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Retirement income
and assets: the
implications for
retirement income
of Government
policies to extend
working lives

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A Discussion Paper by Daniela Silcock, Daniel Redwood and Chris Curry

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Retirement income and assets: the implications for retirement income of Government policies to extend working lives

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Executive Summary

Introduction

In the UK over the last three decades, life expectancy has increased substantially. In 1981 a 65 year old man could have expected to live for another 14 years on average, to age 79. However in 2011 a 65 year old man can reasonably expect to live for another 21 years, to age 86 on average.

These substantial improvements in life expectancy reflect a complex range of changes in lifestyle, diet, healthcare and patterns of work and economic activity and could be positive for individuals. However, increased life expectancy also poses significant challenges to individuals, to employers and to the Government. Individuals who live longer may have increasingly long retirements to save for and support, employers who sponsor Defined Benefit schemes face increases in the costs of providing these pensions and the Government may face increased pressure from funding the state pension and benefits for pensioners.

This research examines current patterns of work and retirement in the UK among people over age 50 and considers how these might change in the future. The Government has introduced a range of policies and programmes aimed at extending working lives such as policies aimed at moving people off benefits and into paid work, changes to the age at which people can receive state pension and benefit income, and the removal of legal barriers to working longer. The research looks at international experience of similar policy changes and considers what lessons the UK might learn from them. Finally, the research considers what patterns of work and retirement might mean for income adequacy in retirement.

The proportion of people over age 50 in work has risen over the last few decades in the UK

Employment rates have been increasing for people aged 50 and above in the UK. For example, in 1993, around 64% of men aged 50 to 64 were in work in the UK, by 2011 this had increased to 70%. The proportion of men working beyond the current male State Pension Age of age 65 has also increased. In 1993 around 8% of men over age 65 were in work, by 2011 this had increased to 11%.

The increase in employment rates at older ages has been even more substantial for women. The State Pension Age for women was age 60 until 2010, but is now increasing towards the male State Pension Age of 65 under legislation intended to equalise the male and female State Pension Age at age 65 by 2018.

In 1993, around 57% of women aged 50 to 59 in the UK were in work, by 2011 this had increased to around 72%. The proportion of women

working beyond the women's State Pension Age of age 60 has also increased substantially. In 1993, 23% of women aged between 60 and 64 were in work, by 2011 this had increased to 34%.

The average age of exit from the labour market has been increasing for both men and women. In 1984, the average age of exit from the labour market for men in the UK was age 64, by 2011 this had increased to around age 65 for men. For women, the average age of exit from the labour market was around age 61 in 1984 and increased to age 63 by 2011.

These increases in employment beyond age 50 for both men and women mask considerable differences in employment rates at older ages by occupation, skill level and wealth. Working at age 50 and above is more likely for men, for those with higher wealth, for those with higher education and for the self-employed.

Why do people leave work before reaching State Pension Age?

While the proportions of people working at older ages has increased, many people are compelled to leave work before State Pension Age due to circumstances beyond their control, such as health problems or the need to provide care for a family member.

Health problems are one of the main, non-voluntary reasons for people to leave work before State Pension Age. By the time men and women are aged between 60 and 64, around 30% of them have a disability that limits their ability to work. Age, gender, ethnicity, occupation and location affect both the likelihood of having a work limiting disability and the likelihood of continuing to work while disabled. Work limiting disability is more common among older people in lower wealth quintiles, those with lower levels of education and manual workers who are more likely than those in other occupations to leave work due to health problems.

Providing care can also affect people's ability to work at older ages; in 2008/9, 10% of women and 1% of men aged 50 and older who were not in employment were providing care.

Equally some people choose to leave work voluntarily before reaching their State Pension Age. Men are more likely to retire voluntarily before reaching their State Pension Age than women. In 2008/9, around 29% of men reported that they were retiring voluntarily in the five years before State Pension Age, compared to around 8% of women.

People in the highest wealth quintile are more than twice as likely to retire voluntarily before reaching their State Pension Age, than people in the middle wealth quintile. Those with a Defined Benefit pension are almost twice as likely to retire voluntarily before their State Pension Age than those with no private pension income.

In order for older workers to be able to engage in employment there needs to be an appetite from employers to recruit and retain older workers and employers need to be able to provide appropriate support to those older people who need it.

Trends and changes within private pensions could affect future work and retirement patterns

Within the private sector, many of the employers who offer Defined Benefit (DB) pensions have closed their schemes to new members, and increasingly to existing members too, as the costs and risks of providing this type of pension have increased. Increasingly employers are offering current employees Defined Contribution (DC) pension schemes. Auto-enrolment into private pensions, which begins in 2012, will also lead to a substantial increase in people saving in DC pensions.

Members of DC schemes may have more incentive to work longer than members of DB schemes, as working longer can lead to increases in income in retirement from a DC scheme and because levels of contribution into DC schemes have tended to be lower than to DB schemes. This could mean that some people may have to work for longer than expected in order to ensure sufficient income during working life and save for longer into a pension to ensure they have adequate incomes in retirement.

Some policies aimed at extending working lives could increase income for those who can work longer, but may disadvantage those who cannot

The Government is keen to encourage people to work longer in order to combat the potential financial problems both for the individual and for the state posed by a declining birth rate and increases in longevity. The Government has a range of policies and programmes aimed at extending working lives, including:

- policies aimed at moving people off benefits and into paid work;
- changes to the age at which people can receive state pension and benefits income;
- the removal of barriers to working longer, including the removal of legal barriers and efforts to tackle age discrimination in the workplace.

While these policies will encourage and enable some people to work longer, and to take their state and private pension later, there may be negative financial implications for those who cannot work longer because of health problems, or other factors such as caring responsibilities. For those who are unable to work longer, rises to the State Pension Age and changes to the benefit system may result in lower incomes in retirement. Changes to the benefit system may affect older people in particular. Around a million people who are over age 50 are currently receiving Incapacity Benefits. Over the next few years these people will be phased on to Employment and Support Allowance (ESA) which has a stricter

assessment regime. Being found Fit for Work is no guarantee of actually being able to find work. Of those aged 55 and over who were found Fit for Work under the ESA assessment (or had their claim dropped) only around a quarter were in work a year to 16 months later.

A number of other countries have undertaken policy reforms to encourage extending working lives similar to the policies being implemented in the UK. For example:

- Denmark is formally linking increases in State Pension Age to increases in Life Expectancy from 2015. Under current proposals State Pension Age in Denmark is expected to increase to 72 by 2055.
- The USA removed mandatory retirement during the 1970s and 1980s. This has contributed to increases in employment above age 65, which has risen from 11% of people aged 65 and over in 1985 to 17% in 2010.
- New Zealand introduced policies aimed at extending working lives from the early 1990s onwards. New Zealand increased its State Pension Age, removed mandatory retirement on the basis of age and introduced a positive ageing strategy. Although other factors have also played a significant role in increasing participation at older ages including a skills shortage, the increase in the employment rate among older workers increased dramatically. In 1990, 26% of people aged 60 to 64 were in employment in New Zealand. By 2000, this had risen to 46% and by 2010, 70% of people aged 60 to 64 in New Zealand were in employment.

Although the environment and context in the countries where these policies have been implemented differs from that in the UK, there are still some policy conclusions for the UK:

- It is important to have safeguards built into policies designed to encourage working at older ages to help those individuals who cannot work longer.
- Other factors, such as economic changes and changes in pension design, are also likely to be important in determining participation rates at older ages.
- Increases in life expectancy, even if accompanied by increases in working at older ages, are likely to need to be accompanied by increased saving if individuals are to have an adequate income in retirement.

What could future patterns of work and retirement mean for retirement income adequacy?

This research uses two measures of income adequacy in order to test whether pensioners might have enough income in order to meet their needs in retirement:

- The **Minimum Income Standard**, which calculates how much income pensioners require to meet a *minimum acceptable standard of living* (as defined by pensioners in focus groups) is just under £11,000pa (£211pw) for a single pensioner Before Housing Costs (BHC), and around £15,700pa (£303pw) for a couple in 2011. For people who have lived on medium to high incomes during working life, the minimum acceptable standard of living may not seem adequate as it would generally constitute a drop in living standards.
- **Working life replacement rates** which calculate how much income an individual pensioner might need in order to achieve a similar standard of living to the one they had in working life. Replacement rates are generally in the range of 50% to 80% of people's gross working life income. A median-earning man with a weekly income at the point of retirement of around £500pw might need a gross weekly retirement income of around £17,400pa (£335pw) to meet a 67% replacement rate of working life income (and recreate working life living standards). In this analysis, the lowest replacement rates are aligned with the Minimum Income Standard, so that no one has a target income below the Minimum Income Standard.

In order to examine how working longer can affect the adequacy of retirement income, the PPI has modelled the retirement income that individuals aged between 50 and State Pension Age in 2011 might expect to achieve if they continue to work and save at current levels, up until or beyond their State Pension Age.

The analysis assumes that the individuals remain in work, and continue to earn and save at their existing levels until they hit the target level of retirement income. In reality of course, some people may not be able to continue to work and save longer, so the analysis is illustrative of the extent of longer working that may be needed to achieve adequate retirement incomes, rather than a projection of what will actually happen.

The analysis is based on the English Longitudinal Study of Ageing data set of people still in work aged between 50 and State Pension Age in England. Where individuals are not currently saving in a pension it is assumed that, if eligible, they are automatically enrolled into pension saving at minimum required levels – (which are phased in between 2012 and 2019 to reach 8% minimum total contributions on band earnings by 2019).

The following results have been rounded to the nearest 5%. Totals may not sum to 100% because of this rounding.

How many people aged between 50 and State Pension Age in 2011 might be able to meet a Minimum Income Standard of retirement income?

Meeting the Minimum Income Standard will be easier for people than meeting a target replacement rate of working life income using only state pension and benefits and private pension income:

- **The vast majority, around 85%, of those aged between 50 and State Pension Age in 2011 and still in work might have sufficient state and private pension income to meet the Minimum Income Standard by their State Pension Age** assuming that everyone continues to work and save until their State Pension Age and that those who are entitled to means-tested benefits claim them.
- Means-tested benefits can play an important role in helping those on low incomes during working life achieve minimum acceptable standards of living in retirement. Some of those who don't meet the Minimum Income Standard are not eligible for means-tested benefits as their savings are too high.
- **Around 10% of those aged between 50 and State Pension Age in 2011 and still in work** will only be able to meet the Minimum Income Standard if they continue to work and save for a further one to five years after State Pension Age.
- **Around 5% of those aged between 50 and State Pension Age in 2011 and still in work** might need to work for six years or more after their State Pension Age in order to meet the Minimum Income Standard.

How many people aged between age 50 and State Pension Age in 2011 might be able to meet a target replacement rate of retirement income?

Fewer people will be able to meet a target replacement rate of working life income that would allow them to replicate working life living standards by their State Pension Age, using only state pension and benefit income and private pension income:

- **Around 40% of those aged between 50 and State Pension Age in 2011** and still in work might have sufficient state and private pension income to meet a target working life replacement rate by their State Pension Age.
- **Around 10% of those aged between 50 and State Pension Age in 2011 and still in work** may be able to meet their target replacement rate if they continue to work and save for a further one to five years after State Pension Age.
- **Around 5% of those aged between 50 and State Pension Age in 2011 and still in work** may be able to meet their target replacement rate if they continue to work and save for a further six to ten years after State Pension Age.
- **Around 45% of those aged between 50 and State Pension Age in 2011 and still in work, might need to work and save for 11 or more years** after their State Pension Age in order to meet a target replacement rate of working life income.

People with certain characteristics may be more or less likely to be able to meet a target replacement rate by State Pension Age from state and private pension income:

- Those in the lowest income quartile may be more able to meet a target replacement rate of working life income by State Pension Age, as state pension and benefit levels can be close to or above their target replacement rate levels.
- Single women and people in couples are more likely to meet a target replacement rate than single men. For single women this is because they are more likely to have low incomes than single men, and couples can benefit from pooling incomes.
- People with Defined Benefit pension savings might find it easier to meet a target replacement rate in retirement, as historically Defined Benefit pensions have been more generous than Defined Contribution pensions.
- Contributing more to a Defined Contribution pension could mean that people do not need to work as long to meet a replacement rate of working life income which would allow them to replicate working life living standards.

Further modelling analysis explored the impact of working longer and not working longer on 3 hypothetical individuals who have different income levels and saving histories during their working life. The modelling analysis illustrated that:

- Leaving work before State Pension Age can result in lower income both before and after State Pension Age.
- Shopping around and purchasing an enhanced annuity (for example, an annuity offered to individuals with a medical condition that pays a higher annual pension in recognition that their life expectancy is shorter than average) could increase income in retirement for people with health problems.
- Disability benefits can play an important role in meeting income needs for those who have to leave work early due to health problems.
- Remaining in work until State Pension Age can help to maintain living standards up until retirement.
- A high earner, contributing at average levels of salary into a Defined Contribution pension may need to work beyond State Pension Age in order to meet and sustain his target income during retirement.
- Working after State Pension Age can increase net income as a result of tax treatment.

The analysis explored how changes in behaviour in response to a rise in State Pension Age can affect income both before and after retirement:

- As expected, a rise in State Pension Age could reduce income for those who cannot work longer.
- But a rise in State Pension Age could result in higher income both before and after retirement for those who can work longer.

Introduction

In the UK over the last three decades, life expectancy has increased substantially. In 1981 a 65 year old man could have expected to live for another 14 years on average, to age 79.¹ However in 2011 a 65 year old man can reasonably expect to live for another 21 years, to age 86 on average.²

These substantial improvements in life expectancy reflect a complex range of changes in lifestyle, diet, healthcare and patterns of work and economic activity. Improvements in life expectancy could be positive for individuals. However, increased life expectancy also poses significant challenges to individuals, to employers and to the Government. Individuals who live longer may have increasingly long retirements to save for and support, employers who sponsor Defined Benefit schemes face increases in the costs of providing these pensions and the Government may face increased pressure from funding the state pension and benefits for pensioners.

The Government has introduced several policies aimed at extending working lives. Changes to the State Pension Age in particular are likely to impact on future patterns of work, saving and retirement. Other Government policies (such as removing the Default Retirement Age) and trends within private pensions (such as changes to public sector pension schemes and the private sector shift from Defined Benefit to Defined Contribution) are also likely to affect the length of people's working lives and their retirement income.

This report draws together the latest information on current patterns of work and retirement in the UK. It also describes the Government's policy agenda to extend working lives and looks at the lessons the UK can learn from international experience. Finally, using the PPI's modelling capability, this paper considers how much longer individuals may need to work beyond State Pension Age if they wish to meet target levels of retirement income solely through state and private pension income.

Chapter one describes current patterns of work and retirement, and investigates the different social, political, economic and personal factors which impact the decisions people make and the options people have regarding work and retirement.

Chapter two describes and examines the potential implications of Government policies which will affect future work and retirement patterns for older people and looks at the lessons that the UK can learn from other countries that have implemented similar policies.

¹ 2010 based cohort expectation of life, 1981 to 2060, principal projection, United Kingdom, ONS

² 2010 based cohort expectation of life, 1981 to 2060, principal projection, United Kingdom, ONS

Chapter three analyses how working and retirement patterns could impact on future levels of income adequacy for people in retirement.

Chapter four analyses how different patterns of work and retirement could affect the income of individuals who have different income levels.

Chapter one: what are the current patterns of work and retirement in the UK?

This chapter describes current patterns of work and retirement, and investigates the different social, political, economic and personal factors which impact the decisions people make and the options people have regarding work and retirement.

For the purposes of this research the term ‘older people’ refers to people over age 50

This chapter investigates work and retirement trends amongst all people over the age of 50, ‘older people’, and also separately investigates trends among those over State Pension Age (SPA) which is currently rising from age 60 to 65 for women and is age 65 for men. These are both useful groups to examine. Working trends among people over the age of 50 can tell us about the impact of economic and policy changes on general working at older ages, for example, by exploring rises in the average age of labour-market exit. It is also useful to explore trends among those over SPA as SPA is a natural choice as a retirement age for many people.³

Figures in this chapter have been drawn from two main sources. High level information on employment has been estimated using the Labour Force Survey (LFS), which covers the UK. More detailed analysis of movements within the Labour Market and analysis of retirement is generally based on the English Longitudinal Study of Ageing (ELSA), which covers only England.

The next section of this chapter investigates how retirement ages and the proportion of older people in work have changed over the last two decades.

The proportion of older people in work has risen over the last few decades

Employment rates have been increasing for people over the age of 50 since the mid-1990s. While some people may work until or beyond SPA because they enjoy their work, other people work at older ages because they feel that they cannot afford to retire for financial reasons.⁴

³ Crawford, Tetlow (2010)

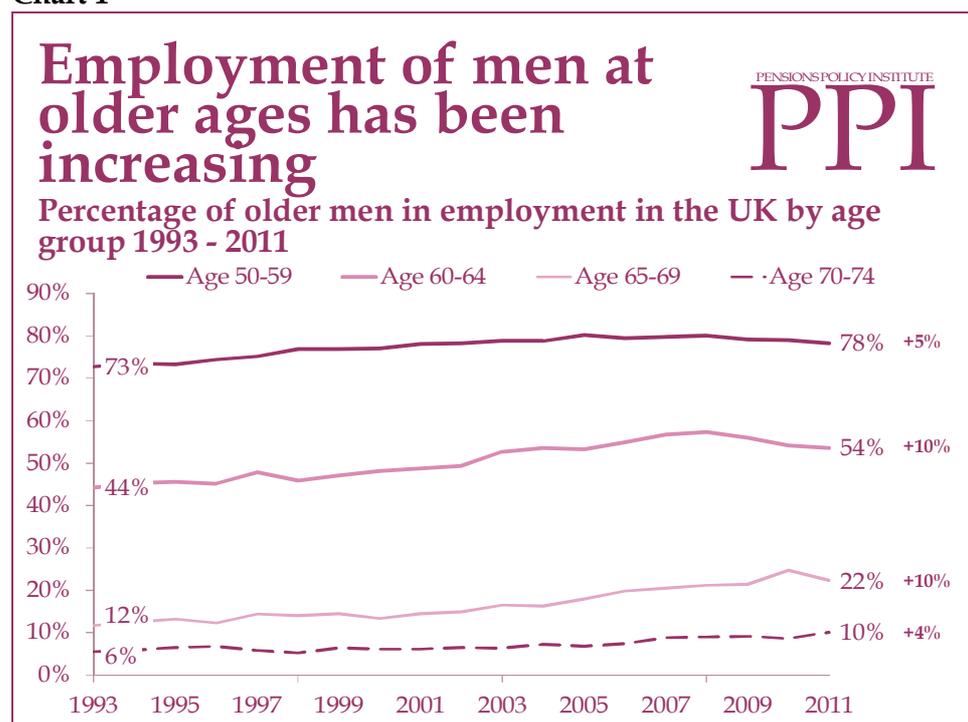
⁴ AIFA (2010)

Employment rates have been growing for men at older ages

There has been an increase in working at older ages among men:

- In 1993, around 64% of men in the UK aged 50 to 64 were in work. In 2011, this had increased to around 70% of men aged 50 to 64 in work.⁵
- In 1993, around 8% of men in the UK over the current male SPA (of age 65) were in work. In 2011, this had increased to around 11% of men over the age of 65 in work.⁶

Chart 1⁷



The increase in employment is especially high for men in age groups just before and just after Men's State Pension Age (Chart 1).

