9.2 years in “Good” health; 1.2 years higher than Wales, which was the lowest.

Although Scotland has the lowest Life Expectancy of all UK nations, both men and women, between 2010 and 2012, could expect to live the longest in “Good” health (at 9.3 and 10.2 years, respectively). Compared to the UK, this was 0.2 years higher for men and 0.6 years for women. Similarly, when looking at the proportion of life spent in “bad” health, Wales presents by far the highest figure (19.5% for men and 20.1% for women) and Scotland the lowest (13.9% for men and 14.1% for women).

Table 2: Health state Life Expectancies (general health) and Life Expectancy (LE) for men and women at age 65, 2010 to 2012

Men at 65

	LE (years)	“Good” health (years)	“Fair” health (years)	“Bad” health (years)	Proportion of life spent in “Bad” health (%)
England	18.4	9.2	6.4	2.8	15.4
Wales	17.9	8.0	6.4	3.5	19.5
Scotland	17.1	9.3	5.4	2.4	13.9
Northern Ireland	17.8	8.3	7.0	2.5	14.0
United Kingdom	18.3	9.1	6.3	2.8	15.4

Women at 65

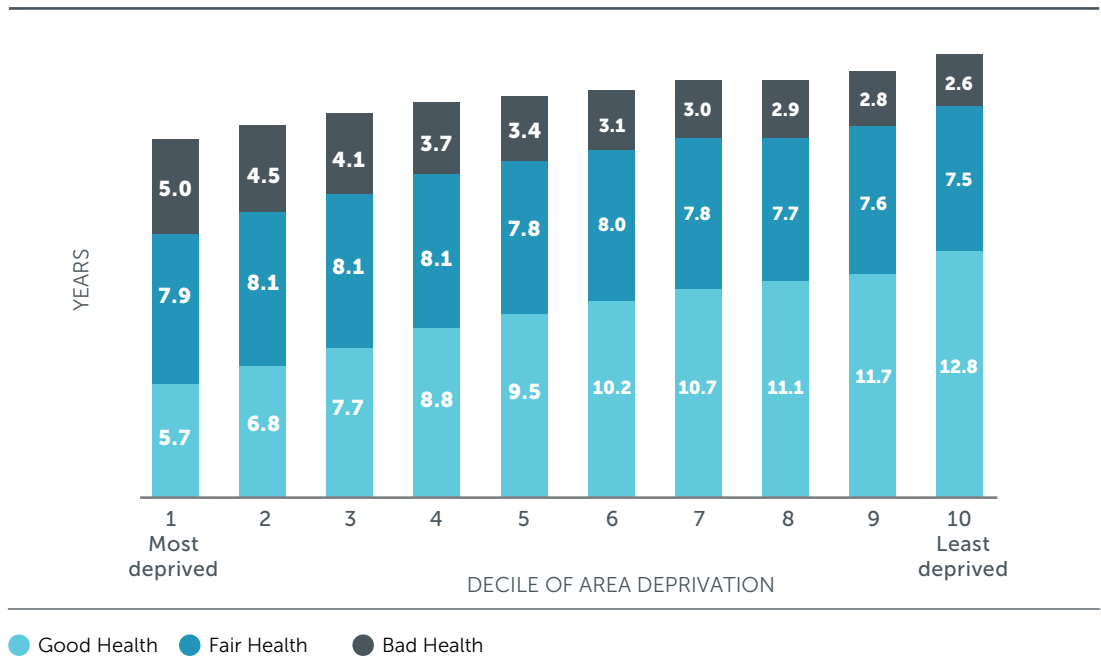
	LE (years)	“Good” health (years)	“Fair” health (years)	“Bad” health (years)	Proportion of life spent in “Bad” health (%)
England	20.9	9.7	7.8	3.4	16.4
Wales	20.5	8.5	7.9	4.1	20.1
Scotland	19.4	10.2	6.5	2.7	14.1
Northern Ireland	20.5	8.7	8.7	3.1	15.2
United Kingdom	20.8	9.6	7.7	3.4	16.4

Source: ONS, 2016, Health state Life Expectancy (general health) and Life Expectancy, 2010-12

Healthy Life Expectancy by Social Deprivation

Similarly, there is evidence of wider variations within nations of the UK than between them when we look at either Local Authority level, or use measures of social deprivation for different neighbourhoods. The chart below shows the position for women in England at age 65:

Figure 21: Health State Life Expectancies for Women at Age 65 by National Deciles of Area Deprivation, England (2010-2012)



Source: ONS 2016 Health state Life Expectancies (general health) and Life Expectancy, 2010 to 2012

Ranking small areas of roughly the same population by relative measures of social deprivation makes it possible to look at how Healthy Life Expectancy varies from the most to least deprived. The least deprived are living longer overall, and spend half the time the most deprived live in bad health.

Lower Life and Healthy Life Expectancy are clearly associated with higher levels of deprivation, and data from the Public Health Outcomes Framework,⁴⁷ shows that high smoking prevalence and larger than average alcohol related hospital admissions, were associated with areas of lower Healthy Life Expectancy, as were lower rates of exercise and dietary factors.

Wider determinant risk factors are also relevant to health status such as the relative skills base of those of working age, support available for accessing the labour market, a buoyant economy and affordable, good quality housing to raise families. It is the synergy between wider determinants and how it influences attitudes to health and manifests in health-related behaviours which largely accounts for these stark contrasts observed.

⁴⁷ Public Health Outcome Framework, www.phoutcomes.info

Conclusions

There are a wide range of views about prospects for future longevity. ONS mortality assumptions are based on expert advice covering a range of factors including biomedical technology, effectiveness of healthcare, behavioural factors, emergence of new diseases, antibiotic resistance etc. For planning purposes the Government has to rely on the best evidence available however, and uncertainty about future Life Expectancy means that there will always be estimating sensitivities associated with the substantial costs of running the state pension system.

In light of what can be sharp differences in Life Expectancy between areas and between certain groups of people, some commentators have suggested that an alternative to a universal State Pension age increasing with Life Expectancy would be to provide people with a State Pension age based on individual circumstances (for example place of birth). In the absence of future estimates of Life Expectancy by groups, such an approach is likely to be impractical and introduce new issues and new unfairness. In Chapter 5, we discuss options which have been presented to us that would allow forms of early retirement for groups with key characteristics which could indicate they have been at a disadvantage during their working life.

The Pension Commission provided another view and recommended that for socio-economic groups with lower Life Expectancy policy should focus on improvements to health and occupational health rather than altering State Pension age itself.

Question:

The Pensions Commission suggested that lower Life Expectancy should be tackled through improvements to health and occupational health. Do you agree? How should we take into account the Life Expectancy and Healthy Life Expectancy information when considering State Pension age?