- In 1993, 44% of men in the UK aged between 60 and 64, in the run up to men's SPA, were in employment which increased to 54% by 2011, an increase of 10 percentage points.
- In 1993, 12% of men in the UK aged between 65 and 69, the 5 years just after SPA, were in employment which increased to 22% by 2011, an increase of 10 percentage points.

However, even after these increases the number of men working at older ages is still relatively low. In 2011 there were 330,000 men aged between 65 and 69, 115,000 men aged between 70 and 74, and 60,000 men aged 75 or older in work in the UK.⁸

⁵ PPI analysis of LFS data

⁶ PPI analysis of LFS data

⁷ PPI analysis of LFS data - includes all full-time and part-time work

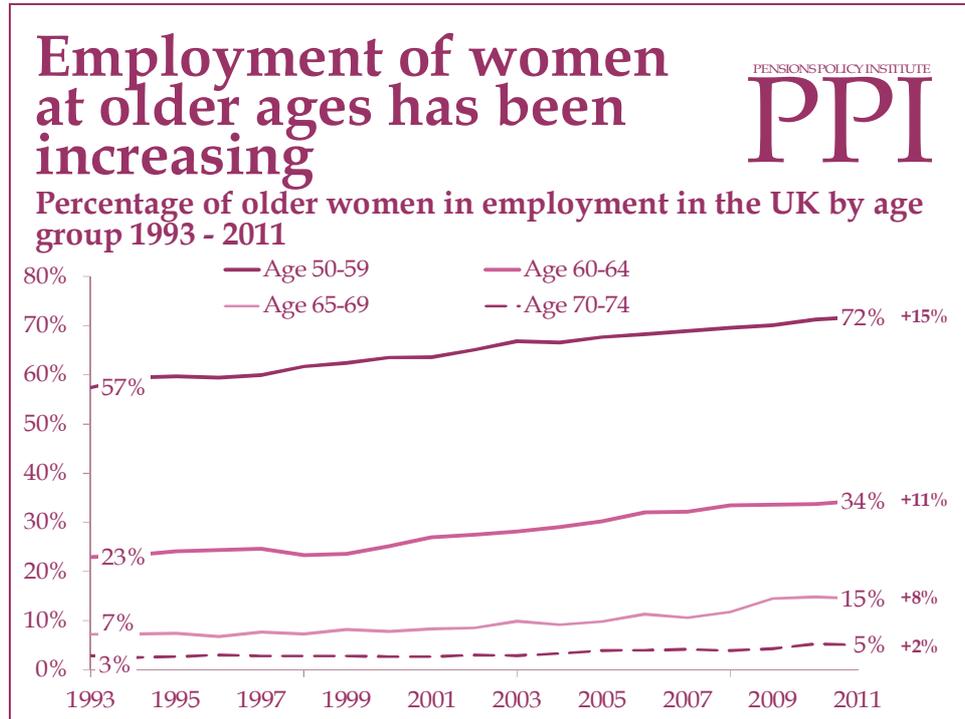
⁸ PPI analysis of LFS data - rounded to the nearest 5,000.

Levels of working at older ages have increased significantly for women

Working at older ages has increased significantly over the last few decades for both men and women, but women have seen a faster increase:

- In 1993, around 57% of women in the UK aged between 50 and 59, the ten years below women’s SPA of age 60, were in work. In 2011, around 72% of women in the UK aged between 50 and 59 in the UK were in work.⁹
- In 1993, around 8% of women in the UK over women’s SPA of 60 were in work. In 2011, around 13% of women in the UK over age 60 were in work.¹⁰

Chart 2¹¹



There have been substantial increases in labour market participation for women over age 60 (Chart 2). The age groups that have seen the greatest increase in participation are women in the ten year run up to women’s State Pension Age and the 4 years after women’s State Pension Age.

- In 1993, 57% of women in the UK aged between 50 and 59, in the ten year run-up to SPA, were in employment which increased to 72% by 2011, an increase of 15 percentage points.
- In 1993, 23% of women in the UK aged between 60 and 64, in the 5 years after SPA, were in employment which increased to 34% by 2011, an increase of 11 percentage points.

⁹ PPI analysis of LFS data

¹⁰ PPI analysis of LFS data

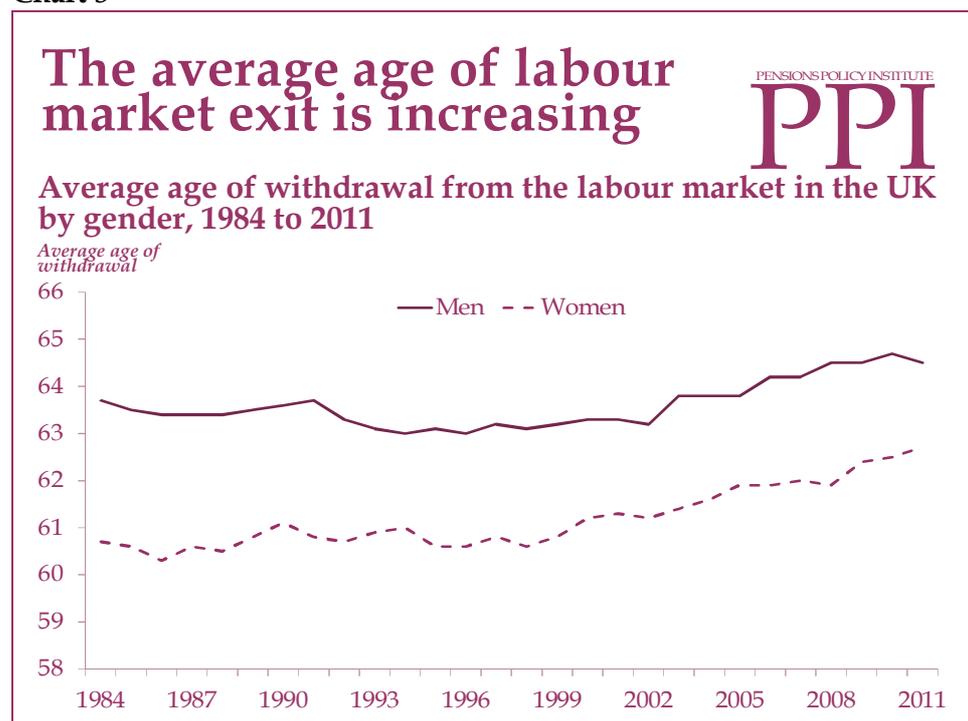
¹¹ PPI analysis of LFS data – includes all full-time and part-time work

Again, despite the increase in employment rates the number of women in employment at older ages is still low. In 2011 there were 230,000 women aged between 65 and 69, 65,000 women aged between 70 and 74, and 10,000 women aged 75 or older in work in the UK.¹²

People are leaving work at older ages than they used to

The average age of leaving the labour market has increased in the UK for women from around age 61 in 1984 to around age 63 in 2011 and for men from around age 64 in 1984 to around age 65 in 2011 (Chart 3).¹³

Chart 3¹⁴



Working at age 50 and above is more likely for those with higher wealth and education

Older people are not a homogenous group and their experiences of, and likelihood of being engaged with, the labour market at older ages varies according to their characteristics. Working at age 50 and above is more likely for:

- Men over age 50 than women over age 50.
- Those with higher wealth - with 24% of the richest quintile of people over age 50 in full-time work in 2008/9 and 14% of those in the poorest.¹⁵

¹² PPI analysis of LFS data - rounded to the nearest 5,000.

¹³ ONS (2012) figure 4.10

¹⁴ ONS (2012) figure 4.10

¹⁵ Crawford, Tetlow (2010) p. 62, Table 2A3. rounded to nearest percent

- Those with higher education - with 35% of those with the highest education in full-time work in 2008/9 and 16% of those with the lowest education.¹⁶
- The self-employed and people working for small employers (Chart 4) - who are more likely to work until they are physically unable to do so than the people in other groups. However, the self-employed are a very diverse group, ranging from highly skilled professionals to people with small or contract based businesses¹⁷ who might need to continue working to provide themselves and their families with an income.¹⁸
- Those in higher skilled occupations (Chart 4), though there is little difference between high and low skilled occupations in the very oldest age groups (aged 75 and older). Some individuals in the low skilled category at these ages may have classified themselves as higher skilled workers earlier in their life.

Chart 4¹⁹

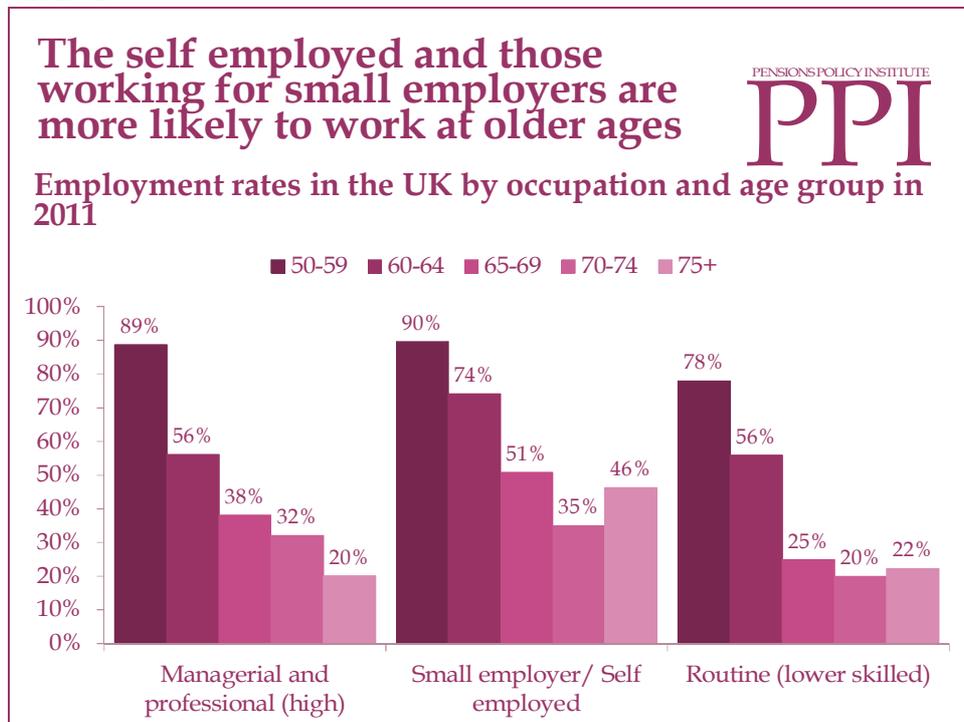


Chart 4 is based on self-reported occupation type, and excludes individuals who report themselves as retired, and so only include those individuals with some attachment to the labour market. The figures in Chart 4 are not therefore directly comparable with the employment rates

¹⁶ Crawford, Tetlow (2010) p. 61, Table 2A.2. rounded to nearest percent. **Low education** = those who left school at or before UK compulsory school leaving (CSL) age for their cohort. **Mid education** = those who left school after CSL age but before age 19. **High education** = those who left school at or after age 19.

¹⁷ For example, building/ decorating services or running a small shop

¹⁸ Phillipson, Smith (2005)

¹⁹ PPI analysis of Labour Force Survey data, July 2011

shown in Charts 1 and 2, but do give an indication of the differences between different occupational groups.

Working beyond State Pension Age is more likely for women, people with higher education, those without a long standing illness, and people whose partners are still working

Working beyond State Pension Age (SPA) is also more likely for people with certain characteristics:

- Working beyond SPA is more likely for people with higher levels of education.²⁰
- Those *without* a long standing illness are more likely to work beyond SPA.²¹
- Those with partners still working are more likely to work after SPA than those whose partners have retired.²²
- Though working at ages over 50 is more likely for men, working beyond SPA is more likely for women, however this could be because they have a lower SPA than men (though this will no longer be the case after 2018).²³ Although women who have never married appear to have similar pension entitlements to men who never married,²⁴ women who have been married are less likely to have paid into a pension,²⁵ and this may contribute to decisions around working if, for example, women feel they cannot afford to retire.²⁶

People can transition from work to retirement by flexible working

There are many ways to phase the transition from full-time work into retirement through the use of flexible working. Flexible working can take many forms (Box 1).

²⁰ Crawford, Tetlow (2010), 40% more likely than those with low education

²¹ Crawford, Tetlow (2010), Those who have a partner with a long standing illness are also more likely to work at older ages

²² Crawford, Tetlow (2010)

²³ Banks, Tetlow (2008)

²⁴ DWP (2006)

²⁵ Because, for example, of broken work history, low earnings or an expectation of depending on their husbands pension.

²⁶ Banks, Tetlow (2008)

Box 1: Flexible working

Flexible working can take many forms, within three broad types of flexibility.²⁷

Flexible working hours, such as:

- Part-time working, working shorter days, or fewer days in a week.
- Flexible hours, where people can choose which hours they work.
- Compressing hours, by allowing people to work long shifts in return for extra days off.
- Working only the hours that are necessary to do the job.
- Becoming self-employed (and setting one's own hours).
- Sharing a job between two workers.

Flexible work space, such as

- Working from home for some or all of the time.

Flexible work, such as:

- A shift to work which is less physically demanding or stressful.

Flexible working is increasing among workers aged 50 and older

There has been an increase in the proportion of workers aged 50 and older who are working flexibly. Using one definition of flexible working, the proportion of people aged 50 or older in the UK in employment who were working flexibly increased from around 30% in 2005 to 38% by 2010.²⁸

This estimate does not explicitly include one of the most commonly considered forms²⁹ of flexible working, part-time working. This is because not all part-time working is necessarily flexible working. Part-time work might be considered flexible if the hours are as a result of agreement between the employer and employee, but might not be flexible if an employee is working part-time only because no full-time work is available.

However, despite the problems in identifying whether part-time workers are working flexibly or working shorter hours than they would prefer due to the lack of opportunity, analysis of the trends in part-time work can help identify potential trends in flexible working.

The next section of this chapter therefore looks at current trends in part-time working among older people and investigates the potential for developments in part-time working in the future.

²⁷ Hedges, Sykes (DWP) (2009), and Age UK (2012)

²⁸ Age UK estimates based on the LFS where flexible working is defined as one of: Flexi-time, annualised hours contract, term time working, job sharing, nine-day fortnight, 4.5 day week, zero hours contract, on-call working or home working. Part-time work is not explicitly included, although part-time workers are treated as working flexibly if they use one of the other options listed.

²⁹ Alongside self-employment Phillipson, Smith (2005)

The use of part-time working is increasing at older ages

The proportion of older people in part-time work is increasing, with a greater proportional increase in part-time working among men than women (Table 1).

Table 1: The proportion of men and women in England over age 50 in part-time work by year³⁰

	2002/3	2008/9
Men	8%	10%
Women	18%	19%

Between 2002/3 and 2008/9 around 10% of people in England over age 50 moved from full-time work to part-time work (Table 2), and around 20% of these people then moved into retirement from part-time work.³¹ The following table shows the transitions men and women in employment made between 2002/3 and 2008/9.

Table 2: The employment transitions of men and women in England between age 50 and State Pension Age between 2002/3 and 2008/9³²

Type of work, non-work or transition during 2002/3 - 2008/9	Men	Women
Always full-time	30%	11%
Always part-time	3%	16%
Always inactive	26%	26%
Full-time to part-time	7%	7%
Full-time to part-time to inactive	2%	2%
Full-time to inactive	15%	7%
Part-time to inactive	4%	16%
Other	13%	15%

Women are more likely to work part-time than men

The likelihood of working part-time varies between different groups:

- Women are more likely to work part-time than men. In 2011, 30% of women in the UK and 5% of men aged between 50 and 54 were in part-time work (Chart 5).
- The self-employed are more likely to work part-time than employees,³³ though it may also be the case that people wishing to work part-time may become self-employed if there is a lack of opportunity for employed part-time work.

³⁰ Crawford, Tetlow (2010) Table 2a.1

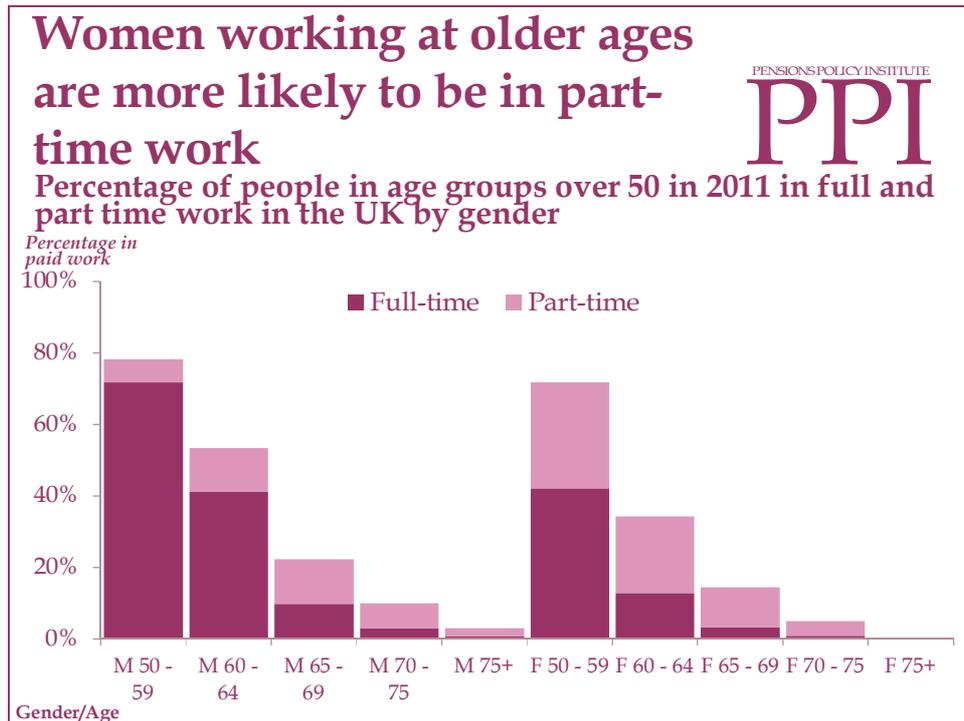
³¹ Crawford, Tetlow (2010)

³² Crawford, Tetlow (2010) p. 72, Table 2A.12. rounded to nearest percent. Other includes all other work patterns not already listed.

³³ Banks, Tetlow (2008)

- Older people are more likely to work part-time than younger people; beyond age 65 part-time work is more common for both men and women than full-time work.³⁴
- People in good health and with higher levels of education are more likely to phase into retirement by moving from full-time work to part-time work before retiring outright.³⁵
- People who are entitled to a Defined Benefit pension, on the other hand, are more likely to retire outright from full-time work rather than to phase through part-time work first.³⁶

Chart 5³⁷



Flexible working is not an option for everyone

A number of organisations³⁸ actively promote flexible working and the recruitment of older workers. In 2003, around 46% of employees reported having access to flexible working.³⁹ However flexible working is not available to all employees across all sectors. Employers in some sectors may find it harder than others to offer flexible working. Larger employers may find it easier to accommodate the need for flexible working through reducing hours or changing people’s roles or job descriptions.

³⁴ Banks, Tetlow (2008)

³⁵ Crawford, Tetlow (2010)

³⁶ Crawford, Tetlow (2010)

³⁷ PPI analysis of Labour Force Survey data, July 2011

³⁸ For example, ASDA and B&Q

³⁹ Phillipson, Smith (2005)

The way people take their pension can impact access to flexible working

Pensions can play a role in access to flexible working. Since 2006 the requirement for people to leave the employer who manages their pension scheme before receiving a pension from that scheme has been removed, meaning that more flexible ways of working and receiving income could be available than were previously. For example, some people can now work part-time for the same employer, while taking their occupational pension to supplement their income (although not all employers offer this option). People with private Defined Contribution pensions can generally convert some or all of their fund into an income at any point from age 55 and use it to supplement earnings.

Why are some people working longer?

Many people work longer because they need income

For many people, working at older ages or beyond State Pension Age (SPA) will be a necessity rather than a choice. Many people work longer because they have financial commitments such as mortgages, children at university, non-working partners or other dependents.⁴⁰ Those with a mortgage are twice as likely as those who own their homes outright to work after SPA.⁴¹ Many people also work longer because they feel they simply cannot afford to retire, or want to ensure that they have saved enough in their pension to provide themselves with an acceptable income in retirement.⁴²

Attitudes to work have an impact on whether people work at older ages

As well as being associated with characteristics such as wealth and education level, the attitudes people have to work will be associated with their likelihood of working at older ages. Those who have a strong identification with work are more likely to continue working at older ages.⁴³ People have also cited the following wide-ranging reasons for staying in work at older ages:⁴⁴

- maintaining social contact,
- keeping motivated and having something to do with their time,
- maintaining structure,
- maintaining personal status and self-worth,
- not feeling 'old', and,
- in some cases, people have identified wishing to avoid spending too much time at home with their spouse as the reason for staying in work.

⁴⁰ Phillipson, Smith (2005)

⁴¹ Crawford, Tetlow (2010)

⁴² Phillipson, Smith (2005)

⁴³ Phillipson, Smith (2005)

⁴⁴ Hedges, Sykes (2009)

Expectation of working at older ages in future is increasing

The expectation of being in work in future is highly correlated with actually being in work,⁴⁵ and the expectation of working after SPA has been increasing over the last decade (Table 3).

Table 3: Average⁴⁶ expectations of being in work after different ages by age and gender in 2002/3 and 2008/9,⁴⁷ England

Expectation of being in work after age	Gender/Age	2002/3	2008/9
55	Women aged 50-54	66%	72%
	Men aged 50-54	55%	60%
60	Women aged 55-59	36%	48%
	Men aged 55-59	56%	62%
65	Men aged 60 to 64	26%	32%

Why are some people not working longer?

Some people retire voluntarily before State Pension Age, others retire early because they are ‘pushed’ by redundancy, ill-health or the need to provide care

People who leave work before SPA do so for a variety of reasons. Some of those who leave before SPA may feel that they have made sufficient financial provision to support themselves through retirement. However many people say they are compelled to leave work before SPA due to circumstances beyond their control such as health problems or the need to provide care for a family member. Some people may leave work before SPA because they are made redundant and are unable to find another job.

Although many reasons are given for not working longer there is little quantitative evidence with which to gauge which reasons are the most important, or the possible interactions between the reasons. However, many of the people who leave work before SPA for reasons beyond their control may not have made sufficient financial provision for their retirement and may suffer financially as a result.

Men are more likely to retire *voluntarily* before their SPA than women (as opposed to being compelled to by circumstances). In 2008/9, around 29% of men reported that they were ‘retiring’ in the five years before their SPA, compared to around 8% of women.⁴⁸

Those who are most likely to retire *voluntarily* before SPA are:⁴⁹

- Those in the highest wealth quintile, who are 2.2 times more likely than those in the middle quintile to retire voluntarily before SPA.

⁴⁵ Banks, Tetlow (2008)

⁴⁶ Mean average

⁴⁷ Crawford, Tetlow (2010) p. 73 Table 2A.13.

⁴⁸ Crawford, Tetlow (2010)

⁴⁹ Crawford, Tetlow (2010)

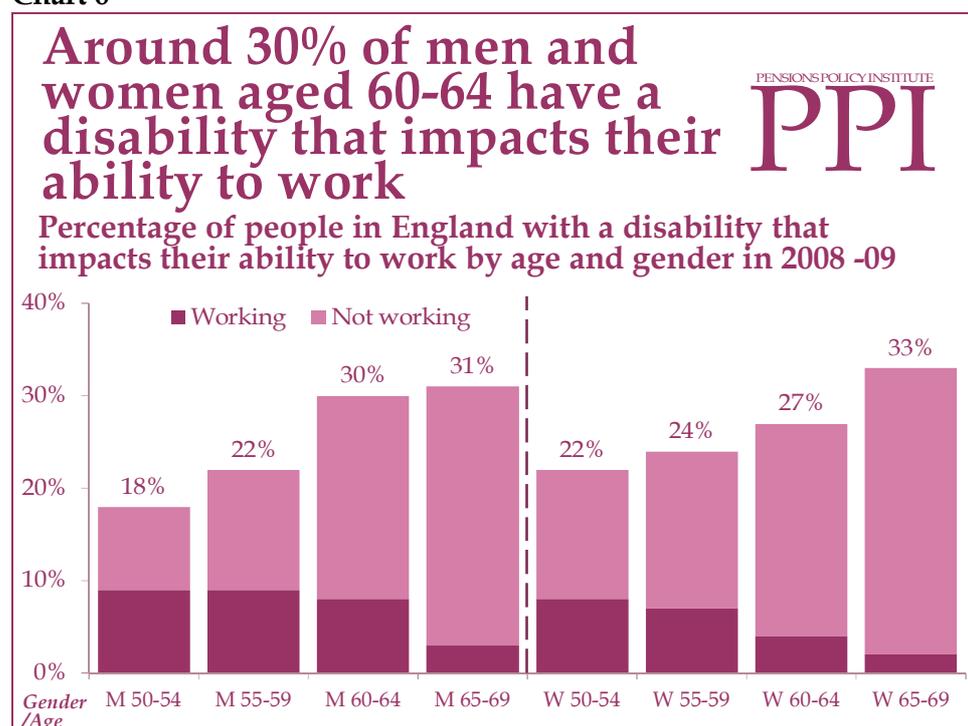
- Those with a DB pension, who are almost twice as likely to retire voluntarily before SPA than those with no private pension.
- Those with a long standing illness, who are over 50% more likely to retire voluntarily before SPA than those without, (though a large number of older people with a long standing illness reported leaving work for illness reasons and not as 'retiring'.)
- Those in Northern England, who are more likely to report being retired voluntarily than those in the South East.

The next sections consider the reasons for involuntary retirement. In general, involuntary retirement is more likely than voluntary retirement to be associated with negative outcomes in retirement, such as lower levels of well-being.⁵⁰

Health problems are one of the main, non-voluntary reasons for people to leave work before State Pension Age

Around 20% of men and women in England aged between 50 and 54 have a disability which limits their ability to work. By the time men and women are between ages 60 to 64, around 30% have a disability that limits their ability to work (Chart 6).

Chart 6⁵¹



Some people with a work limiting disability continue to work at older ages. However, in order to continue working with a disability many people will need support from their employer, for example, through

⁵⁰ Smith (2004)

⁵¹ Crawford, Tetlow (2010) p. 68, Table 2A.7. rounded to nearest percent

reduced hours or a shift of responsibilities. Some workplaces are unable or unwilling to offer support to disabled employees. Therefore some people with a disability, who may be capable of working if supported, may not have access to suitable support and may therefore be compelled to leave work altogether.

Age, gender, ethnicity, occupation and location affect both the likelihood of having a work limiting disability and the likelihood of continuing to work while disabled:

- Work limiting disability is more common amongst older people in lower wealth quintiles, though the direction of causation is not clear (the deprivation associated with low wealth could lead to disability, conversely being ill during working life could lead to low wealth as earning and saving capability may have been constrained).⁵²
- Work limiting disability is also more common amongst older people with low levels of education.⁵³
- The likelihood of working while disabled varies:
 - Ø Older people with a work limiting disability in the North East are less than half as likely to be working than those in the South East.⁵⁴
 - Ø Older women who have a work limiting disability are less likely to be in paid work than men.⁵⁵
 - Ø Manual workers are more likely than those in other occupations to leave work due to health problems, either because the employer cannot offer them suitable alternative employment or because the employee does not feel capable of changing/shifting roles.⁵⁶
- Occupation type affects the type of disability people experience: white collar workers are more likely to report that health problems at work are stress-related rather than physical.⁵⁷
- In the UK, people from particular ethnic minority groups are more likely to suffer from health problems than white people. For example, Pakistani men are twice as likely as those in the general population to suffer from heart disease.⁵⁸ People from some ethnic minority groups may therefore be more likely to need to leave work at younger ages as a result of their health problems.

Some people who leave work due to a disability, may be able to return to work at a later date

Of people aged between 50 and 69 who reported a work limiting disability in 2004/5, 41% reported no longer having a work limiting

⁵² Crawford, Tetlow (2010)

⁵³ Crawford, Tetlow (2010)

⁵⁴ Crawford, Tetlow (2010)

⁵⁵ Crawford, Tetlow (2010) however this may be also related to the fact that women over age 50 are generally less likely to be in work than men

⁵⁶ Hedges, Sykes (DWP) (2009)

⁵⁷ Phillipson, Smith (2005)

⁵⁸ Mai Sims, Vanderaa (2008) The differences in health outcomes for people from particular ethnic minority groups are due at least in part to a lack of access to culturally appropriate care and support from healthcare providers

disability either in 2006/7, 2008/9 or both.⁵⁹ However, whether someone can return to work will depend on whether there are any jobs on offer, whether a potential workplace can offer support in terms of flexibility and training (if necessary), and the employee's willingness to return to work. In practice, it may be very difficult for an older person to return to work after they have left work due to disability, even if they recover from their disability. On the whole, people who leave work due to health problems (after age 50) are unlikely to re-join the labour market.⁶⁰ This is due to several factors, including the following: many older people leave work due to health problems or caring responsibilities which may hinder their return; the older someone is when they leave the labour market the less likely they are to feel motivated to return; and there are perceptions among those out of work that discrimination among employers will prevent their return.⁶¹

Returning to work at older ages can be difficult and associated with receiving lower wages

For each additional year that people over age 50 are out of work, women are around 9% and men are around 24% less likely to return.⁶² And if people do return to work after time out, this is often associated with a reduction in wage of around a quarter for those over age 50, and around 20% for those aged 25-49.⁶³ The prospect of lower wages may make returning to work after time out less attractive. For example, the smaller the gap is between wages and benefits, the more reluctant many jobcentre attendees are to return to work.⁶⁴

Some people leave work at or before State Pension Age because they do not feel there is enough financial incentive to remain

Leaving work before or at SPA is not necessarily a poor choice for everyone. For people who have made extensive financial provision or are entitled to a good pension, leaving work before SPA is both more common (for example, people with a DB pension are twice as likely to retire before SPA than people with no private pension⁶⁵) and less likely to lead to economic deprivation.

However, some people who may benefit from remaining in work at older ages may still choose to leave work. Some people might not understand the potential financial benefits of staying in work or even believe that working after the SPA is prohibited.⁶⁶ But even those who are aware that you can work after SPA may feel that there are incentives to leave work, for example, some people believe that post-SPA income is too heavily

⁵⁹ Crawford, Tetlow (2010)

⁶⁰ Phillipson, Smith (2005), Banks, Tetlow (2008)

⁶¹ Phillipson, Smith (2005),

⁶² Banks, Tetlow (2008)

⁶³ Phillipson, Smith (2005)

⁶⁴ Phillipson, Smith (2005)

⁶⁵ Crawford, Tetlow (2010)

⁶⁶ DWP (2010b)

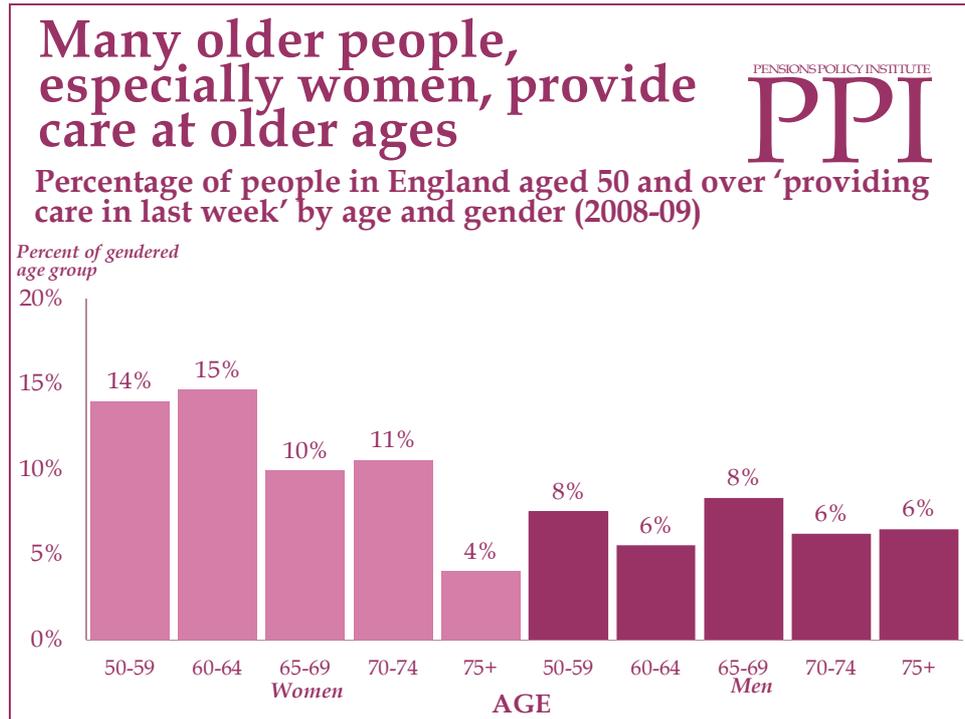
taxed to make work after the SPA rewarding.⁶⁷ Many people also have limited knowledge regarding the potential benefits of state and private pension deferral,⁶⁸ or a belief that they will not live long enough to make deferral worthwhile.⁶⁹

On the whole, qualitative studies reveal very little understanding amongst the majority of people regarding pension planning and the potential benefits of working longer. However, there is some evidence that communicating with people about the potential benefits can make working longer seem more attractive.⁷⁰

Many people leave work to provide care for a family member

As people age they are more likely to provide care for a family member (most often a partner or a parent). Women, and people from some ethnic minority groups,⁷¹ are more likely to provide care at older ages with 14% of women in England aged 50-59, and 15% of women in England aged 60-64, reporting that they ‘actively provided care in the last week’ in 2008/9 (Chart 7).

Chart 7⁷²



⁶⁷ Hedges, Sykes (DWP) (2009)

⁶⁸ In 2008-09 around 2% of individuals aged between SPA and age 75 were in receipt of a state pension but had deferred it until some point above their SPA, Crawford, Tetlow (2010)

⁶⁹ Hedges, Sykes (DWP) (2009)

⁷⁰ Hedges, Sykes (DWP) (2009)

⁷¹ Such as people from Bangladeshi and Pakistani backgrounds, Buckner, Yeandle (2006)

⁷² PPI analysis of English Longitudinal Study of Ageing (ELSA) WAVE 4 data

Providing care impacts people's ability to work; in 2008/9, 10% of women and 1% of men in England aged 50 and older who were not in employment were providing care.⁷³ The need to provide care can lead to an exit from the labour market because the need to provide care often means that people are no longer able to work regular hours or work too far from their home. Some carers report having found satisfaction from their job but felt that they were unable to continue working due to the demands of caring.⁷⁴ Some who wished to return to work while caring found that suitable work (e.g., with flexible hours or close enough to home)⁷⁵ was not available to them.⁷⁶

Obstacles to older working can come directly from employers

In order for older workers to be able to engage in employment there needs to be an appetite from employers to recruit and retain older workers. Employers can facilitate older working by engaging with 'active ageing' policies and practices by, for example, actively recruiting and offering training to older workers, engaging positively with diversity policies, offering on-going career management and options for phased and flexible working and retirement.

Before the introduction of the Employment Equality Age Regulations (EEAR), relatively few organisations seemed to be engaged in active ageing policies.⁷⁷ However, there is evidence that the introduction of the EEAR and the more recent removal of the Default Retirement Age has resulted in some progress with regards to the recruitment and retention of older workers, and engagement with diversity and performance management policies.⁷⁸ While this suggests that at least in terms of formal employer policies and HR best practice organisations are removing barriers to older working, more evidence is needed of this being converted into practical changes in behaviour and attitudes.