04 Serious impacts to consider





Introduction

In Chapter 2 we looked at the factors that will formally determine our State Pension age policy recommendations for the future. In this Chapter we consider the impact of changing State Pension age on different groups and systems. We examine the pension outcomes that people will see in the future and the material impact that waiting longer for a state pension will have on those groups. We then identify the dependencies between the State Pension age, the remaining welfare system and private pensions.

In Chapter 2, we discuss our approach to fairness across and within the generations when considering State Pension age. In this Chapter, we examine the impact of changing State Pension age on certain groups. Firstly we look at what their pension outcomes will be in future by providing some case studies showing the impact this has on individuals and then examine the material impact that waiting longer for a state pension has on people's weekly income.

Using the ONS Wealth and Assets Survey (WAS), we can analyse private pension wealth at a household and individual level. We know that private pension and property wealth accumulate over time and tend to increase with age but the data shows disparities between certain groups. On average the self-employed, disabled, women and ethnic groups had less pension wealth, although the self-employed appear to supplement their overall wealth with property wealth to an extent. These groups of people are likely to be amongst those who will rely on the state the most in their retirement. These groups also correspond to the groups identified by the Pensions Policy Institute as being "under-pensioned".

We have identified a similar list of impacted groups based on those characteristics but also on the impact that a delay might have on them, because they may be unable to rely on other wealth or income just before State Pension age. These are:

- Carers
- People with poor health or disability in later life
- Self-employed
- Ethnic Minorities

We examine the impacts on these groups below to assess whether State Pension age changes would affect them disproportionately. We have used case studies to demonstrate the impact specifically for carers. These case studies show the potential impact on pension outcomes for people who have their working lives interrupted in such a way as to restrict their ability to save privately. It also shows how generations are affected in terms of pension incomes, particularly the phasing out of defined benefit schemes and the introduction of automatic enrolment. The case studies also include an assessment of how people's incomes in retirement compare to their incomes before retirement. This provides an insight into the relative value of a pension to someone and the loss they would feel by securing their pension later in life if State Pension age increased.

The examples used to demonstrate the situation for carers are drawn from case studies used by the Pension Commission but take into account recent changes to the pension system such as automatic enrolment.

Carers⁴⁸

Around 1 in 10 adults have some caring responsibilities, and although many people manage to balance work and caring, employment rates are lower than the general population and there is a greater prevalence of part time work (which is on average less well paid)⁴⁹. Some stakeholders suggested that many more people will have caring responsibilities in future as life expectancy increases.

Our initial analysis of what carers might receive in future reflects what we have heard from many stakeholders, namely that they have worse pension outcomes compared to their non-caring peers. The analysis of the estimated gap between carers and non-carers median income in retirement is smaller than other affected groups at around 4% higher for non-carers. On average across all generations, just a third of carers' total pension is made up of private pension, compared to just over a third of non-carers. This is a statistically significant difference.

The recurring issue of private pension accounting for the gap in pension income appears to be the case for carers. This gap occurs because carers are much more likely either to be out of work entirely or have breaks in their work history due to their caring responsibilities. These periods out of work are periods of time not spent building up a private pension, whereas they would receive National Insurance credits towards their State Pensions.

Pension outcomes now and in the future: Some worked examples

iPen is a case study based model which can be used to produce illustrative pension incomes based on a variety of modelled working age incomes and private pension choices. As a result, these iPen cases are worked examples which illustrate the mechanism of the pension system and are not the whole picture⁵⁰.

⁴⁸ A carer is defined as someone who is projected to be caring for someone when they reach State Pension age. They may or may not be in receipt of Carer's Allowance or Carer's credits.

⁴⁹ Department for Work and Pensions, 2016, Family Resources Survey 2016

⁵⁰ iPen is a case study based model which can be used to produce illustrative pension incomes based on a variety of modelled working age incomes and private pension choices

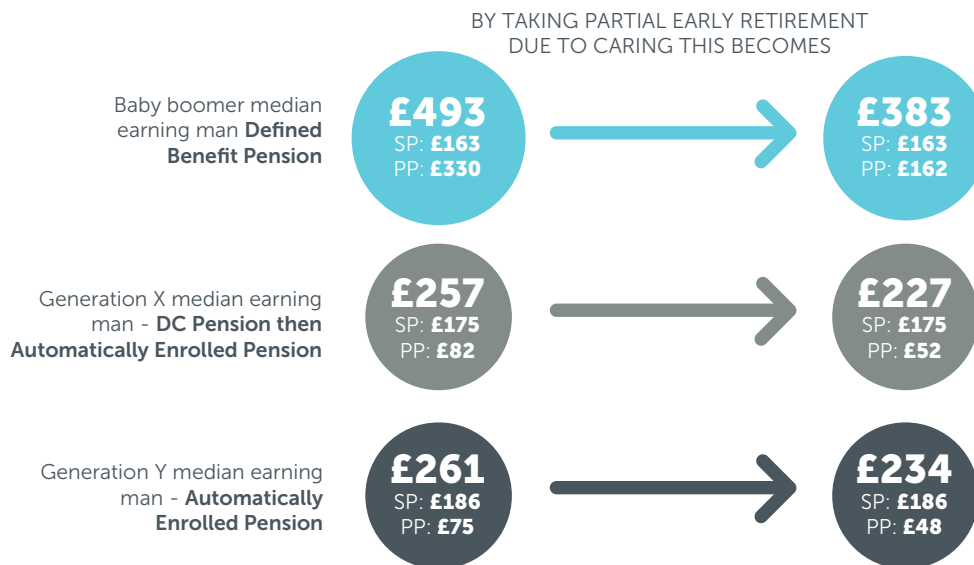
In the iPen output, the modelled retirement income⁵¹ is an average over a person’s total retirement, taking average life expectancy and reducing pension income (relative to earnings) into account. The replacement rate is based on the modelled retirement income expressed as a proportion of working age income received in the final 10 years prior to retirement.

Where a person pays into a defined benefit scheme, an accrual rate of 1/60th of final salary is assumed in iPen. Where a person pays into a defined contribution automatic enrolment scheme, a combined minimum contribution of 8% is assumed in iPen. Given the falling numbers of people in DB schemes we assume that people in Generation X and Y will not be in one – but it should certainly not be assumed that all baby boomers have a DB pension with a complete work history.

Median earning men with caring responsibilities

This example focuses on Generation X man who is a median earner starting work aged 21 and is constantly employed at 100% of median earnings. He has paid into a defined contribution scheme from the age of 21, then changed to an automatic enrolment scheme at the age of 34 (in 2012). He has 47 years in employment and 47 years in defined contribution and automatic enrolment schemes. He will have a weekly income of £257 (£175 from the state and £82 private pension) which will give him a replacement rate of 58.4% of his pre-retirement income.

The following diagram shows what the projected weekly income in retirement would be for each generation and how this is affected by leaving full-time employment and taking a part-time job aged 50 due to caring responsibilities and stopping paying into a private pension scheme.



⁵¹ In terms of retirement income, iPen only counts State Pension and Private Pension (plus any Pension Credit / Housing Benefit for those on very low earnings). Note that none of these iPen examples contain any Pension Credit / Housing Benefit



“Overall the evidence suggests that an increase in the State Pension age can be expected to lead to a prolongation of poverty among older working-age carers, especially when the person being cared for is their partner”

New Policy Institute Submission to the Review



Question:

How can we best take into account the impact of caring responsibilities in later life and specifically within the decade prior to State Pension age?

Health and Disability

In 2014/15, 17% of working age people reported a disability. Predictably this proportion rises with age – 45% of those over State Pension age reported a disability in 2014/15.⁵² Disability, and specifically the age from which a person is affected by a disability, has an impact on people’s employment and therefore also on their retirement income.

Analysis of the wealth and assets survey from the ONS shows a gap of private pension wealth between those with and without a disability - this is true across all age groups. In the future our modeling suggests average pension outcomes will vary between those with disabilities and those without. For non-disabled people, projected median income in the first year of retirement is around 7% higher than for those with disabilities. We propose to use PENSIM to further explore the impact of disability in our final report.

The divergence in pension income for disabled people, as with the gender pension gap, is derived from a discrepancy in private pension. On average across all generations, just under a third of disabled people’s total pension is made up of private pension, compared to just over a third of non-disabled people’s. This is a statistically significant difference.

This reflects the greater challenges some people with disabilities face in the labour market. People who report having a disability on average have lower employment rates and so are less likely to have consistently built up a private pension across the entirety of their working lives.

Those who live with a disability from a young age are particularly affected. The Labour Force Survey shows that younger people with disabilities are more likely to have disabilities associated with very low employment rates, such as mental illness or learning difficulties, making it harder for them to find employment and the opportunity to build up a private pension.

Older people with disabilities tend to acquire physical disabilities later in life, such as problems with their back / neck / other limbs. As they are more likely to have acquired their condition later in life, they may well have been paying into a private pension for several years up until that point.

⁵² Department for Work and Pensions, 2016, Family Resources Survey 2016

Question:

How can we best take into account the impact of poor health and disability in later life and specifically within the decade prior to State Pension age?

Self-Employed

A further group that appears to suffer a disproportionate impact by any State Pension age changes may be the self-employed. PPI evidence shows a downward trend of self-employed people saving into a private pension, which would suggest that this group could become over-reliant on the State Pension in retirement.

In 2013, 22% of self-employed men were saving in a private pension, a drop of 40% over 16 years.⁵³ The low rate of saving can be partly explained by the fact that most self-employed people are not subject to automatic enrolment and so have to proactively decide to save into a private pension. Further, many choose not to do so due to the greater insecurity of stable income in self-employment. We have heard from some self-employed groups that saving into a pension, where the money is then inaccessible, feels too risky. They prefer to save into assets such as property which they feel they can be access at any time if there is the financial need.

It is important to recognise the range of experiences for the self-employed as a group, which can encompass a broad range of professions and incomes, including for example household cleaners and owners of large companies. It is also important to note that the self-employed will receive a boost in state pension with the introduction of new State Pension (self-employed earners were not covered in additional State Pension). That said, there is a significant variation of retirement and saving experiences in this group and we are keen to hear any evidence surrounding the self-employed and their pension outcomes, as well as how we can accurately reflect the different experiences of this diverse group.

We are also keen to gain further evidence about the future size and shape of this group. Our initial analysis suggests that over the longer term, self-employment makes up a similar proportion of employment in 2015 as it did in 1995.⁵⁴

Taking the 2008 to 2015 period as a whole, the level of self-employment increased by around 730,000: from 3.8 million to 4.5 million. Of this increase, around half was accounted for by full-time self-employment, and around half was accounted for by part-time self-employment. Taking the 2001 to 2015 period as a whole -when the level of self-employment increased from 3.2 million to 4.5 million – roughly half of the increase was accounted for by full-time, and around half by part-time self-employment. Part-time self-employment has played an important role in raising the prevalence of self-employment as a whole. The number of workers in this mode of employment grew by 88% between 2001 and 2015 – compared with 25% for full-time self-employment. We would like to understand if this trend of increasing self-employment is set to continue and if so, what impact it might have on pensions in 2028 and beyond.

⁵³ PPI, The Underpensioned 2016, p10

⁵⁴ Office of National Statistics, 2016, Trends in self – employment in the UK: 2001 – 2015

Question:

How would any State Pension age changes affect the self-employed in the future? How can we take into account the very diverse profiles in this group?

Ethnic Minorities

We have seen some indication that due to impacts from State Pension age changes BAME groups should also be considered specifically as part of our Review. Research from the Joseph Rowntree Foundation highlights many of the multiple disadvantages BAME groups face. For instance, Pakistani, Bangladeshi, Black African, and Black Caribbean groups are the most likely to be in persistent poverty.⁵⁴ Furthermore, there is evidence that there are ethnic inequalities in the labour market;



“the overwhelming picture is one of continuing ethnic minority disadvantage compared with the White British majority group”.⁵⁵

Joseph Rowntree Foundation



We can expect that across their working lives those from ethnic minority groups on average can expect to earn less or have more employment gaps than their White British counterparts. As we have seen with other disadvantaged groups, this would likely therefore also play into any potential private pension savings they might expect to make.

We have also seen evidence from the PPI that ethnic minority groups currently derive a lower state pension compared to other pensioner groups. Their analysis suggests that Asian/Asian British/Chinese households receive around 22% less than the average of the pensioner’s population and around 25% less than pensioners from the majority white population.⁵⁶

We are keen to see further analysis to support this hypothesis and to hear any evidence that shows how ethnicity can impact access to fair pension provision.

Question:

Does ethnicity affect pension outcomes? Are educational outcomes improving for ethnic minority groups and how is this likely to translate into both improved employment rates, earnings, and ultimately retirement income? Are there any other data or consideration that you can contribute that might be significant in our consideration of ethnic minority impacts from a change in State Pension age?