Trends and changes within private pensions could affect work and retirement patterns

The levels and types of private pensions held by individuals can affect retirement behaviour. Individuals with Defined Benefit (DB) pensions are more likely to retire at earlier ages than individuals with Defined Contribution (DC) pensions, or those without any private pension.⁷⁹ A typical DB scheme allows individuals to keep building up a pension until a certain pension age (generally age 65) but does not increase after that point, so there is less incentive to stay in work.

⁷³ Crawford, Tetlow (2010) p. 65, Table 2A.5. rounded to nearest percent

⁷⁴ Vickerstaff *et. al.* (2009)

⁷⁵ Vickerstaff *et. al.* (2009)

⁷⁶ Vickerstaff *et. al.* (2009)

⁷⁷ Metcalf, Meadows (2006)

⁷⁸ Metcalf, Meadows (2010), McNair *et al* (2007)

⁷⁹ Crawford, Tetlow (2010)

In contrast, for those saving into a Defined Contribution pension there are greater incentives to work longer. For example, working and saving longer could: increase the number of contributions that have been paid into the fund, increase the period over which investment returns are built up, and, if an annuity is purchased to convert the pension fund into an income stream, reduce the cost of an annuity due to the shorter expected period in payment.⁸⁰

The rest of this chapter examines trends within private pensions and investigates how these could affect the options people have around work and retirement.

- **Defined Benefit pensions are becoming less common in the private sector:** Within the private sector, many Defined Benefit (DB) pension schemes are closing to new members, future accruals and, in some cases, selling their liabilities to third parties and closing their schemes altogether. Some DB schemes which are remaining open in the private sector are trying to reduce costs by lowering their accrual rate, basing final pension income on average salary rather than final salary, or, as a result of a change in Government policy, changing the index by which pension payments and deferred entitlement is uprated from the Retail Prices Index (RPI) to the Consumer Prices Index (CPI), which generally increases more slowly out of the two.
- **Public sector Defined Benefit pensions are undergoing change:** Within the public sector, DB schemes are undergoing changes which could result in higher contributions from scheme members and a move to basing final pension income on average salary rather than final salary, as well as potential future increases in the age at which people are expected to take their pension. Public sector pension payments (as well as valuations of deferred entitlement) have all been adjusted to uprate annually in line with growth in the CPI rather than the RPI.
- **Rises in the Normal Pension Ages of people in DB pension schemes could lead to scheme members working longer:** The minimum age at which people can take their private pension without a reduction in value, the Normal Pension Age (NPA), rose from 60 to 65 in many public sector occupational pension schemes during the last few years. There are Government proposals to link some public sector schemes NPAs to the State Pension Age (SPA) in the future. Some private sector schemes may also decide to link their NPA's to the SPA in the future.

⁸⁰ Assuming that other factors that could affect the annuity rates (such as changes in life expectancies and interest rates) are not changed in the intervening period.

People with occupational pensions have historically left work at younger ages on average than people without them,⁸¹ in 2008/9 those with DB pensions were almost twice as likely to retire before SPA than those without pension provision.⁸² However, rises in the NPA could lead to many people in occupational pension schemes waiting longer to take their pension and working longer in order to provide themselves with income in lieu of a pension.

- **More people will be saving in DC pension scheme in the future:** Because many private sector DB schemes are closing, many people who may in the past have saved in a DB scheme will only have the option of saving in a DC scheme if they want a private pension. Auto-enrolment will also lead to an increase in people saving in DC pensions when it begins in 2012. Active membership in DC schemes could grow to around 15 million by 2020 and around 17 million by 2050, compared to an estimated 5 million in 2008.⁸³
- **An increased number of people saving in DC pensions rather than DB pensions can lead to greater risks and lower pension incomes for some individuals:** Saving in a DC pension scheme is inherently more risky for the individual than saving in a DB pension scheme. This is because in a DC scheme, the risk of market fluctuations causing fund depletion or poor investment return is carried by the individual, whereas in a DB scheme the risk is carried by the employer. Members of DC schemes also receive lower pension incomes on average than those in DB schemes partly due to the lower average level of contributions in DC schemes:
 - Ø In private sector occupational DC schemes, average employee contributions in 2010 were 2.7% of salary and average employer contributions were 6.2 % of salary.⁸⁴
 - Ø In private sector occupational DB schemes, average employee contributions in 2010 were 5.1% of salary and average employer contributions were 15.8 % of salary.⁸⁵

As a result of the reduction in coverage of DB schemes and the growth of DC schemes, future pensioners will face more uncertainty about their income in retirement. This could mean that some people may have to work for longer than expected in order to ensure sufficient income during working life and save for longer into a pension to ensure they have adequate incomes in retirement.

⁸¹ Phillipson, Smith (2005), this could be partly because NPAs have historically been lower than SPA and some people may have felt that their occupational pension provided sufficient income to live off of in retirement. Some people may also have been encouraged to leave at NPA by their organisations.

⁸² Crawford, Tetlow (2010)

⁸³ PPI (2009b), PPI Aggregate Model

⁸⁴ ONS (2011a)

⁸⁵ ONS (2011a)

Conclusions

Employment rates have been increasing for people aged 50 and above:

- In 1993, around 64% of men aged 50 to 64 were in work. In 2011, this had increased to around 70% of men aged 50 to 64 in work.
- In 1993, around 57% of women aged 50 to 59 were in work. In 2011, around 72% of women aged 50 to 59 were in work.
- In 1993, around 8% of men over the SPA (65+) were in work. In 2011, this had increased to around 11% of men over the SPA (65+) were in work.
- In 1993, around 8% of women over the SPA (60+) were in work. In 2011, around 13% of women over the SPA (60+) were in work.

The use of flexible working, such as part-time working, as a way to phase into retirement is growing amongst older people though not all organisations are able or willing to offer flexible working to their employees.

Many people are compelled to leave work before SPA due to circumstances beyond their control such as health problems or the need to provide care for a family member. Some people with a disability or caring responsibilities, who may be capable of working if supported, may not have access to suitable support from their employer and may therefore be compelled to leave work altogether.

People who leave work before SPA for reasons beyond their control may not have made sufficient financial provision for their retirement and may therefore suffer financially as a result, and have lower levels of well-being.

In order for older workers to be able to engage in employment there needs to be an appetite from employers to recruit and retain older workers and to provide appropriate support to those older people who need it. While there is some evidence of this in HR policies, it is not clear if this has yet fed through into employer behaviour and attitudes.

As a result of the reduction in the coverage of Defined Benefit (DB) schemes and the growth of Defined Contribution (DC) schemes, future pensioners will face more uncertainty about their income in retirement. This could mean that some people may have to work for longer than expected in order to ensure sufficient income during working life and save enough in a pension to ensure they have adequate incomes in retirement.

Chapter two: what are the implications of the Government's extending working lives policy agenda?

This chapter describes and examines the potential implications of Government policies which will affect future work and retirement patterns for older people.

The Government is committed to encouraging people to work for longer

The Government is keen to encourage people to work longer in order to combat the potential financial problems both for the individual and for the state posed by a declining birth rate and increases in longevity. The Government has said that it *"would like to foster a climate in which people become: less inclined to retire before State Pension Age (SPA); more likely to give favourable consideration to working on after they reach SPA; [and] more understanding of any regulatory changes the Government may need to bring in to cushion the effects of pension shortfalls, where these may lead to people working longer."*⁸⁶

What constitutes the Government's extending working lives policy agenda?

The Government has a range of policies and programmes aimed at extending working lives. The rest of this chapter describes these in turn and investigates what the implications might be for the Government and for individuals of the following policies:

- **Policies aimed at moving people off benefits and into paid work:**
 - Ø Changes to disability related benefits
 - Ø The Government's Work programme
- **Changes to age at which people can receive state pension and benefits income:**
 - Ø State Pension Age rises
 - Ø Changes to the age at which people can claim Pension Credit
- **Removal of barriers to working longer:**
 - Ø Removal of the Default Retirement Age
 - Ø Efforts to tackle age discrimination in the workplace: The Employment Equality Age Regulations 2006; The Age Positive Initiative

⁸⁶ Hedges, Sykes (DWP) (2009)

Policies aimed at moving people off benefits and into paid work

In order to tackle unemployment and ensure the sustainability of the benefit system, the Government has made several changes to the benefit system

The Government is committed to increasing employment amongst people of all ages and reducing benefit dependency in order to ensure the sustainability of the benefit system and to make sure that people who are able to work do so. Therefore they have made some changes to the way that disability benefits are paid and the way that 'fitness for work' is determined for benefit applicants. Specifically, Incapacity Benefit and disability related Income Support are being phased out and are being replaced by Employment and Support Allowance (ESA).

The Government has designed the ESA eligibility assessment to be stricter than the previous Incapacity Benefit assessment, so that fewer people will be eligible for means-tested benefits. The Government anticipates a reduction in benefit claimants of around 110,000 people by 2017/18 with yearly savings reaching £215m by 2017/18.⁸⁷

Under the new benefit assessment regime, fewer individuals are being found eligible for benefits

Under the previous Personal Capability Assessment used for Incapacity Benefit before the introduction of ESA, around 37% of claimants were found Fit for Work and therefore ineligible for benefits. A higher proportion of claimants have been found Fit for Work under the newer ESA work capability assessment where around 57% of new claimants were found Fit for Work (before taking appeals into account) and ineligible for ESA.⁸⁸

As well as assessing all new claims for benefit under the new assessment regime, the Government has also been re-assessing existing recipients of Incapacity Benefit under the new regime, and adjusting benefit entitlement subject to the outcome of the assessment. There are differences in the outcomes of assessments between new and existing claimants. For claimants *transitioning from Incapacity Benefit to ESA*, 37% were assessed as Fit for Work and are not entitled to ESA (before taking appeals into account).⁸⁹

⁸⁷ DWP (2008), p. 5

⁸⁸ DWP (2012b) official statistics for all new claims started between March 2011 and May 2011

⁸⁹ DWP (2012a)

Many older people will be affected by the changes to the benefit system

Around a million people who are over age 50 are currently receiving Incapacity Benefits.⁹⁰ At some point during the next few years these people will be phased on to ESA and it is likely that many will be found Fit for Work under the new, stricter assessment regime and therefore ineligible to continue receiving benefits unless they successfully appeal the decision. Some older people who are found Fit for Work may have difficulties finding work.

Those who are found Fit for Work will not necessarily all end up in paid employment

For those aged 50 and over who have applied for the new Employment and Support Allowance and either were found Fit for Work, and therefore ineligible for benefits, or had dropped their claim, a year to 16 months later:⁹¹

- 28% of those aged 50–54 and 24% of those aged 55+ were in work,
- 23% of those aged 50–54 and 17% of those aged 55+ were temporarily unable to work due to sickness,
- 29% of those aged 50–54 and 30% of those aged 55+ were permanently unable to work due to sickness,
- 12% of those aged 50–54 and 11% of those aged 55+ were looking for work,
- 3% of those aged 50–54 and 1% of those aged 55+ were providing care.

For those who do not successfully appeal a Fit for Work decision, there are several potential destinations such as: entering paid employment, claiming another benefit, or living off a partner's income or off their savings.⁹²

Those who are found Fit for Work but are unable to find employment may suffer from a reduction in income as well as from the stress of being unable to find work. It is well recognised that:

- It is harder for those who have been unemployed than those who have been in continuous employment to find work;⁹³
- This difficulty increases the longer the period of unemployment lasts; and,
- Older people especially can find it difficult to return to work after a period of unemployment.⁹⁴

⁹⁰ DWP tabulation tool, <http://83.244.183.180/100pc/tabtool.html>, (February 2011 data) includes Severe Disablement Allowance recipients (closed to new claimants). Existing recipients of Severe Disablement Allowance are being phased on to ESA alongside Incapacity Benefit recipients.

⁹¹ Barnes *et. al.* (2011) figure 4.1, excludes successful appeals and appeals in progress

⁹² Barnes *et. al.* (2011)

⁹³ Because of many factors including: the attitudes of employers to people who have spent time outside the workforce; mental health problems and other behavioural and emotional effects of unemployment; deterioration of skills; deterioration of confidence etc.

⁹⁴ Hedges, Sykes (DWP) (2009)

Those who were found Fit for Work but did not find work were more likely to experience deterioration in health and well-being,⁹⁵ making it less likely that they would be able to work in the future.

The Work Programme is intended to provide help to the long-term unemployed and vulnerable groups

Alongside changes to benefits, the Government has also introduced the Work Programme,⁹⁶ which is intended to provide help to the long-term unemployed who have not been able to find work through Job Centre programmes and assistance.

Many older people who may be moving off benefits or transitioning from Incapacity Benefit to ESA may end up in the Work Programme as they may find it harder to return to work than younger participants.

The Work Programme was launched in 2011 and there is not yet enough data to assess the impact it is having on older people and their employment. An evaluation of the Work Programme is due to be undertaken between 2011 and 2013⁹⁷ which will give an indication of the impact that the Work Programme is having on the employment of older people.

Changes to the age at which people can receive state pension and benefits income

Increases in longevity can increase Government expenditure on the state pension

When the State Pension Age (SPA) of age 65 for men and age 60 for women was introduced in 1948 the life expectancy of a man aged 65 was 12 years and the life expectancy of a woman aged 65 was 15 years.⁹⁸ However, in 2011 the life expectancy of:

- a man aged 65 had risen to 21 years, and is expected to rise to 22 years by 2015 and 25 years by 2050.⁹⁹
- a woman aged 65 had risen to 24 years, and is expected to rise to 25 years by 2015 and 28 years by 2050.¹⁰⁰

Increases in longevity increase the cost to the taxpayer of paying the State Pension

The Government estimates that the UK is currently spending around £100 billion per year on 'pensioner benefits' which include the state pension, Pension Credit and other benefits for pensioners.¹⁰¹ This is around 6.9% of

⁹⁵ CAB (2010)

⁹⁶ www.dwp.gov.uk/policy/welfare-reform/get-britain-working/#work

⁹⁷ By a consortium led by the Institute for Employment Studies, www.employment-studies.co.uk/main/index.php

⁹⁸ Office of Health Economics data

⁹⁹ ONS 2010 based cohort expectations of life, www.ons.gov.uk

¹⁰⁰ ONS 2010 based cohort expectations of life

¹⁰¹ DWP (2010a)

GDP in 2010.¹⁰² The proportion of GDP spent on the state pension and pensioner benefits will rise as longevity increases, unless either the SPA rises with it or the Government reduces the amount people receive from the state pension. The Government estimates that, as a result of upwards revisions of life expectancy, they may have to spend around £6.5 billion more than previously estimated on the cohort of pensioners who reached SPA in 2010 over their lifetime.¹⁰³

The Government is raising the age at which people can claim their state pension

Without policy change, increases in longevity result in people receiving their state pension for longer periods than older generations. For example, people who reached SPA in 2010 will on average receive their state pension for 32% of their adult life, compared to those who reached SPA in 1981, who will receive their state pension for, on average, 25% of their adult life.¹⁰⁴

If the SPA remains unchanged and longevity continues to improve, the proportion of adult life spent in receipt of the state pension would continue to increase. This would not only increase the cost to the UK taxpayer and the Government of providing state pensions, it also creates intergenerational unfairness because it means that the level of benefit people receive from the state pension depends on the generational cohort to which they belong.

Therefore, the Government is raising the SPA. The SPA in the UK in 2012 is age 61 for women and is age 65 for men. From 2010 to 2018, women's SPA is rising and will reach age 65 by 2018. Both men and women's SPA will rise to 66 by 2020. Current legislation means that the SPA will continue to rise further in a series of steps: from 66 to 67 between 2026 and 2028¹⁰⁵ and from 67 to 68 between 2044 and 2046 for both men and women (Chart 8).¹⁰⁶ The Government estimates that their revisions to the SPA rise timeline will save £30.6 billion in spending on state pensions between 2016/17 and 2025/26.¹⁰⁷

¹⁰² 2010 GDP = £1,458,452,000,000 ONS Blue Book 2011, www.ons.gov.uk

¹⁰³ DWP (2010a)

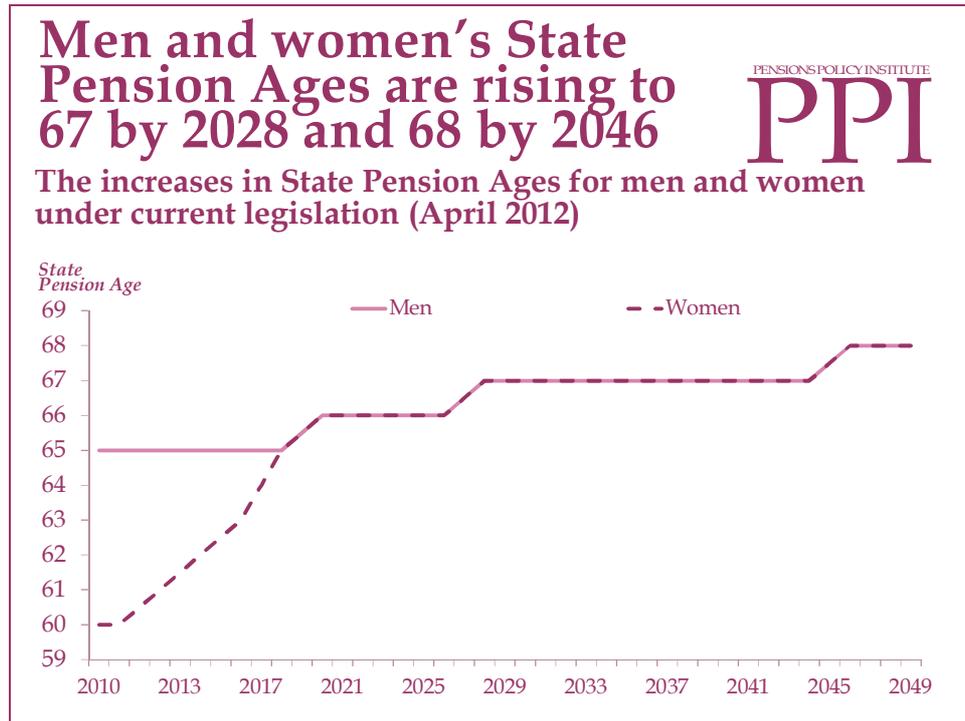
¹⁰⁴ Adult life is assumed to begin at age 18 and assuming a combined average life expectancy for men and women. PPI Briefing Note 60 *What are the implications of the Government's latest legislation increasing State Pension Age?* www.pensionspolicyinstitute.org.uk

¹⁰⁵ Pensions Act 2011

¹⁰⁶ Pensions Act 2007

¹⁰⁷ DWP (2011b) Table 3

Chart 8



The current Coalition Government has indicated that it believes that the SPA may need to rise faster and further than this, that there may need to be a link to longevity in future increases (to be reviewed automatically when life expectancy projections are revised), and that it might bring forward the rise to age 68.¹⁰⁸

The next section of this chapter briefly summarises the impact that SPA rises could have on the incomes of particular groups, specifically those who may have either shorter life expectancies or those who might need to leave work at earlier ages.

State Pension Age rises might reduce the proportion of life people in lower social classes spend in receipt of the state pension relative to those in higher social classes

People in lower social classes have lower life expectancies on average than those in higher social classes.¹⁰⁹ Because of this, any rises in SPA will mean that those in lower social classes and manual jobs will spend, on average, relatively less time in receipt of the state pension as a result of rises in SPA than those with higher life expectancies.

The Government argues that the current legislated rises in SPA will not unfairly disadvantage those with lower life expectancies because people in all social groups will still experience increases in life expectancy which

¹⁰⁸ DWP (2010a)

¹⁰⁹ Using the Registrar General's classification of social class: I - Professional, II - Intermediate, IIN - Skilled non-manual, IIIM - Skilled manual, IV - Semi-skilled manual, V - Unskilled manual

are equal to or higher than the increases in SPA.¹¹⁰ However, the *proportion* of life spent in receipt of state pension for those with lower life expectancies may be more substantially reduced by SPA rises than for those with higher life expectancies.

Those on lower incomes are likely to have lower private pension entitlement or savings when they reach retirement and are more likely to receive a large proportion of their income from the state pension. Therefore, they might lose a higher proportion of total lifetime income as a result of SPA rises than those with higher private pension savings and other income and assets.¹¹¹

Women will see a greater reduction in state pension income and in proportion of time spent in receipt of state pension as a result of equalisation

The SPA rises which are currently legislated for, especially the equalisation of men and women's SPA at age 65 by 2018, mean that women will lose out more than men both in terms of reduction of their total pension income (including Pension Credit for those on very low incomes) and in terms of a reduction in the proportion of life spent in receipt of state pension.

Women will be particularly affected by the equalisation of their SPA with men's between 2010 and 2018, which will be followed quickly by a rise to age 66 for both men and women by 2020. This involves women's SPA rising by 6 years over a period of around 10 years. The final rise has been accelerated by recent Coalition Government legislation. Women's SPA was originally intended to reach 65 in 2020 and 66 in 2028 alongside men's. The recent legislation has a particular impact on women who are currently within 10 or less years of their previously expected SPA who may have already made work, saving and retirement decisions based on having a particular SPA and who may not be able to adjust to a higher SPA by working or saving longer (see Box 2).

However, if women work longer as a result of SPA increases they may have a higher overall income in both working life and retirement. For some women who are able to work longer, SPA rises could therefore potentially be financially beneficial.

¹¹⁰ DWP (2010a)

¹¹¹ DWP (2010a)

Box 2: Adjusting to rises in State Pension Age**One important consideration when evaluating when SPA should rise is the amount of notice people might need in order to adjust their finances**

An adequate amount of notice regarding SPA rises is necessary in order to allow people to adjust their working and saving plans accordingly. For people who are already economically inactive when an SPA rise is announced it may be difficult to adjust their work and retirement plans. This is because people may have saved up only enough to support themselves up until the SPA that they had on leaving paid work. It might be difficult for older people to re-enter the labour market in order to increase their retirement savings or fund themselves until their SPA.

SPA changes in the past have aimed to avoid this issue by using long lead-in times. Women were given at least 15 years' notice in relation to the equalisation of male and female SPAs between 2010 and 2020 as originally scheduled.¹¹²

Evidence on participation rates at older ages would suggest that if less than five years notice is given of changes to male SPA, many men might find it difficult to adjust. Within 5 years of the current SPA of 65, only 60% of the male workforce is still economically active. Men may need at least 5 years notice and ideally 10 years notice of an SPA change, because within 10 years of the current SPA of 65, around 75% of men were still economically active in 2010¹¹³ and may therefore have been in a position to respond to the policy change by delaying their retirement if they needed to. A smaller proportion, around 65% of women aged 50-59 were economically active in 2010¹¹⁴ suggesting that women may need more notice of SPA changes than men.

Women are likely to receive higher state pensions in future

Women have historically tended to have lower state pension entitlement than men, due to being more likely to take time out of work for caring responsibilities and because women have lower earnings on average than men. But in the future, (by around the end of 2018) around 90% of both women and men are expected to reach retirement with a full Basic State Pension.¹¹⁵ Therefore, many women will be reaching SPA later than previous cohorts, but some will receive a higher state pension income as a result of reforms to the qualifying system, and the introduction in 2016 of the single-tier pension.¹¹⁶

¹¹² The legislation for previous SPA rises was introduced in 1995 but the actual changes did not start to be implemented until 2010 to 2020

¹¹³ ONS, Pension Trends, Chapter 4 (2011)

¹¹⁴ ONS, Pension Trends, Chapter 4 (2011)

¹¹⁵ DWP (2010a)

¹¹⁶ Announced in the Chancellor of the Exchequer's Budget Statement, March 12, 2012 www.hm-treasury.gov.uk

People from some ethnic minority groups and people with disabilities are less likely to be in paid work and may therefore be more affected by State Pension Age rises¹¹⁷

People from non-white ethnic groups are more likely to have low or no private pension savings, more likely to be in receipt of state benefits during working life and twice as likely as white people to be entitled to Pension Credit when they reach age of entitlement.¹¹⁸ People from some ethnic minority groups are also more likely to be unemployed during working life, especially people from a black ethnic background. People from Asian ethnic backgrounds are less likely to be in paid work than other ethnic groups, due to illness, disability or the need to provide care.¹¹⁹

Therefore rises to SPA are likely to have a greater negative financial impact on people from some ethnic minority groups than they will on the general population. Similarly, people with disabilities are less likely to be in paid work and more likely to be eligible for Pension Credit at the minimum qualifying age, and may therefore lose out more than people in other groups as a result of policy changes.¹²⁰

Changes to the age at which people are entitled to Pension Credit could affect the incomes of some people over the age of 60

Pension Credit is the main means-tested benefit for pensioners and there are currently around 2.5 million pensioners claiming it.¹²¹ Pension Credit is made up of two elements: Guarantee Credit, which tops pensioners' income up to a minimum weekly income of £142.70 (2012/13) and Savings Credit, which pays extra income to pensioners with savings.¹²²

The age at which pensioners can claim Pension Credit is linked to women's SPA and has therefore been age 60 since its introduction in 2003. Changes to women's SPA mean that the age at which all people can claim Pension Credit is rising, and could impact the incomes of people between age 60 and SPA who may previously have been able to claim Pension Credit. The age at which some people can claim Pension Credit will also be impacted by changes in the Welfare Reform Act 2012 which stipulate that an individual over the SPA will not be entitled to Pension Credit if they have a spouse under the SPA. This stipulation will come into force when Universal Credit is introduced, which is currently expected to be in October 2013.

¹¹⁷ There isn't enough data on life expectancy and ethnicity to make conclusions regarding how SPA rises might affect the proportion of lifetime that people from ethnic minority groups spend in receipt of the state pension

¹¹⁸ DWP (2010a)

¹¹⁹ DWP (2010a)

¹²⁰ DWP (2010a)

¹²¹ DWP data, February 2011. DWP tabulation tool, <http://83.244.183.180/100pc/tabtool.html>

¹²² Including state and private pensions in payment

The Government is investigating options for linking future rises in State Pension Age to longevity

If longevity continues to increase, the SPA will also need to continue rising in order to ensure that the state pension remains affordable and that there is intergenerational fairness. The Government has announced an intention to ensure the SPA is increased in future to take into account increases in longevity.¹²³ Although the Government has not yet determined the formula they will use, they have suggested that there will be automatic reviews of SPA whenever there is a revision of life expectancy projections. The Government plans to publish proposals later in 2012.¹²⁴

Many countries are exploring ways of linking pensions to life expectancy, but linking Pensionable Age (State Pension Age) to life expectancy is still relatively uncommon

Many countries are exploring methods of linking state pension benefits to life expectancy; either by adjusting the amount of benefit that people are paid or by adjusting the number of qualifying years required to be eligible for a full state pension. However, linking Pensionable Age itself to life expectancy is less common; only Denmark, Italy and Greece are currently legislating for a direct link between Pensionable Age and life expectancy.¹²⁵

The following case study describes Denmark's plans for linking life expectancy to their Pensionable Age (State Pension Age) and highlights the lessons that the Danish experience has for the UK.

International Case Study: Denmark - Linking Pensionable Age to life expectancy

Denmark - relevant statistics:¹²⁶

- **Pensionable Age** - 65, rising to 67 by 2022 and 68 by 2030 (UK - equalising at 65 then rising to 66 by 2020, 67 by 2026, then 68 by 2046 at the latest)
- **Average life expectancy at age 65** - 83¹²⁷ (UK - 84)¹²⁸
- **% GDP spent on state pension** - 5.6% (UK - 6.9%)
- **Average age of labour market exit for men (2011)** - 64 (UK - 64)¹²⁹

Denmark will link Pensionable Age to life expectancy from 2015

From 2015, Danish Pensionable Age will be indexed to life expectancy using the average life expectancy of 60 year olds over the previous two

¹²³ Chancellor of the Exchequer's Budget Statement, March 12, 2012 www.hm-treasury.gov.uk

¹²⁴ At the time of the Office for Budget Responsibility's (OBR) 2012 Fiscal sustainability report

¹²⁵ OECD (2011)

¹²⁶ OECD (2011) OECD figures are used in order to make comparisons across countries on a consistent basis, internal country statistics may vary from OECD stats.

¹²⁷ OECD figure of average between men and women.

¹²⁸ OECD (2011) this is the OECD figure for UK life expectancy.

¹²⁹ OECD (2011)

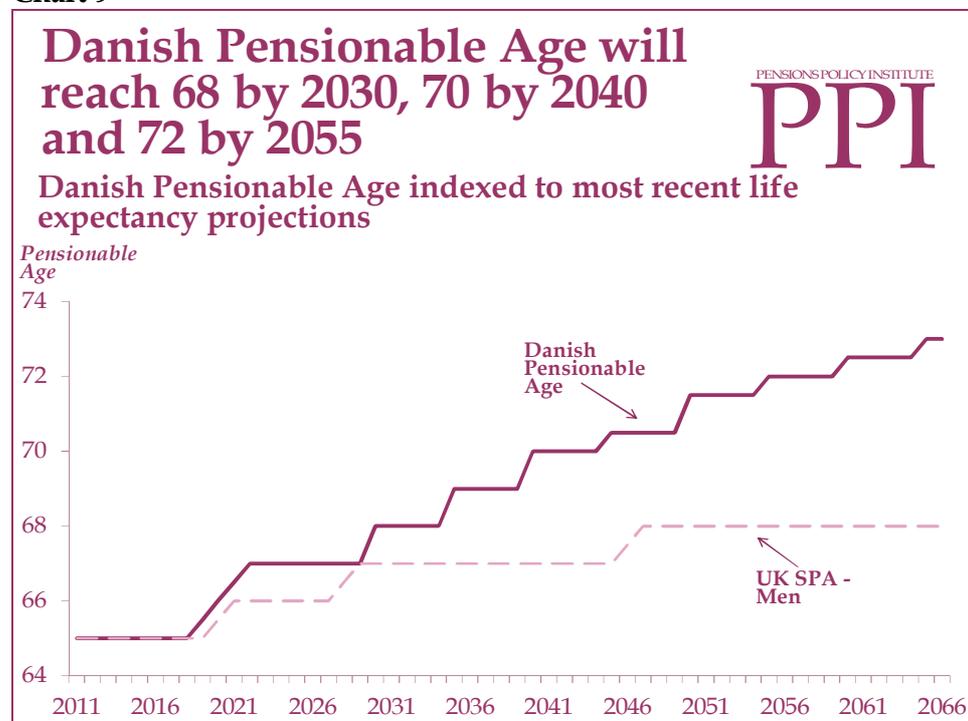
years. Under current calculations, Pensionable Age is expected to rise from 65 to 67 by 2022, and reach 68 by 2030, 70 by 2040, and 72 by 2055 (Chart 9).

In the UK under current legislation the SPA will rise from just above age 60 for women to age 65 between 2010 to 2018, and both men and women's SPA will rise from 65 to 66 by 2020. The SPA will continue to rise further in a series of steps: from 66 to 67 between 2026 and 2028 and from 67 to 68 between 2044 and 2046 for both men and women (Chart 9).

Denmark is reducing the average time spent in receipt of the state pension in order to ensure sustainability

The average number of years Danish people spend in receipt of their state pension, in 2010, is around 19½ years. The Government is raising the Pensionable Age in a series of steps in order to reduce the average number of years Danish people spend in receipt of their state pension to 14½ years, and then maintain that average with increases linked to life expectancy. The Danish Government anticipates that the proportion of the population in work will increase as a result of policies on work, disability and changes to Pensionable Age.¹³⁰ Chart 9 shows the projected impact on the Danish Pensionable Age of both improvements in life expectancy and the gradual reduction in the average number of years people will receive their state pension.

Chart 9¹³¹



¹³⁰ PM Helle Thorning-Schmidt speech to Parliament October 2011 www.stm.dk/_p_13523.html

¹³¹ Danish ministry of finance

There are safeguards built into the system

All Danish employees, as well as the majority of people on benefits and many self-employed people belong to ATP (the Danish Labour Market Supplementary Pension). ATP is a “*statutory, fully funded, collective insurance based, defined-contribution scheme.*”¹³² ATP directly pays a flat-rate pension annuity to its members from the age of 65 and functions as an addition to the Danish state pension.

ATP allows people who have made sufficient contributions and are unemployed or working part-time to make use of an *early retirement age* and take their ATP pension up to five years before Pensionable Age at a reduced rate. The early retirement age is being reduced in a series of stages to three years before Pensionable Age between 2018 and 2023. There is an exception for those who are disabled who can claim an early ATP pension on the basis of their disability.

There are therefore some safeguards built into the rises to Pensionable Age in the form of the early retirement and the exception for disabled people, though they will not protect people who have not made sufficient contributions (such as some self-employed people) who might need to claim state benefits if they cannot work anymore.

Conclusions and lessons for the UK from the Danish experience

Denmark is raising their Pensionable Age in line with projected changes in life expectancy from 2015 in order to ensure sustainability of their state pension. Though these rises will ensure that the Danish Government can continue to pay the state pension without reducing the benefits paid the rises also mean that some people who cannot work until Pensionable Age will have to wait longer for their state pension. There are some safeguards built into the system in the form of the early retirement age and the special senior disability scheme, although the minimum age for early retirement is rising alongside changes to Pensionable Age.

The current Coalition Government has announced that there will be a link between the SPA in the UK and life expectancy in future. The UK SPA may therefore rise fairly quickly, as seen in current projections of rises in the Danish Pensionable Age. If the UK were to adopt a direct link between SPA and life expectancy then safeguards may be needed to protect those who may not be able to work longer.

¹³² OECD (2011)

The removal of barriers to working longer

The Government has removed the right to compulsorily retire employees on the basis of their age

In 2006, the previous Labour Government brought in the Default Retirement Age (DRA). The DRA allowed employers to compulsorily retire employees when they reached the age of 65 while also removing the power of employers to compulsorily retire employees at ages *below* 65 which had previously been legal, although exceptions applied for people in some occupations.

In 2011, the Coalition Government fully removed the right to compulsorily retire employees on the basis of their age, by abolishing the DRA.¹³³

Removing the DRA will allow some employees to continue to work after age 65 if they wish to, however many employees already had that option

While the removal of the DRA will allow some employees to continue working past the age of 65 many employees may have retired voluntarily at, or under, age 65 regardless of the presence of the DRA. Furthermore, not all employers made use of the DRA before it was removed; less than half the workforce worked in an organisation with a compulsory retirement age before the abolition of the DRA.¹³⁴

Even when it was legal to compulsorily retire employees at age 65, people were allowed to request to work on beyond age 65 and around 80% of requests to stay on were accepted by employers.¹³⁵ In 2009, according to research commissioned by Age UK, around 100,000 people were made to retire at or over the age of 65 under DRA legislation.¹³⁶ Therefore, the removal of the DRA is likely to affect a minority of people who would like to work after age 65 but whose employers might not have allowed them to under the previous system. However, it is possible that in future many more employees will wish to work beyond the age of 65 than do so today. In future, the absence of the DRA may remove a barrier for a larger number of employees who wish to or need to work for longer.

The USA removed the right to compulsorily retire employees on the basis of age during the 1970s and 1980s. The following case study investigates the effects this had on employment rates and highlights the lessons that the US experience may have for the UK.

¹³³ The Employment Equality (Repeal of Retirement Age Provisions) Regulations 2011

¹³⁴ Metcalf, Meadows (2010)

¹³⁵ Sykes *et. al.* (2010)

¹³⁶ AGE UK (2010)

International Case Study: USA - 25 years after the removal of mandatory retirement ages

USA - relevant statistics:¹³⁷

- **Pensionable Age** - 66 from 2008, rising to 67 by 2022 (UK - equalising at 65 then rising to 66 by 2020, 67 by 2026, then 68 by 2046 at the latest)
- **Average life expectancy at age 65** - 84 (UK - 84)¹³⁸
- **% GDP spent on state pension** - 6% (UK - 6.9%)
- **Average age of labour market exit for men** - 66 (UK - 64)¹³⁹

The USA removed mandatory retirement in a phased process between the late 1970s and 1986

In 1986 the USA became one of the first countries to outlaw mandatory retirement on the basis of age,¹⁴⁰ as a result of pressure from lobbying groups, a desire to tackle age discrimination in the workplace and the financial pressures on the state pension funding as a result of an ageing population.¹⁴¹ In the 1960s and 1970s between 40% and 50% of men in the USA worked for an employer who had a mandatory retirement age.¹⁴²

Removing the option for employers to use mandatory retirement ages increased employment for those aged 65 to 70 by between 10% and 20%

Research which allowed for other factors affecting labour force participation in the USA, shows that labour market participation by those aged 65 to 70 rose by between 10% and 20% during the 1980s as a direct result of the phasing out of Mandatory Retirement.¹⁴³ There is evidence that abolishing Mandatory Retirement has somewhat smoothed out the historical spike of retirement at age 65.¹⁴⁴

Some employers made changes to their pension arrangements to encourage older workers to retire

There is some evidence that after the removal of Mandatory Retirement, employers in the USA initially started using private pensions to encourage employees to retire by lowering Normal Pension Ages and increasing the generosity of early retirement options.¹⁴⁵ However this changed during the late eighties as a result of economic pressures on companies that provide pensions to their employees, and employers began to reduce the generosity of early retirement options.¹⁴⁶

¹³⁷ OECD (2011) OECD figures are used in order to make comparisons across countries on a consistent basis, internal country statistics may vary from OECD stats.