⁵⁴ Joseph Rowntree Foundation, 2015, Poverty across ethnic groups through recession and austerity

⁵⁵ Joseph Rowntree Foundation, 2015, Ethnic minority disadvantage in the labour market

⁵⁶ PPI, 2016, The Underpensioned 2016, p5

The position of men and women

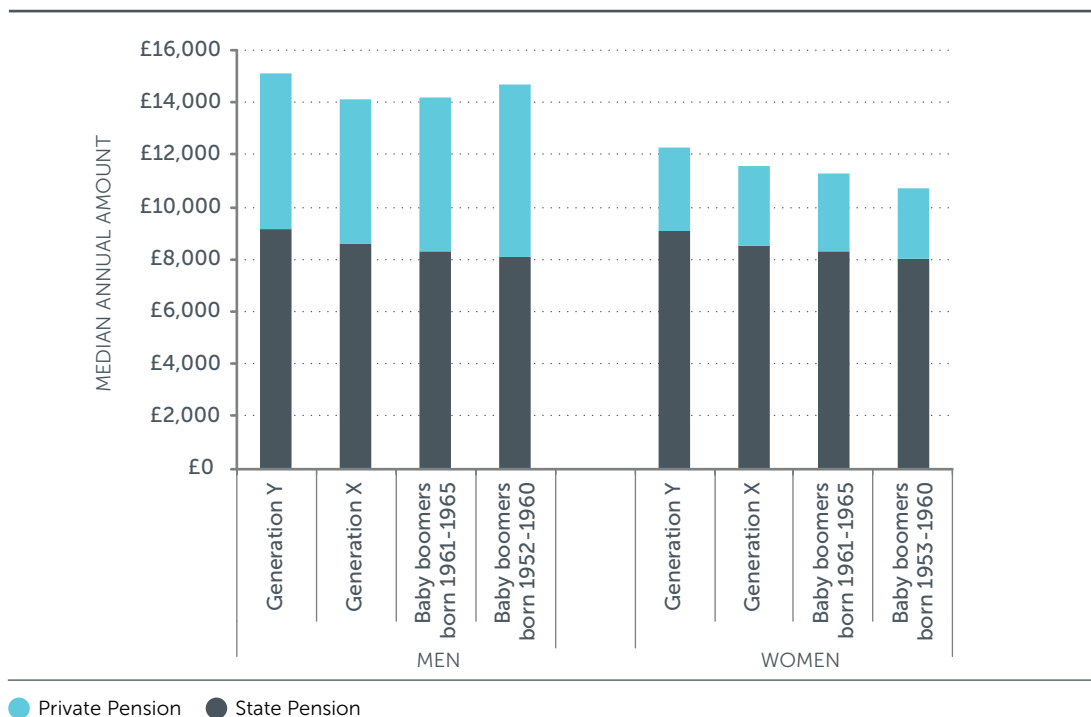
DWP’s PENSIM2 model allows us to look at what people’s annual income is estimated to be in retirement and illustrates variations between groups. We have used this model to look at the projected median income for various groups in the first year of retirement for ease of comparison. The PENSIM2 analysis is important as it shows the overall impact of policies on broad representative groups and emphasises the importance of private pensions in delivering favourable outcomes in retirement.

Taking a broad look across all current working age groups, men are projected to have around a 25% higher income on average than women in their first year of retirement. This equates to a difference of approximately £3,000 per annum. Although the gender gap in pension income is set to narrow for generation X, it in fact widens again for generation Y. This is due to the fact that automatic enrolment’s better coverage and the decline in defined benefit income is offset by the continuing trend of men’s consistent higher earnings and women taking time out of the labour market.

Men and women across all generations are set to receive very similar amounts of State Pension. The discrepancy in pension outcomes for men and women instead reflects different private pension outcomes. On average across all generations, just under 30% of women’s total pension is made up of private pension, compared to just over 40% of men’s. Private pension outcomes are driven by the labour market and reflect the fact that women currently earn on average less than men across their working lives and are more likely to take career breaks and this is assumed to continue into the future.

The chart below shows amounts received by men and women on reaching State Pension age:

Figure 22: Projected median average amounts of State and Private Pension in 1st year of retirement, by gender and generation



Source: PENSIM2

Women appear to be consistently overrepresented in the most impacted groups. We do recognise that for many couples today decisions around work and caring have been taken jointly and for them the important factor may be overall household pension income.

Question:

What is the best way to take into account the lower pension outcomes for women in our recommendations?

Question:

For older workers in particular, the adequacy of income in retirement may be best considered at a household level. However, when planning future changes to the pension system, how reliable is this assessment now and how reliable will it be for future generations?

Conclusions

Our initial analysis of some affected groups shows a number of areas where there may be gaps in outcomes; including for those who suffer poor health or disability in later life, the self-employed, ethnic minorities and those who are carers. This highlights a more general issue. For every group, this gap is not necessarily a gap in total pension income but specifically a gap in private pension income. This is because these groups appear to have different labour market experiences – in general they have lower employment rates and have more breaks in their work history. These issues can translate to less time building up a private pension and ultimately a lower private pension. This will be true for all groups who do less well on average in the labour market.

The evidence suggests that groups such as low paid workers, carers and the disabled will have on average less income in retirement. The principal reason for this is that these groups will secure the least private pension by the time they reach retirement. A combination of interrupted working lives and low earnings when in work mean they will invest less and as a consequence receive less.

Conversely, these groups are likely to have higher replacement rates and many will have higher incomes in retirement than in working life. In relative terms they will be better off as pensioners than they were as workers. This is partly because of the value of the new State Pension with the triple lock. For example, by 2046 and after 34 years of work a Generation X woman who left the labour market at 50 to undertake caring responsibilities and had been automatically enrolled for 16 years would have a new State Pension of £175 a week and a private pension of £3 a week. In this example, she was earning 40% of median earnings during her working life, up until age 50. From age 50 onwards she did not have an income.

However, if this same woman had been in the old two tiered system and had been covered by State Second Pension for 34 years she would have a state pension income, at retirement,

of over £180 a week.

In this example, the triple locked new State Pension and private pension is replacing the income she would have received under the pre 2016 state pension system, although over time the triple-locked new State Pension would increase more than the previous two tier pension.

If the triple lock were withdrawn, as some people have proposed, there is no current mechanism to allocate some of the triple lock savings to mitigate the impact of the withdrawal for the most disadvantaged groups.

Question:

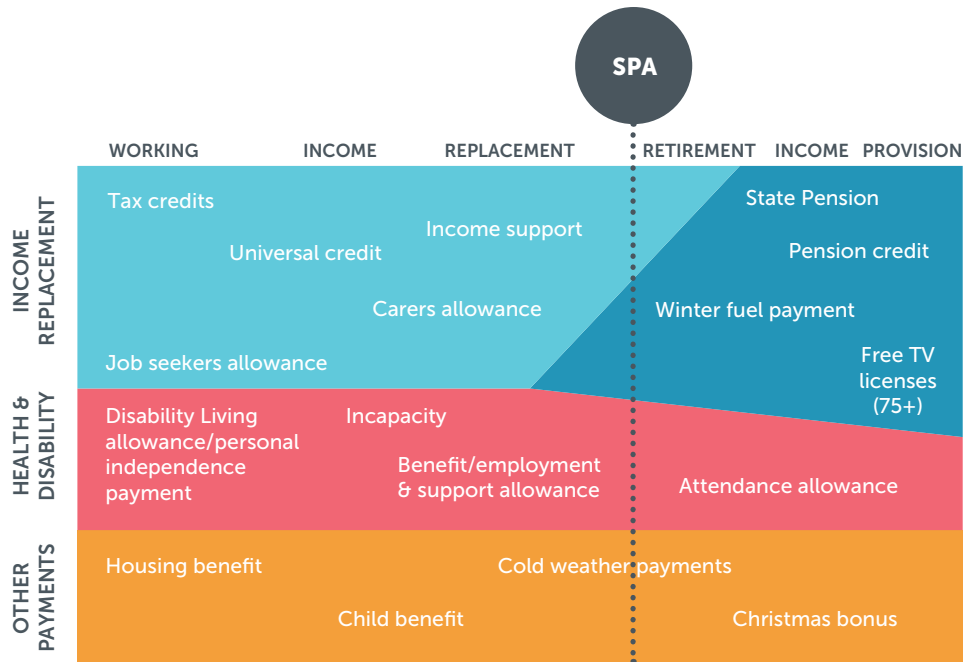
What approach is more appropriate in your view, if we were to protect impacted groups? Should we consider ways to remove any barriers to building their own private retirement income or to support them through the welfare system or is there another approach altogether?

The Review recognises the fact that having worse outcomes in the labour market, and by extension lower private pension income implies that people will be less able to adjust to changes in their circumstances as they get older including possible changes in State Pension age. In particular, they may not be able to draw down early on their private pension or be able to change how they participate in the labour market in response to changes in their circumstances without considerably impacting their retirement income later. We discuss these issues in Chapter 5.

Welfare System Dependencies

State Pension age interacts with other parts of the Welfare system where dependencies can be complex, as well as having a link through to private pensions. In this last part of Chapter 4 we describe these interfaces.

The diagram overleaf provides a summary of the various benefit payments available to people over their lives. It shows that some of the benefit payments associated with those who are retired can be accessed before State Pension age and some working age benefits can continue to be paid after a person reaches State Pension age.



The table summarises the specific age entitlements in more detail.

Benefit	Directly linked to State Pension age?	Age qualification
Pension Credit	Yes	You can claim once you reach SPa. Until equalisation, men can claim when they've reached the SPa of women born on the same day.
Attendance Allowance	Yes	You can claim once you reach State Pension age.
Winter Fuel Payments	Yes	You can claim once you reach women's State Pension age and standard SPa after equalisation.
Cold Weather Payment	No	
Free TV licences	No	You can receive a free TV licence if you are over 75.
Christmas Bonus	No	All those reaching SPa can claim the benefit, but those on some other benefits can receive it earlier.

Working Tax Credits	No	If you are over 60, you must work at least 16 hours to qualify.
Universal Credit	Linked to Pension Credit qualifying age	A couple moves from Universal Credit to Pension Credit once the younger partner reaches Pension Credit age.
Income Support	Linked to Pension Credit qualifying age	Once you reach Pension Credit qualifying age, you no longer are eligible for income support.
Carer's Allowance	No	You must be over 16. If your State Pension is less than Carer's Allowance (currently £62.10 per week), you can have it topped up to this amount by Carer's Allowance.
Job seeker's Allowance	Yes	You can only qualify if you are under State Pension age.
Housing Benefit	No	Housing Benefit is a means-tested benefit for people of working age and pensioners designed to assist with their rental liabilities. How much you get depends on your income and circumstances.

Question:

Is it appropriate for this Review to include in its considerations the entry point for all the welfare policies that are linked to State Pension age? Which ones should be excluded and why?

The impact of increasing State Pension age on welfare recipients

The analysis in this Chapter has focused on information about broadly defined disadvantaged groups once they have reached State Pension age. We now look at the position of these groups immediately before State Pension age to identify the material impact an increase in State Pension age would have on them. We have done this using today's rates of working age benefits (and earnings) comparing them to the full rate of the new State Pension in 2016/17. The alternative, to forecast the position at the point people reach State Pension age, would mean making significant assumptions on future uprating policies for working age benefits.

Position prior to State Pension age/ single person	income/means tested allowance – weekly amount	New State Pension/ Pension Credit at State Pension age - excluding private pension - weekly amount	Increase/decrease at State Pension age
Carer – Receiving Carer’s Allowance	£62.10	£155.65 (nSP)	+£93.55
Carer – Receiving Income Support	£107.70	£190.20 Pension Credit (GC only) with an additional amount for carers	+£82.50
ESA – Support Group contributory	£109.30	£155.65 (nSP)	+£46.35
ESA – Support group income based with severe disability	£186.90	£217.45 – Pension Credit with severe disability	+£30.55
Low earner – 40% median income	£188.00	£155.65	-£32.35

In reality many in the disadvantaged group will be part of a couple and more likely to be assessed as households in the means tested benefits. The following chart summarises the position for a couple both approaching State Pension age (and both entitled to full new State Pension).

Position prior to State Pension age/ couple	income/means tested allowance – weekly amount	New State Pension/ Pension Credit at State Pension age - excluding private pension - weekly amount	Increase/decrease at State Pension age
Receiving Income Support – additional amount for two carers	£184.05	£311.30 (2 x full new State Pension)	+£127.25
ESA – Support group income based with additional amounts for severe disability/caring	£270.10	£334.00 – Pension Credit (GC only) with additional amount for severe disability/caring	+£63.90
Low earning couple – 40% median income	£415	£311.30	-£103.70

Impacts on Occupational Pensions

There are some specific issues for private pension schemes if State Pension age changes. It should be noted that private pension entitlement is a property right (unlike state pensions where entitlement is based on the rules approved by Parliament on the day the person claims). A consequence of this is that people normally accrue entitlement to a private pension according to the rules in force at the time they were a member of a scheme.

The only time where there is crossover between state rules and private pension rules is where State Pension age is used as a reference point in the private pension rules. The main cross over points are:

- Public Sector pensions – where many public sector schemes now tie scheme retirement age to State Pension age;
- Pension Scheme Rules – a significant number of defined benefit and defined contribution pensions are linked to State Pension age, either by age as a number or as a concept.
- Bridging pensions – this is where scheme benefits include an additional amount to bridge the gap between scheme retirement age and State Pension age. Schemes then reduce the pension by typically the full amount of basic State Pension (£119.30 a week for 2016/17). In schemes where State Pension age is defined as say age 65, member will see their bridging amount withdrawn before they receive corresponding amount from the state.
- Early access to private pensions – the point where people can access their private pensions without incurring a tax penalty (which had been fixed at age 55) increases in step with State Pension age

There may be new issues because of pension freedoms. For instance, some people may use their pots to cover the gap between their aspirational retirement date and an increased State Pension age. The most important issue is to ensure people are aware of changes in State Pension age and the implications this will have for them and their retirement planning.