¹³⁸ OECD (2011)

¹³⁹ OECD (2011)

¹⁴⁰ Exceptions applied to certain employees for example, those in the armed services, aviation, judicial and safety industries

¹⁴¹ Wachter (2009)

¹⁴² Wachter (2009)

¹⁴³ Wachter (2009)

¹⁴⁴ Wachter (2009)

¹⁴⁵ Wachter (2009)

¹⁴⁶ Wachter (2009)

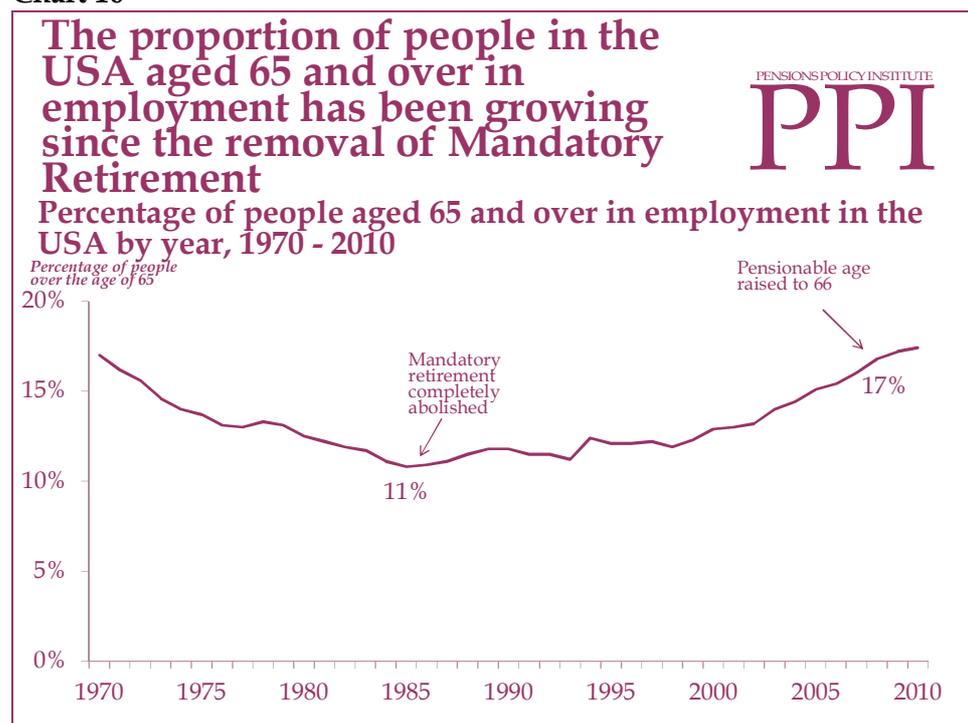
Pension arrangements continue to affect retirement decisions in the USA

Changes to pension arrangements are continuing to impact work and retirement decisions in the USA: in particular the shift from Defined Benefit to Defined Contribution pensions is changing the way many people access their private pension savings¹⁴⁷ and the amount of income people expect to receive. This means that some people may be working longer in order to ensure they have a sufficient pension or other savings and assets to finance their retirement.

Pension arrangements are only one among a number of factors impacting the decisions people in the USA make about retirement

The employment rate among older people in the USA has been growing since the 1980s (Chart 10) due to many factors, including the removal of mandatory retirement, but also because of trends similar to those experienced in the UK, such as the shift from DB to DC pensions, increases in longevity and healthy longevity and the trend for more people to need to work longer from economic necessity.¹⁴⁸

Chart 10¹⁴⁹



¹⁴⁷ Anderson *et. al.* (1997)

¹⁴⁸ Boston College, Center for Retirement Research (2008) A Micro-Level Analysis of Recent Increases in Labour Force Participation Among Older Workers <http://crr.bc.edu/>

¹⁴⁹ Data from United States Department of Labor, Bureau of Labor statistics using data from the Current Population Survey, www.bls.gov

Conclusions and lessons for the UK from the US experience

Lifting the mandatory retirement age has contributed to increases in employment at older ages in the USA. However there are many other factors also playing a role. Economic changes, changes to pension arrangements and increasing the Pensionable Age are likely to also contribute to current and future increases in employment at older ages. The USA has put in place safeguards which enable individuals to take their state pension early, at a reduced rate.

Efforts to tackle age discrimination in the workplace in the UK

2006 legislation tackling age discrimination could make working at older ages easier for some employees

Age discrimination can manifest itself through the decisions employers make regarding recruitment, promotion, pay rises, redundancies, offers of training, supervision and other support, and the general treatment of older people in the workplace. Around 40% of older employees report having experienced age related discrimination at work.¹⁵⁰ Recognising that age discrimination represents a barrier to the success of a policy agenda which aims to extend working lives, the previous Labour Government brought in legislation designed to tackle age discrimination in the work-place in 2006, (the Employment Equality Age Regulations 2006 (EEAR)) alongside the introduction of the DRA.

EEAR and the introduction of the DRA have led to some change among employers regarding redundancies and performance management policies

There is no available data on the effect of the EEAR on redundancies for workers over the age of 65 as the DRA was still in force during the most recent surveys measuring the impact of the EEAR. However, the EEAR and the introduction of the DRA do appear to have had some effect on reducing redundancies linked to ages below 65, and has prompted growth in formal performance management policies and equal opportunities policies.¹⁵¹ Around 32% of organisations, employing 55% of the workforce, were found to have changed some of their policies or practices as a result of the EEAR. Positive age related changes were least common in smaller organisations, private sector organisations and the construction industry.¹⁵²

The Government has introduced an initiative aimed at encouraging employers to adopt more age positive policies

In 2001, as part of the wider policy strategy aimed at extending working lives and enabling people who are dependent on state benefits to return to employment (the Welfare to Work campaign) the previous Labour

¹⁵⁰ Macleod *et. al.* (2010)

¹⁵¹ Metcalf, Meadows (2010)

¹⁵² Metcalf, Meadows (2010)

Government introduced the Age Positive Initiative. The Age Positive Initiative is the responsibility of the DWP and aims to *“raise employer’s awareness and change attitudes and culture through highlighting the business benefits of an age diverse workforce.”*¹⁵³

The Age Positive initiative focuses mainly on providing sector bodies with guidance and research in order to encourage them to take Age Positive codes of practices, initiatives and policy documents forward under their own branding. For example, in 2009 the Institute of Directors published *‘A Director’s Guide: Extending working lives. How businesses can benefit from the skills of an ageing workforce’*,¹⁵⁴ which drew on Age Positive information and support.

There is still age discrimination in employment, and some employers may have to work to ensure they are complying with the EEAR

Despite the EEAR and the Age Positive Initiative, discrimination at older ages continues to remain a barrier to work for older employees, especially in the areas of recruitment and offers of training and skill development. This could be the result of a lack of awareness among managers regarding their own organisations policies, and can manifest itself through a lack of awareness or understanding on the part of managers and employers of the needs of older people, or a lack of willingness on the part of employers to adapt, for example, by offering more flexible working options.¹⁵⁵

New Zealand implemented an extending working lives policy approach similar to the one currently being deployed in the UK

New Zealand implemented a policy approach to extending working lives which contained policies that are similar to the ones being deployed in the UK: raising the State Pension Age (SPA), removing default retirement and attempting to tackle barriers to working at older ages. The following case study investigates the effects these policies had on employment rates and the labour market, and highlights the lessons that the New Zealand experience has for the UK.

¹⁵³ <http://statistics.dwp.gov.uk/asd/asd5/agepositive.asp>

¹⁵⁴ www.director.co.uk/content/pdfs/EWL_Jul09.pdf

¹⁵⁵ Macleod *et. al.* (2010)

International Case Study 3: New Zealand - A three strand policy approach to extending working lives

New Zealand – relevant statistics:¹⁵⁶

- **Pensionable Age** – 65 (UK – equalising at 65 then rising to 66 by 2020, 67 by 2026, then 68 by 2046 at the latest)
- **Average life expectancy at age 65** – 84 (UK – 84)¹⁵⁷
- **% GDP spent on state pension** – 4.3% (UK – 6.9%)
- **Average age of labour market exit for men** – 67 (UK – 64)¹⁵⁸

New Zealand instituted a multi-strand policy approach to extending working lives in the 1990s, similar to the policy approach being pursued in the UK

New Zealand began to tackle the issue of the need to extend working lives before many other countries as part of a drive to ensure the sustainability of the state pension. The three-pronged policy approach that New Zealand used in the 1990s is similar to the one the UK is currently implementing. The policy approach in New Zealand included the following:

- Mandatory retirement on the basis of age was made illegal in a staged process between 1993 and 1999.
- The New Zealand Pensionable Age (the age at which people are eligible to claim a full state pension) was increased from age 60 to age 65 between 1992 and 2001.
- The removal from 1998 of taxation on non-state pension income (which had been in effect since 1985).
- The New Zealand Positive Ageing Strategy was introduced in 2001 and focussed specifically on eliminating ageism in the workplace and the promotion of flexible work options to enable older people to work for longer.¹⁵⁹

Working at older ages has been increasing in New Zealand

Since the three policies were implemented in the 1990s, working at older ages has increased substantially in New Zealand. People who are aged 60 to 64 have seen the most dramatic increase in participation rates probably owing, at least partially, to the rise in Pensionable Age from age 60 to age 65. In 1990, 26% of people aged 60 to 64 in New Zealand were in employment. By 2000, this had risen to 46% and by 2010, 70% of people aged 60 to 64 in New Zealand were in employment (Chart 11).¹⁶⁰

¹⁵⁶ OECD (2011) OECD figures are used in order to make comparisons across countries on a consistent basis, internal country statistics may vary from OECD stats.

¹⁵⁷ OECD (2011)

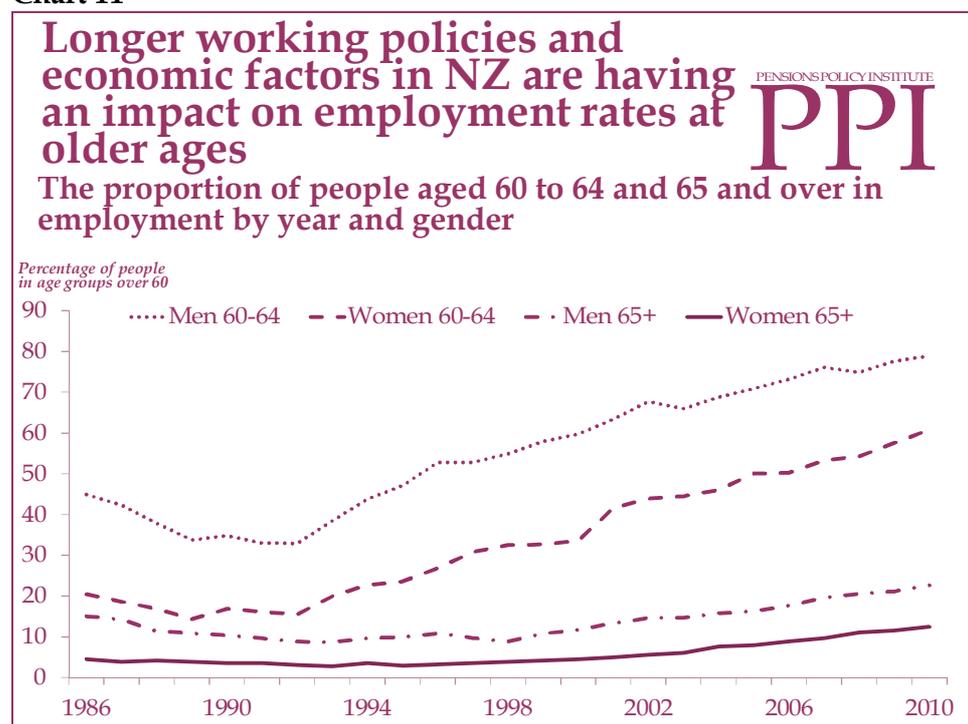
¹⁵⁸ OECD (2011)

¹⁵⁹ www.msd.govt.nz/about-msd-and-our-work/publications-resources/planning-strategy/positive-ageing/goals-and-actions.html

¹⁶⁰ New Zealand Government statistics using the Household Labour Force Survey (HLF), Annual December data, www.stats.govt.nz/infoshare/Default.aspx

Labour market participation for people over age 65 has increased as well, at least partially as a result of rises in the SPA, the removal of mandatory retirement and changes in employment policy.¹⁶¹ However other factors have played a significant role in increasing participation at older ages such as: a skills shortage facing employers; a decrease in the taxes charged for those who earn income as well their pension; improvements in health; an increase in the availability of work which is not too physically taxing; and the incentive to work inherent in a system with little means-testing.¹⁶² In 1990, 7% of those over age 65 were in employment, which rose to 17% by 2010 (Chart 11).

Chart 11¹⁶³



The policy changes have prompted New Zealand employers to offer more flexible working options to older employees

One of the impacts of the extending working lives policy approach in New Zealand has been an increase in options for flexible working. Flexible transitions into retirement have become common in New Zealand, with around 75% of those in their early to mid-sixties experiencing some form of phased transition into retirement, many of whom went from full-time to part-time work before retiring.¹⁶⁴

¹⁶¹ New Zealand Department of Labour (2007)

¹⁶² New Zealand Department of Labour (2007)

¹⁶³ New Zealand Government statistics using the Household Labour Force Survey (HLF), Annual December data, www.stats.govt.nz/infoshare/Default.aspx

¹⁶⁴ Dixon (2008)

Conclusions and lessons for the UK

New Zealand began to tackle the issue of the need to extend working lives before many other countries. The three strand policy approach that New Zealand used in the 1990s is similar to the one the UK is currently implementing. Since the three policies were implemented in the 1990s working at older ages has increased dramatically in New Zealand. One of the impacts of the extending working lives policy agenda in New Zealand has been an increase in options for flexible working.

However, economic factors also contributed to the high rates of working at older ages in New Zealand, in particular, the skills shortage. The UK has a more open approach to immigration, meaning that employers in the UK may have more access to workers when skills shortages arise. Therefore it is not clear that the UK would see such dramatic improvements in the proportion of older people in work.

Conclusions

The Government has implemented a range of policies and programmes aimed at extending working lives, including

- policies aimed at moving people off benefits and into paid work;
- changes to the age at which people can receive the state pension and benefits income;
- the removal of barriers to working longer, including the removal of legal barriers and efforts to tackle age discrimination in the workplace.

While all of these policies will encourage and enable some people to work longer and take their state and private pension later, there may be negative financial implications for those who cannot work longer because of health problems, or other factors. For those who are unable to work longer, rises to the State Pension Age and changes to the benefit system may result in lower incomes in retirement.

Chapter three: how much longer might individuals need to work and save in order to meet target levels of retirement income?

This chapter analyses how working and retirement patterns could impact on future levels of income adequacy for people in retirement.

How long would people need to work in order to achieve adequacy in retirement?

This analysis investigates how long people aged between 50 and State Pension Age (SPA) in 2011 and still in work,¹⁶⁵ might need to continue working and saving at current levels in order to meet two different measures of income adequacy:

- The **Minimum Income Standard**, which calculates how much income pensioners require to meet a *minimum acceptable standard of living*,¹⁶⁶ is just under £11,000pa (£211pw) for a single pensioner Before Housing Costs (BHC), and around £15,700pa (£303pw) for a couple in 2011.¹⁶⁷ For people who have lived on medium to high incomes during working life, the minimum acceptable standard of living may not seem adequate as it would generally constitute a drop in living standards.
- **Working life replacement rates** which calculate how much income an individual pensioner might need in order to achieve a similar standard of living to the one they had in working life, are generally in the range of 50% to 80% of people's gross working life income. Lower income individuals have higher replacement rates than higher income individuals as their income may be closer to the levels required to meet basic needs. A median-earning man with a weekly income at the point of retirement of around £500pw¹⁶⁸ might need a gross weekly retirement income of around £17,400pa (£335pw) to meet a 67% replacement rate of working life income (and recreate working life living standards).¹⁶⁹

¹⁶⁵ Data from the English Longitudinal Study of Ageing WAVE 3, based on data collected in 2006/2007

¹⁶⁶ As defined by Pensioners in focus groups, see www.minimumincomestandard.org for further information on how the Minimum Income Standard is calculated

¹⁶⁷ Calculated using www.minimumincome.org.uk and deducting rent and water rates

¹⁶⁸ Median non-age specific earnings, Labour Force Survey, Oct - Dec 2011, EARN04: Gross weekly earnings of full-time employees (last updated February 2012) www.ons.gov.uk/ons/publications/reference-tables.html?edition=tcn%3A77-222482

¹⁶⁹ Pensions Commission (2004) and PPI calculations

Table 4: Assumed target replacement rates needed to replicate working life living standards by income in working life (2011 earnings terms)¹⁷⁰

Income in working life	Target replacement rate
Less than or equal to £11,540	80%
£11,541 - £21,250	70%
£21,251 - £30,360	67%
£30,361 - £60,720	60%
£60,721 or greater	50%

Although replacement rates are higher for low income individuals, they may generally find it easier to meet replacement rate targets as a larger proportion of their retirement income is derived from state pensions. Higher earning individuals who do not meet their target replacement rate will not necessarily have incomes that might be considered low. For example, they may still have incomes well above poverty levels.