“The SPA remains a reference point for access to benefits in many of our member’s schemes, as well as a point at which many DC savers aim to retire...a differentiated system would reduce transparency and complicate workforce management”
CBI Submission to the Review



Question:

How far should this Review take into account impacts on occupational scheme rules? What are the most significant challenges for those pension schemes if State Pension age is changed?

05 Smoothing the Transition





Introduction

Current trends indicate that almost everybody entering the labour market at any point in time is likely to reach State Pension age later than the age their parents reach State Pension age. However, for many people, State Pension age still represents the maximum age point to be in the labour market. Alongside this, State Pension age changes have been delivered as a series of one-off interventions, rather than as a policy programme in itself. In this Chapter we present some approaches to changing attitudes to longer working. We also outline suggested ways of smoothing the transition between work and retirement. Finally, we look at the important issue of appropriately communicating changes to the State Pension age to individuals.

When should people retire?

There is no easy way of determining when people should retire from work. Research shows that what often motivates or deters people from continuing to work can be a mix of financial circumstances and social attitudes.



“The choice of State Pension Age also sends an important signal about what is thought to be an appropriate age (on average) to cease active participation in the labour market.”

Association of Consulting Actuaries Submission to the Review



The current State Pension has a universal age of access and there has never been a time when the state provided a tailored approach in assessing eligibility to the contributions-based State Pension. This universality is frequently challenged.

In considering the high level principles of a universal State Pension age and a more tailored one, we need to consider several factors such as:

- Simplicity of message and symbolism: there is value in a clear point in time when the state will offer retirement income, which is not complicated to calculate and allows enough time for savings planning.

- Changing circumstances in life: a large number of people will differ in their social circumstances throughout their lifetime, for example switching between ill health, low earnings, high earnings, caring, time working abroad etc. Any conditionality attached to earlier access could still disadvantage a significant number of people.
- Different impacts for different groups: we know that there are considerable differences in the labour market experience and the life expectancy of different groups, mostly driven by socio-economic factors. A universal approach can worsen those impacts if applied without effective support systems.

Question:

What are the alternatives to a universal State Pension age? How can they be designed and implemented so that both the principles of Affordability and Fairness are retained?

We have seen some examples where national systems have provided early access to state pension schemes and then the earliest entry point became the default state pension age. We have also seen evidence that the State Pension age can have a strong influence on the decision to retire.

At the moment the majority of workers leave the labour market before they reach 63 (62 for women, 64 for men). Of this group we know that a significant number of people wish they had postponed their retirement.

We also know that for many people, State Pension age can be the most significant reference point in later life planning but a number of other factors are increasingly relevant:

Work: The nature of work has changed and will likely continue to change. We have seen increased trends in self-employment, part-time work and flexi hours work, more flexible careers. This may mean that there is more opportunity to avoid retiring too early, when it is not financially prudent to do so.

Private pension: we can see from Chapter 2 that increasing numbers of people will have some defined contribution pension provision and increased freedom to use this provision in a number of different ways to suit their personal needs.

Longevity and Health: Most people are going to live longer than the preceding generation and they are likely to be able to work until a later point in life, but these improvements are not spread equally for many groups.

Caring: People will enjoy increased longevity, but are also more likely to have increased caring responsibilities for elderly family members in later life. They are also likely to have children later in life than their parents' generation. This can be an increasing barrier to working in later life for certain people.

Adequate income: We have seen suggestions of economic and labour market changes that will impact the definition of an adequate income in retirement for future generations.

We have noted the risk of higher housing costs until much later in life, as well as a sustained dependency on the State Pension as the main source of retirement for many people.

Question:

What other factors and trends are increasingly relevant and will be prevalent in the future when considering an appropriate retirement age for individuals?

Smoothing the transition between work and retirement

In Chapter 2, we examined the impact of a universal State Pension age rising in line with Life Expectancy on affordability and fairness and also looked at the labour market position of older people. In Chapter 3, we looked at Life Expectancy and asked for views on whether the right way to address the position of groups who are less likely to benefit from longer Life Expectancy is through other policies rather than through State Pension age policy. In Chapter 4 we discussed the position of impacted groups and the material difference it makes to them if they have to wait longer for their state pension. Here we explore whether moving to a more personalised way of assessing what it means to retire, and when those key decisions may happen, could be a better choice for people than a fixed decision point around the State Pension age. We will explore whether it is possible and useful to smooth the transition between working age and retirement.

Working longer

As we mention in Chapter 1, Government is committed to a Fuller Working Lives strategy. We expect a publication update in the near future and we will include it in the evidence base of the State Pension age review.

The Fuller Working Lives strategy has so far focused on engaging with employees and employers, in order to create awareness and influence the factors that create barriers for significant groups of people that disengage from the labour market too soon, often much before State Pension age.

Cash incentives, such as the generous deferral arrangements in place for those who reached State Pension age before 6 April 2016 or the ending of National Insurance liability for employees at State Pension age, do not appear effective at encouraging people to work longer.

There is a suggestion that there are apparent gaps in the provision of employment support in the latter part of adult life. For example, Universal Credit, which is designed to make work pay, is not available to people over State Pension age. Its pension age equivalent, the Standard Minimum Guarantee in Pension Credit, can be paid when people are working but apart from a small earnings disregard, earnings are withdrawn penny for penny, providing little incentive to continue working beyond that point.

We have received evidence from stakeholders that individuals in certain occupations may experience “burnout” which means they are unable to carry on with their chosen career. While some groups and some professions consider burnout point as the appropriate time to retire, others suggest that it is simply a point for an occupational health scheme to intervene, a change of duties or hours or a change of job. There may be scope for policy interventions to support people in this crucial transition point and Government might have a key role to play in that, alongside the individual and the employer.

A lot of the evidence shows that later working can be of benefit to workers and to the UK’s economy. However, there is a lack of a coherent evidence base to establish what types of Government investment in later working policies would be effective.

Question:

Is there any evidence that these Government policies have any impact on the decision to work longer? What other policies can Government adopt alongside the Fuller Working Lives strategy to strengthen Fuller Working Lives outcomes, for example supporting profession transitions and incentives to work longer for low earners?

“Public policy needs to address twin challenges. Firstly, enabling those older workers who want to work to do so. And secondly, ensuring that those who cannot work are provided for. Seeking to use an increased State Pension age as a crude tool to encourage longer working is likely both to be ineffective and risk increasing hardship among older people.”

TUC Submission to the Review



Protecting the most vulnerable

In Chapter 4, we describe the material differences that impacted groups will experience if State Pension age increases. They could be left with limited opportunities to earn or save enough in a workplace scheme and that can have long-term implications in their retirement.

We have received a number of submissions exploring ways of addressing the shortfall in working age incomes for older workers, while preserving the coherence of a universal State Pension age. Others look at policy interventions that offer a more flexible approach to retirement. Some of these options respond to questions of fairness for people who are likely to have lower life expectancies than others. All smooth the path for older impacted groups, who have either permanently left the labour market or, are struggling to make ends meet because of reduced earnings.

The following provides a brief overview of these interventions:

- **Early access to the new State Pension after a long working life** - This would allow people with a high number of National Insurance qualifying years to claim their full new State Pension prior to State Pension age. For instance, with 50 qualifying years as a benchmark, a person who started work at 16 could become entitled to state pension at 66 rather than at State Pension age. A variant of this would be to condition early access to accommodate regional variations in Life Expectancy or to recognise certain occupations where people have a greater risk of a lower Life Expectancy.
- **Early access but to a reduced pension** - This would allow people to claim a reduced State Pension early – so for example at age 60 a person claimed their new State Pension that was valued at £120 a week (rather than £155.65 a week now). Apart from the normal annual uprating this amount would not be increased again. There are various options on how the income-related benefits could be shaped around this policy.
- **Enhanced working age benefits** – Additional amounts could be included in the means-tested benefits to reduce the gap with pension benefits. An additional amount of £45 a week for instance, associated with the carer’s additional amount in Income Support, could increase the income of an older working age carer to near that of the new State Pension.

These policy interventions could add significantly to pension expenditure in the future, increasing in effect the burden on the decreasing number of working age people. All of them would challenge to some extent the main policy objective for responding to increased life expectancy – delivering an affordable state pension system, and enabling people to work longer.

Question:

How can the Government best support these disadvantaged groups? We welcome submissions that comment on these suggestions further or alternative proposals.



“We believe it could be beneficial to investigate ways in which some alternative means is found to compensate those people (not particularly whole groups) who are particularly adversely affected by future changes. Such options could include: extending or enhancing other social security benefits available to individuals in particular need in the periods shortly before SPA; or some form of early retirement of State Pension being allowed for individuals in special circumstances.”

IFoA Submission to the Review





“On the assumption that, in aggregate, longevity continues to improve, whilst significant differences in life expectancy continue to exist between different sectors of society, we believe that the retention of a universal but rising State Pension Age will become increasingly difficult. However, we think that there are practical difficulties in identifying specific groups for differential State Pension Ages. We therefore believe that further thought should be given to alternative measures that would allow individuals with shorter life expectancies to access their State Pension or equivalent income before the official State Pension Age.”



[Association of Consulting Actuaries Submission to the Review](#)

Communicating changes to State Pension age

Encouraging individuals to save for their retirement appears central within the recent reforms in pensions and plays a crucial role in building adequate incomes in later life. Ensuring that individuals have access to information regarding their State Pension age and how much they will receive is key to enabling them to plan for retirement effectively. Communications is a critical part of delivering on the State Pension policy intent of “providing clarity and confidence to better support saving in retirement”.

The White Paper on *The single-tier pension: a simple foundation for saving* sets out that the State Pension age review framework “will seek to provide a minimum of ten years’ notice for individuals affected by changes to State Pension age”. A recent Work and Pensions Select Committee report on Communication of State Pension age changes agreed that “it is critical that people affected by any future changes in the State Pension age are fully and properly informed”.

We recognise that an effective strategy will be important in communicating any changes to State Pension age in the future, to enable people to take full advantage of the given notice period. DWP’s current pensions communications strategy uses general awareness campaigns to encourage people to make use of the personalised information resources available, such as Check your State Pension, the online tool which provides an assessment of someone’s state pension and their State Pension age. Our understanding is that DWP recognises that this is not just an issue for Government, and actively seeks to involve stakeholders, to reach the maximum number of people and target communications effectively. For this reason the Department is also supporting the development of the Pensions Dashboard.

As the scope of this Review covers from 2028 onwards, we may expect the communication needs of different groups to be quite different. For example, someone who is within 10 years of retirement may have a different approach to someone who is just entering working life. We would welcome evidence on how the communications approach should be tailored to suit a range of needs.

Finally, we will be looking into how best to align any communications on State Pension age, with other related campaigns and sources of information. Pensions can be a complex area, so anything the Government can do to support citizens to access the information they need at the right time can be beneficial.

Question:

How can the Government and others communicate any future changes on State Pension age? How important is stakeholder involvement in ensuring that the right messages reach the right people in good time?

Annex A

Terms of Reference

1. Purpose

1.1. The purpose of the independent review of State Pension age is to make recommendations to the Secretary of State for Work and Pensions on future State Pension age arrangements. These recommendations should be affordable in the long term, fair to current and future generations of pensioners, and consistent with supporting fuller working lives.

2. Scope

2.1. This review should include:

- Robust, evidence-based analysis of the current State Pension age timetable and its impacts; and
- Recommendations on future State Pension age arrangements.

2.2. As part of this, the review will need to consider:

- What a suitable State Pension age is, in the immediate future and over the longer term;
- Whether the current system of a universal State Pension age rising in line with life expectancy best supports affordability, fairness, and fuller working lives objectives;
- And, if not, how State Pension age arrangements might better support these objectives.

2.3. In conducting its analysis and reaching recommendations, the review is to have regard to:

- Variations between different groups.
- The views of organisations and individuals on factors to be taken into account. It will consult widely to ensure that it has considered the appropriate evidence and the range of views of interested parties.

3. Deliverables

3.1. The review must submit its report to the Secretary of State by January 2017. This report will be laid before Parliament and will inform the Secretary of State's final report on the outcome of the State Pension age review, which must be published before 7 May 2017.