The analysis only compares state pension and benefits and private pension income against the target income thresholds. In reality, individuals (and in particular higher income individuals) may have other assets, such as savings or housing wealth that they may be able to use to help meet target income levels.

A key assumption of this analysis is that individuals who are aged between 50 and SPA in 2011 and are still working, continue in work, and continue to earn and contribute into their pensions at current levels (allowing for growth in average earnings) until they reach target levels of income.

The analysis also assumes that those who are not currently saving into a pension are, if eligible, auto-enrolled in 2012 and contribute at the minimum required levels. In reality, for various reasons, including health problems, caring responsibilities and lack of available and appropriate employment, not everyone aged 50 and above will be able to continue working and saving until or beyond their SPA.¹⁷¹

¹⁷⁰ Pensions Commission (2004) and PPI calculations

¹⁷¹ The impact on the results of assuming that all individuals retire two years before SPA are shown in the Modelling Appendix

Box 3: Uses and limitations of scenario analysis

Scenarios are useful to explore outcomes on the basis of certain assumptions (i.e. to answer questions like: *What would happen if everyone worked and saved at current levels up until their State Pension Age?*). These scenarios are intended as illustrative rather than as forecasts. We do not estimate the likelihood of each scenario occurring.

The projections illustrated in this paper should not be taken as forecasts. The analysis seeks to illustrate the potential impact of working and saving behaviour. However, the decisions that people make and their incomes in retirement will be impacted by personal circumstances (e.g., health, caring responsibilities), employer factors (e.g., the availability of appropriate work), pension provision (e.g., the performance of funds, whether people opt out of pension saving), changes in the structure of the state pension and means-tested benefits system (e.g., impact of the single-tier pension and changes to welfare). If a forecast were to be made of levels of income adequacy among future pensioners, it would need to allow for factors that are not allowed for in this paper.

Further details of the methodology and assumptions used in this analysis, and analysis of the sensitivity of results to key assumptions are contained in the Modelling Appendix to this report.

All of the results shown in this chapter have been rounded to the nearest 5%. Totals may not sum to 100% because of this rounding.

The analysis only covers those in work, or with a partner in work

The following results are based on analysis of the English Longitudinal Study of Ageing (ELSA), so findings apply to England only.

The analysis focuses on individuals aged between 50 and State Pension Age (SPA) who are either in work, or who have a partner who is in work at the time they were interviewed. Of the individuals in the ELSA data aged between 50 and SPA, 80% fall into this category. The remaining 20% of cases are not included in this analysis, as it is unlikely that a majority of these people will enter work again and so working longer is not likely to affect their retirement incomes.

The English population in 2011 aged between 50 and SPA is estimated to be around 7.9 million.¹⁷² The sample used in this project broadly represents 80% of people aged between 50 and SPA, or approximately 6.3 million people.

¹⁷² ONS 2010-based subnational population projections

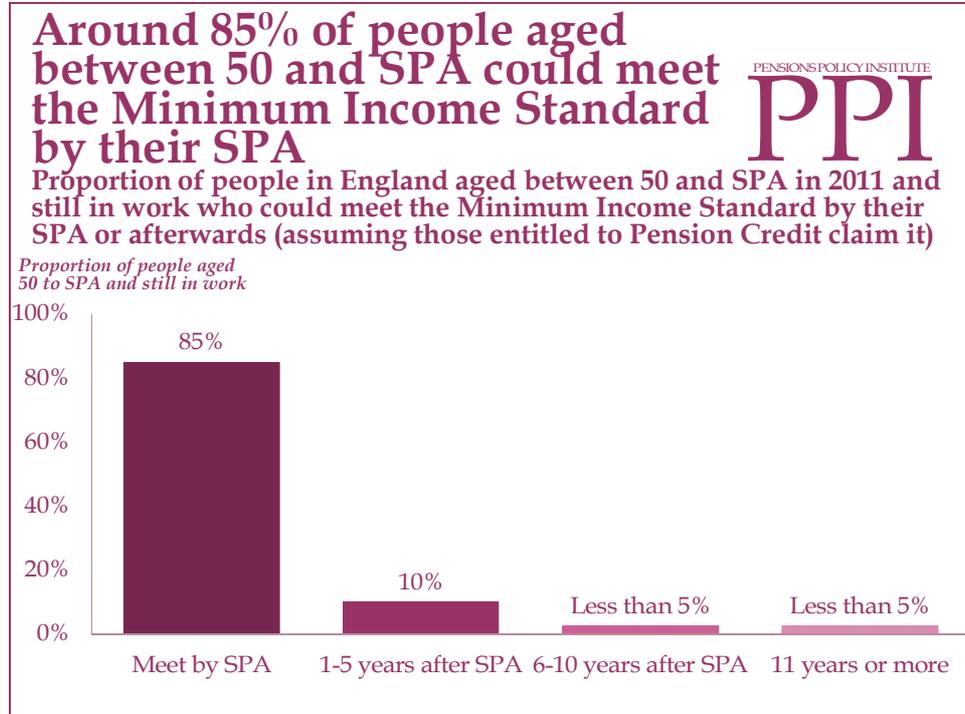
How long will people need to work to meet a basic minimum standard of living in retirement and to replicate working life living standards?

Based on the above assumptions the next section of this report considers how many individuals may be able to meet the Minimum Income Standard from state and private pension savings.

Around 85% of people aged between 50 and State Pension Age in 2011 and still in work could have sufficient state and private pension income to meet the Minimum Income Standard by State Pension Age

- The vast majority, around 85%, (Chart 12) of those aged between 50 and SPA in 2011 and still in work might have sufficient state and private pension income to meet the Minimum Income Standard (calculated to be £211pw for a single pensioner Before Housing Costs (BHC), and £303pw for a couple in 2011)¹⁷³ by SPA assuming that they continue to work and save until SPA and that everyone who is entitled to means-tested benefits claims them.
- Around 10% of those aged between 50 and SPA in 2011 and still in work will only be able to meet the Minimum Income Standard if they continue to work and save for a further one to five years after SPA.
- Around 5% of those aged between 50 and SPA in 2011 and still in work might need to work for six years or more after their SPA in order to meet the Minimum Income Standard.

Chart 12¹⁷⁴



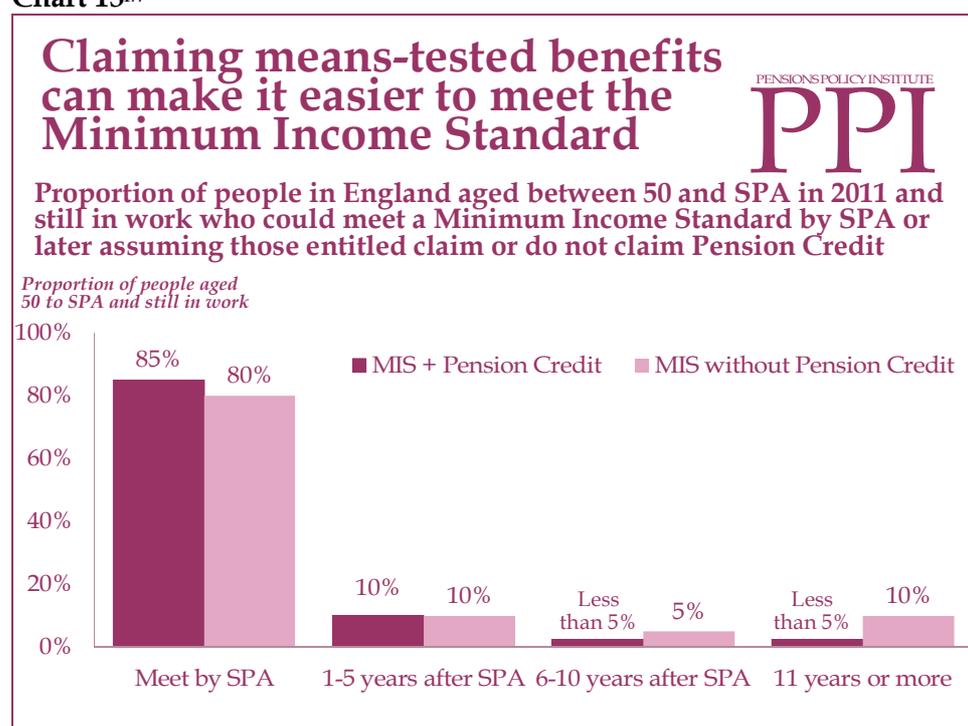
¹⁷³ Calculated using www.minimumincome.org.uk and deducting rent and water rates

¹⁷⁴ PPI Dynamic Model - numbers may not sum to 100% due to rounding

This reason so many people are able to meet the Minimum Income Standard is that people who have very low incomes in retirement are generally eligible to receive some support from the state through means-tested benefits. Someone who receives the maximum rate of Guarantee Credit of £138pw, average Housing Benefit and Council Tax Benefit would have an income of £211pw,¹⁷⁵ which is at or just above the Minimum Income Standard. Those who don't have incomes at or above the Minimum Income Standard tend to have assets that exclude them from eligibility for means-tested benefits.

The above analysis assumes that all those eligible for Pension Credit claim it. However, around one million of the four million people in the UK who are entitled to Pension Credit do not claim it¹⁷⁶ and may therefore be living on an income below the Minimum Income Standard level. The following analysis illustrates the difference that claiming Pension Credit can make for the income adequacy of individuals (Chart 13).

Chart 13¹⁷⁷



Means-tested benefits can play an important role in helping those on low incomes during working life achieve minimum acceptable standards of living in retirement

Around 85% of people currently aged between 50 and SPA in 2011 and still in work could meet the Minimum Income Standard by SPA if it is assumed that everyone who is eligible for Pension Credit claims it (Chart

¹⁷⁵ www.minimumincome.org.uk/

¹⁷⁶ www.ageuk.org.uk/money-matters/claiming-benefits/pension-credit/

¹⁷⁷ PPI Dynamic Model - numbers may not sum to 100% due to rounding

13). However, if it is assumed that no one claims Pension Credit then only 80% of people aged between 50 and SPA in 2011 and still in work could meet the Minimum Income Standard by SPA (Chart 13).

Claiming Pension Credit allows a further 5% of those aged between 50 and SPA in 2011 and still in work to achieve the Minimum Income Standard by SPA, showing that means-tested benefits can play an important role in helping those on low incomes during working life achieve minimum acceptable standards of living in retirement.

Box 4: Adequacy and the Minimum Income Standard

The Minimum Income Standard level will not necessarily be high enough to provide the minimum acceptable standard of living to everyone

- Those with health problems or who live in rural areas¹⁷⁸ may require a higher income to achieve a minimum acceptable standard of living.
- For those who have lived on a higher income during working life the minimum acceptable standard of living is unlikely to *feel* acceptable as it will represent a drop in living standards.
- Many people who receive a level of income equal to or above the Minimum Income Standard may forgo some essentials because of spending in other areas (either discretionary spending on leisure goods or necessary spending, for example, supporting dependents, health related spending or spending on emergencies).

Therefore, just because someone meets the Minimum Income Standard it cannot necessarily be assumed that they are not suffering from deprivation in some capacity.

It will be harder for people to meet target replacement rates than the Minimum Income Standard

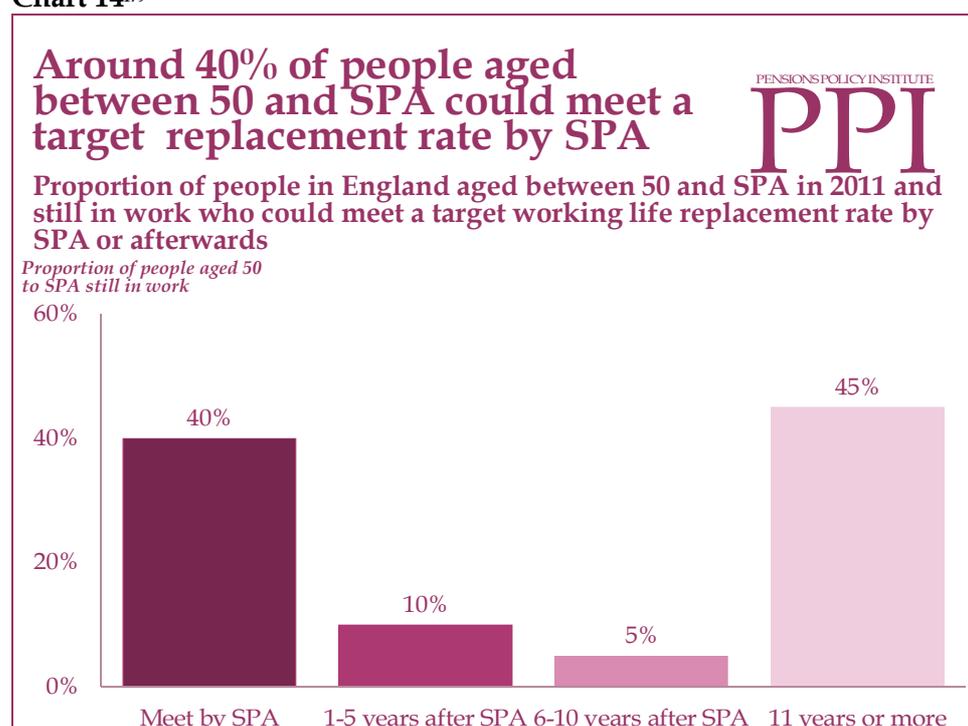
Fewer people will be able to meet a target replacement rate of working life income that would allow them to replicate working life living standards, by their SPA. The exact percentage of working life income needed to meet a target replacement rate varies for each individual depending on their income (Table 4).

If it is assumed that people aged between 50 and SPA in 2011 and still in work, continue to work and save at their current levels, then:

- By SPA, around 40% of those aged between 50 and SPA in 2011 and still in work might have sufficient state and private pension income to meet a target working life replacement rate (Chart 14).
- Around 10% of those aged between 50 and SPA in 2011 and still in work may be able to meet their target replacement rate if they continue to work and save for a further one to five years after SPA.

¹⁷⁸ Because of higher transportation costs and less access to discount shops and services

- Around 5% of those aged between 50 and SPA in 2011 and still in work may be able to meet their target replacement rate if they continue to work and save for a further six to ten years after SPA.
- Around 45% of those aged between 50 and SPA in 2011 and still in work, might need to work and save for 11 or more years after their SPA in order to meet a target replacement rate of working life income.

Chart 14¹⁷⁹

The above analysis shows how close people could come to meeting their target replacement rates through state and private pension income and means-tested benefits. However, some of these people may have other income and assets in retirement which would allow them to meet their target replacement rates when combined with their state and private pension income.

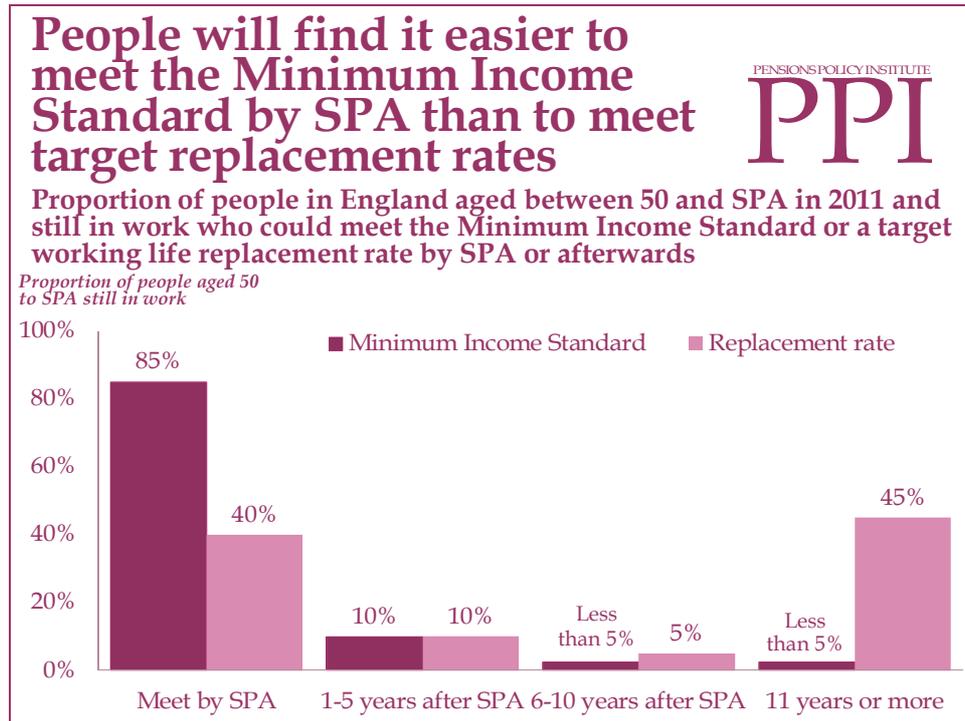
It will be easier for people to meet the Minimum Income Standard by SPA or during retirement than to meet target replacement rates

Overall it will be easier for people to meet the Minimum Income Standard (£211pw for a single pensioner (BHC); £303pw for a couple in 2011)¹⁸⁰ in retirement through state and private pension income than target replacement rates which are likely to be higher at between 50% to 80% of an individuals working life income (Chart 15).

¹⁷⁹ PPI Dynamic Model – numbers may not sum to 100% due to rounding

¹⁸⁰ Calculated using www.minimumincome.org.uk and deducting rent and water rates

Chart 15¹⁸¹



People with different characteristics may be more or less likely to be able to meet their target replacement rates from state and private pension income by State Pension Age (SPA). The next section of this chapter explores how different characteristics such as income level, gender, and type of pension savings can impact people’s likelihood of meeting their target replacement rate by their SPA.

Those in lower income quartiles may be more able to meet a target replacement rate of working life income by State Pension Age

The following analysis shows how long people from different income quartiles may need to work and save in order to have sufficient state and private pension income to meet a target replacement rate by SPA or after their SPA.

It may be easier for people with very low incomes to meet a target replacement rate of working life income because their target will be much lower than the target of someone who had a high income during working life. For example,

- The income of an individual in the bottom quartile would be equivalent to around £14,000pa or below and their target replacement rate would be 70% of this income at £9,800pa or below (however, as this is lower than the Minimum Income Standard (£11,000pa) this individual would in this analysis have their target replacement rate increased to meet the Minimum Income Standard).

¹⁸¹ PPI Dynamic Model - numbers may not sum to 100% due to rounding

- The income of an individual in the top quartile would be equivalent to around £35,000pa or above and their target replacement rate would be 60% of this income at £21,000pa or above.