Annex B

Consultation Questions

1. Is our interpretation of the policy intent for the State Pension correct?
2. How successful are other international policies? Are there any other policies that we could consider? How should the UK policy on State Pension age take these examples into account?
3. Considering the main drivers of State Pension expenditure, which ones are more important to the policy intent, if they were presented as a trade-off? Maintaining early access, a generous increase annually or making the full State Pension amount accessible to most people? Which of these delivers fairer outcomes?
4. Is the Pensions Commission's assessment of the proportion of GDP expenditure on pensioner benefits, over time, still valid, when considering State Pension age affordability post-2028? Is State Pension age the best tool to maintain a steady GDP proportion for pensioner benefits?
5. Are there any other issues around opportunity to achieve adequacy for future generations that we need to consider? How can we best take into account wider economic impacts, for example, the likelihood of low interest rates in pension outcomes or the changes in housing costs and overall wealth distribution?
6. Are there any other factors that may impact the value of the State Pension for each generation?
7. Are replacement rates linked to pre-retirement income a good measure of adequacy for the future? What would be the most relevant alternatives?
8. What evidence is there to suggest "burnout" is a feature of certain professions and what are the alternatives for workers in those roles? How can FWL strategy support best the transition required, if that is the case?
9. To what extent can a delay in State Pension age act as a direct mechanism to enable Fuller Working Lives? What factors would increase the likelihood that people remain in gainful employment during any such delay?
10. How can we best take into account the sensitivity of the life expectancy projections when considering an appropriate State Pension age for the future?

- 11.** Do you think that regional factors have an impact on Life Expectancy and how? How should the Government factor in the combination of regional and socio-economic factors?
- 12.** Are Healthy Life Expectancy and Life Expectancy improving sufficiently for the majority of the population? Are there specific aspects of Healthy Life Expectancy that would directly interact with State Pension age and how?
- 13.** The Pensions Commission suggested that lower Life Expectancy should be tackled through improvements to health and occupational health. Do you agree? How should we take into account the Life Expectancy and Healthy Life Expectancy information when considering State Pension age?
- 14.** How can we best take into account the impact of caring responsibilities in later life and specifically within the decade prior to State Pension age?
- 15.** How can we best take into account the impact of poor health and disability in later life and specifically within the decade prior to State Pension age?
- 16.** How would any State Pension age changes affect the self-employed in the future? How can we take into account the very diverse profiles in this group?
- 17.** Does ethnicity affect pension outcomes? Are educational outcomes improving for ethnic minority groups and how is this likely to translate into both improved employment rates, earnings, and ultimately retirement income? Are there any other data or consideration that you can contribute that might be significant in our consideration of ethnic minority impacts from a change in State Pension age?
- 18.** What is the best way to take into account the lower pension outcomes for women in our recommendations?
- 19.** For older workers in particular, the adequacy of income in retirement may be best considered at a household level. However, when planning future changes to the pension system, how reliable is this assessment now and how reliable will it be for future generations?
- 20.** Is it appropriate for this Review to include in its considerations the entry point for all the welfare policies that are linked to State Pension age? Which ones should be excluded and why?
- 21.** How far should this Review take into account impacts on occupational scheme rules? What are the most significant challenges for those pension schemes if State Pension age is changed?
- 22.** What are the alternatives to a universal State Pension age? How can they be designed and implemented so that both the principles of Affordability and Fairness are retained?
- 23.** What other factors and trends are increasingly relevant and will be prevalent in the future when considering an appropriate retirement age for individuals? [following section on work, caring etc]

24. Is there any evidence that these Government policies have any impact on the decision to work longer? What other policies can Government adopt alongside the Fuller Working Lives strategy to strengthen Fuller Working Lives outcomes, for example supporting profession transitions and incentives to work longer for low earners?

25. What approach is more appropriate in your view, if we were to protect impacted groups? Should we consider ways to remove any barriers to building their own private retirement income or to support them through the welfare system or is there another approach altogether? Why?

26. How can the Government and others communicate any future changes on State Pension age? How important is stakeholder involvement in ensuring that the right messages reach the right people in good time?

Annex C: State Pension age legislated

Women's State Pension age under the Pensions Act 2011

Date of birth	Date State Pension age reached
6 April 1953 – 5 May 1953	6 July 2016
6 May 1953 – 5 June 1953	6 November 2016
6 June 1953 – 5 July 1953	6 March 2017
6 July 1953 – 5 August 1953	6 July 2017
6 August 1953 – 5 September 1953	6 November 2017
6 September 1953 – 5 October 1953	6 March 2018
6 October 1953 – 5 November 1953	6 July 2018
6 November 1953 – 5 December 1953	6 November 2018

Increase in State Pension age from 65 to 66, men and women

Date of birth	Date State Pension age reached
6 December 1953 – 5 January 1954	6 March 2019
6 January 1954 – 5 February 1954	6 May 2019
6 February 1954 – 5 March 1954	6 July 2019
6 March 1954 – 5 April 1954	6 September 2019

6 April 1954 – 5 May 1954	6 November 2019
6 May 1954 – 5 June 1954	6 January 2020
6 June 1954 – 5 July 1954	6 March 2020
6 July 1954 – 5 August 1954	6 May 2020
6 August 1954 – 5 September 1954	6 July 2020
6 September 1954 – 5 October 1954	6 September 2020
6 October 1954 – 5 April 1960	66th birthday

Increase in State Pension age from 66 to 67, men and women

Date of birth	Date State Pension age reached
6 April 1960 – 5 May 1960	66 years and 1 month
6 May 1960 – 5 June 1960	66 years and 2 months
6 June 1960 – 5 July 1960	66 years and 3 months
6 July 1960 – 5 August 1960	66 years and 4 months (1)
6 August 1960 – 5 September 1960	66 years and 5 months
6 September 1960 – 5 October 1960	66 years and 6 months
6 October 1960 – 5 November 1960	66 years and 7 months
6 November 1960 – 5 December 1960	66 years and 8 months
6 December 1960 – 5 January 1961	66 years and 9 months (2)
6 January 1961 – 5 February 1961	66 years and 10 months (3)
6 February 1961 – 5 March 1961	66 years and 11 months
6 March 1961 – 5 April 1977*	67

Increase in State Pension age from 67 to 68, men and women

Date of birth	Date State Pension age reached
6 April 1977 – 5 May 1977	6 May 2044
6 May 1977 – 5 June 1977	6 July 2044
6 June 1977 – 5 July 1977	6 September 2044
6 July 1977 – 5 August 1977	6 November 2044
6 August 1977 – 5 September 1977	6 January 2045
6 September 1977 – 5 October 19677	6 March 2045
6 October 1977 – 5 November 1977	6 May 2045
6 November 1977 – 5 December 1977	6 July 2045
6 December 1977 – 5 January 1978	6 September 2045
6 January 1978 – 5 February 1978	6 November 2045
6 February 1978 – 5 March 1978	6 January 2046
6 March 1961 – 5 April 1978	6 March 2046
6 April 1978 onwards	68th birthday

Please note the above tables represent the current legislated position. Pensions Act 2014 (which increased State Pension age from 66 to 67) introduced a smoother transition compared to the transition arrangements set out in Pension Act 2007.⁵⁵

⁵⁵ Department for Work and Pensions, 2014, State Pension age timetable, gov.uk