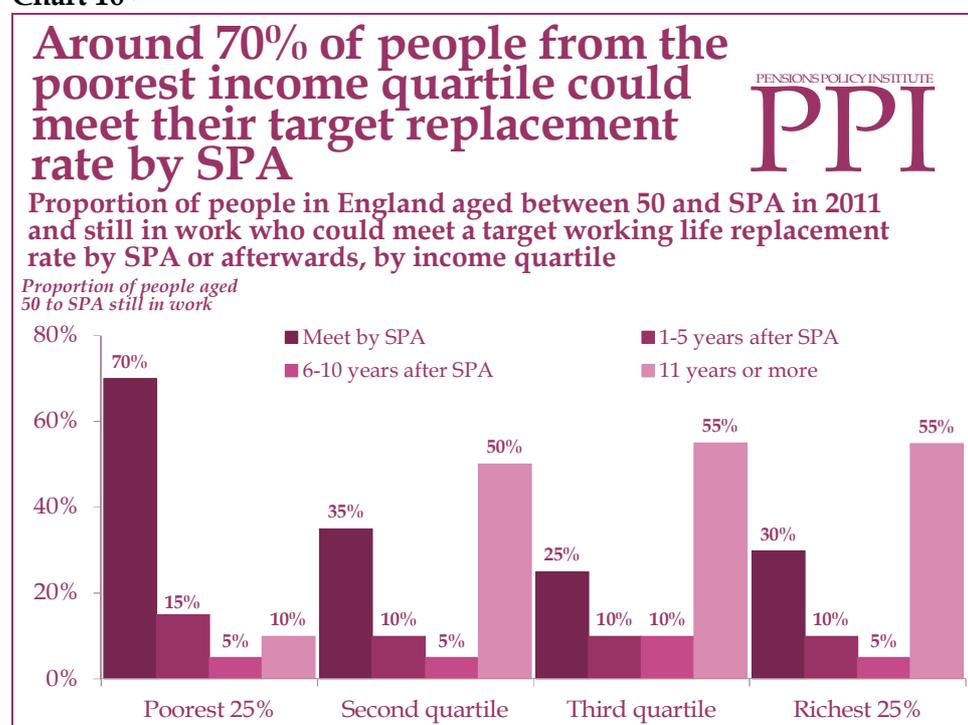
Chart 16¹⁸²

Chart 16 shows that:

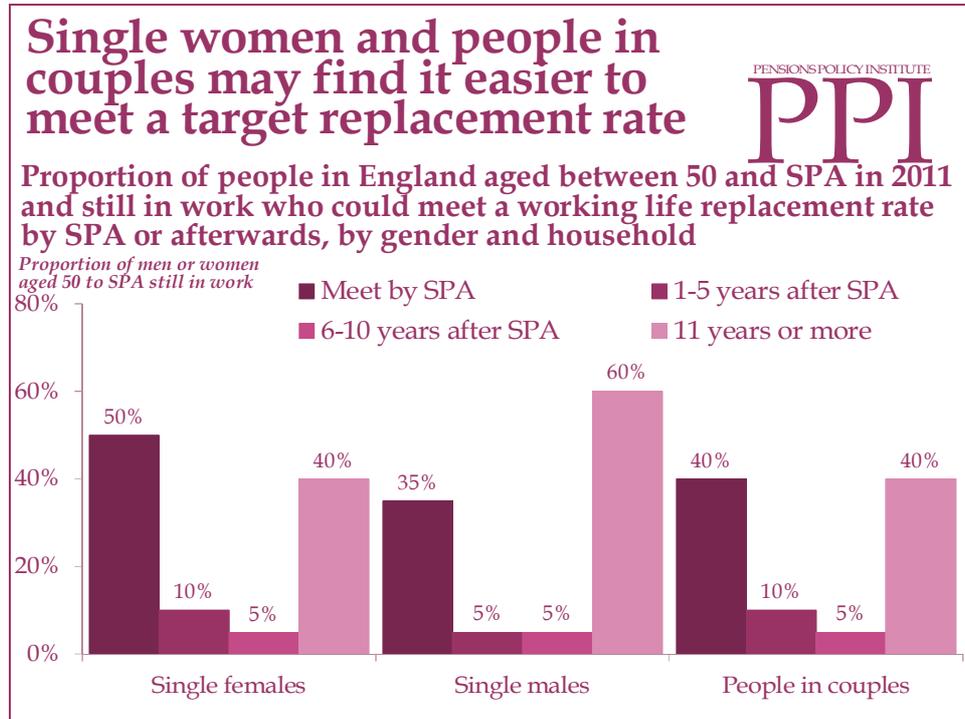
- Around 70% of those aged between 50 and SPA in 2011 and still in work in the lowest income quartile could have sufficient state and private pension income to meet a target replacement rate by SPA. They are likely to have much lower target replacement rates which they are more able to meet with state pension and means-tested benefits income.
- Only around 30% of people aged between 50 and SPA and still in work in the highest income quartile could meet their target replacement rates (which are likely to be at a much higher income level than those in lower income quartiles) by SPA. In order for those in higher income quartiles to be able to meet their replacement rates, they may need to supplement their state pension (and any state benefits) income and income from private pension with income from other savings and assets, which people in higher income quartiles are more likely to have.

¹⁸² PPI Dynamic Model - income quartiles of benefit units who qualify (by being aged between 50 and SPA in 2011 and still in work) derived from ELSA data using PPI calculations - numbers may not sum to 100% due to rounding

Single women and people in couples are more likely to meet a target replacement rate than single men

Chart 17 shows how many people aged between 50 and SPA in 2011 and still in work may be able to meet their individual target replacement rates by SPA and afterwards.

Chart 17¹⁸³



Single women and people in couples are more likely to meet a target replacement rate by SPA than single men.

- Around 50% of single women might have sufficient state and private pension income to reach a target replacement rate of working life income by their SPA, compared with around 35% of single men.
- Around 40% of single women and around 60% of single men might need to work and save for 11 years or more after their SPA to be able to reach a target replacement rate of working life income, compared with around 40% of people in couples.

Women are often earning at lower levels than men and will therefore have lower target replacement rates, making their target replacement rates easier to achieve through state pension, benefit income and minimal pension savings. For example, the median weekly income for a woman in 2011 is around £400pw and for a man in 2011 is around £500pw.¹⁸⁴ The target replacement rate for a median earning woman would be 70% of her

¹⁸³ PPI Dynamic Model - numbers may not sum to 100% due to rounding

¹⁸⁴ Median non-age specific earnings, Labour Force Survey, Oct - Dec 2011, EARN04: Gross weekly earnings of full-time employees (last updated February 2012) www.ons.gov.uk/ons/publications/reference-tables.html?edition=tcm%3A77-222482

income, at around £14,600pa (£280pw) and for a median earning man would be 67% of his income, giving a higher income requirement of around £17,400pa (£335pw). People with very low incomes during working life may be able to meet a target replacement rate through means-tested benefits, and this may disproportionately represent single women.

People in couples may find it easier than single men to meet a replacement rate of working life income as they may be able to supplement their pension income with income from the earnings, savings or pensions of their partner.

- Only around 40% of people in couples may need to work and save for 11 years or more after their SPA to have sufficient state and private pension income to reach a target replacement rate of working life income, compared with around 60% of single men.

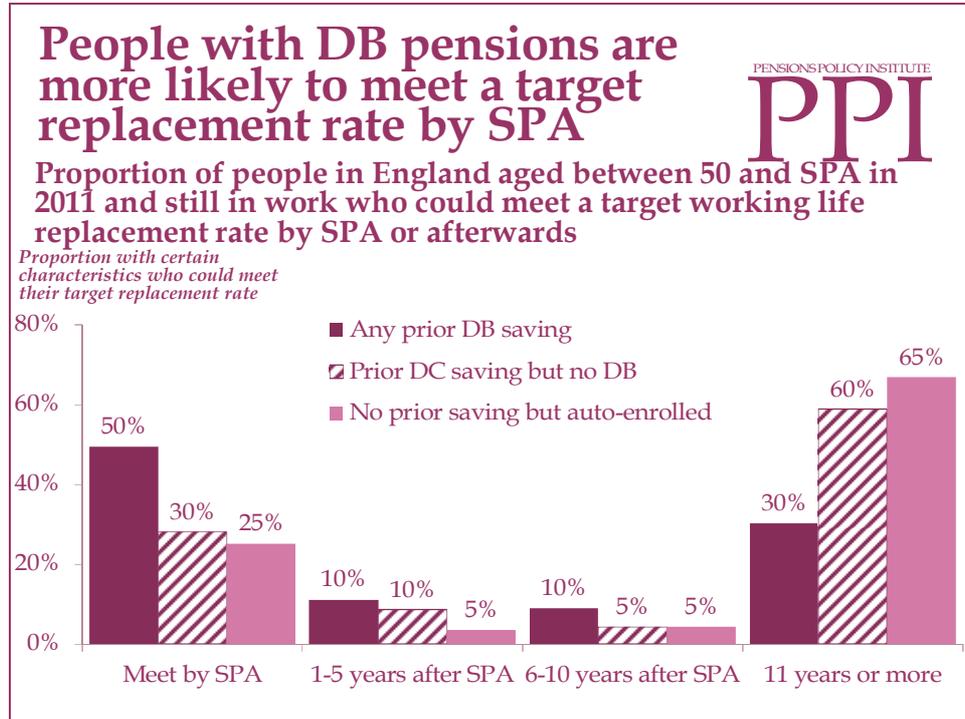
However, this is based on the position at the point of retirement, and only considers the joint income while both partners in a couple are alive. Widow(er)s may have lower incomes in retirement after bereavement. These findings are also based on both partners making a joint retirement decision and retiring at the same time.¹⁸⁵

¹⁸⁵ The impact of assuming that partners in a couple make individual retirement decisions based on individual incomes is shown in the Modelling Appendix

People with Defined Benefit pension savings might find it easier to meet a target replacement rate in retirement

Chart 18 illustrates the proportions of people with different levels and types of pension saving who could meet a target replacement rate by SPA or after.

Chart 18¹⁸⁶



People aged between 50 and SPA in 2011 and still in work who have prior Defined Benefit savings (which could also include additional Defined Contribution savings) are much more likely to be able to meet a target replacement rate.

Around 50% of those with prior DB savings could have sufficient state and private pension income to meet their target replacement rate by SPA, while only around 30% of those with prior DC savings (and no DB savings) and only around 25% of those who have no prior pension savings but are auto-enrolled at minimum levels could meet their target replacement rate by SPA.

People aged between 50 and SPA in 2011 and still in work with DB pension savings are less likely to have to work and save for long periods after their SPA in order to meet their target replacement rate. Around 30% of those with DB savings, 60% of those with DC savings (but no DB) and 65% of those with no prior pension savings before auto-enrolment

¹⁸⁶ PPI Dynamic Model - numbers may not sum to 100% due to rounding

may need to work and save for 11 years or more after their SPA in order to meet target replacement rates.

Contributing at higher levels to a pension could mean that people with Defined Contribution pensions do not need to work as long to meet their target replacement rates

DB savers have a higher chance of meeting a target replacement rate by SPA partly because they and their employers on average make higher contributions to their pensions.

The following analysis looks at people aged between 50 and 54 and in 2011 and still in work who do not have any DB savings. The analysis assumes that:

- Those who are already saving into DC pensions double their existing contributions; and,
- All auto-enrolled employees and their employers contribute at double the minimum level phased in between 2012 and 2019, (bringing their total contribution level to 16% of band earnings, including tax relief,¹⁸⁷ by 2019) and continue working and contributing until they meet their target replacement rates.

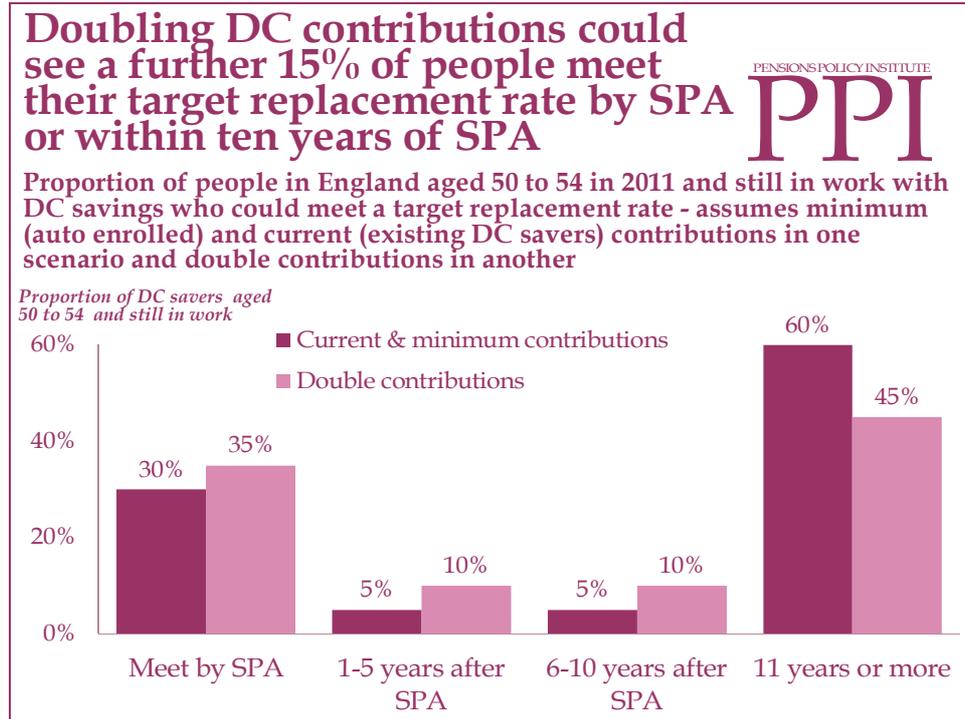
The people in this analysis are aged between 50 and 54 in 2011 and therefore have at least five to ten years to save into a pension (depending on their gender) and some have up to 15 years before their SPA in which to see some benefit from doubling their contributions.

However, this particular cohort of people will not benefit fully from the introduction of auto-enrolment. They will have already completed most of their working lives before auto-enrolment is introduced, and will also only make and receive low levels of contribution for the first few years after the introduction of auto-enrolment, as the full level of employer, employee and Government contributions will not be in place until 2019. For individuals in this cohort that are auto-enrolled, doubling contributions may have little impact as initial contribution levels are very low.

If analysis was done on people in their 20s and 30s, and it was assumed that all those who were saving in DC pensions paid double contributions, it is likely that the difference in the proportion of people able to meet target replacement by their SPA under the different scenarios would be greater, because they would have several decades in which to accrue a larger pension pot with double contributions. Younger people who are auto-enrolled will also have more years to benefit from saving at the fully phased in contribution levels.

¹⁸⁷ 8% employee, 6% employer, around 2% in tax relief

Chart 19¹⁸⁸



If it is assumed that of those aged between 50 and 54 in 2011 and still in work who are saving in a DC pension or are auto-enrolled (with no DB savings), all DC savers double their contributions and those who are auto-enrolled and their employers contribute at double the minimum level,¹⁸⁹ then 35% of these people might have sufficient state and private pension income to meet their target replacement rate by SPA compared to 30% under minimum contributions (Chart 19).

Under the double contribution scenario around 45% of those aged between 50 and 54 in 2011 and still in work (with no DB savings), may need to work and save for 11 years or more after their SPA to meet their target replacement rate. This is around 15% fewer than under the current and minimum contributions scenario.

¹⁸⁸ PPI Dynamic Model - numbers may not sum to 100% due to rounding

¹⁸⁹ bringing the total contribution level to 16% of band earnings (including tax relief) 8% employee, 6% employer, around 2% in tax relief

Conclusions

In order to examine how working longer can affect the adequacy of retirement income, the PPI has modelled the retirement income that individuals aged between 50 and State Pension Age (SPA) in 2011 might expect to achieve if they continue to work and save at current levels, up until or beyond their SPA.

This paper uses two measures of income adequacy in order to test whether pensioners might have enough income in order to meet their needs in retirement:

- The **Minimum Income Standard**, which calculates how much income pensioners require to meet the *minimum acceptable standard of living*,¹⁹⁰ and,
- **Working life replacement rates** which calculate how much income an individual pensioner might need in order to achieve a similar standard of living to the one they had in working life.

Meeting the Minimum Income Standard will be easier for people than meeting a target replacement rate of working life income:

- The vast majority, around 85%, of those aged between 50 and SPA in 2011 and still in work might have sufficient state and private pension income to meet the Minimum Income Standard by SPA assuming that everyone who is entitled to means-tested benefits claims them.
- Means-tested benefits can play an important role in helping those on low incomes during working life achieve minimum acceptable standards of living in retirement.
- Around 10% of those aged between 50 and SPA in 2011 and still in work will only be able to meet the Minimum Income Standard if they continue to work and save for a further one to five years after SPA.
- Around 5% of those aged between 50 and SPA in 2011 and still in work might need to work for six years or more after their SPA in order to meet the Minimum Income Standard.

Fewer people will be able to meet a target replacement rate of working life income that would allow them to replicate working life living standards, by their SPA:

- By SPA, around 40% of those aged between 50 and SPA in 2011 and still in work might have sufficient state and private pension income to meet a target working life replacement rate.
- Around 10% of those aged between 50 and SPA in 2011 and still in work may be able to meet their target replacement rate if they continue to work and save for a further one to five years after SPA.
- Around 5% of those aged between 50 and SPA in 2011 and still in work may be able to meet their target replacement rate if they continue to work and save for a further six to ten years after SPA.

¹⁹⁰ As defined by pensioners in focus groups

- Around 45% of those aged between 50 and SPA in 2011 and still in work, might need to work and save for 11 or more years after their SPA in order to meet a target replacement rate of working life income.

People with certain characteristics may be more or less likely to be able to meet a target replacement rate by SPA from state and private pension income:

- Those in lower income quartiles may be more able to meet a target replacement rate of working life income by SPA.
- Single women and people in couples are more likely to meet a target replacement rate than single men.
- People with Defined Benefit pension savings might find it easier to meet a target replacement rate in retirement.
- Contributing at higher levels to a pension could mean that people do not need to work as long to meet a replacement rate of working life income which would allow them to replicate working life living standards.

Chapter four: how might different patterns of work and retirement impact the pension income of individuals?

This chapter analyses how different patterns of working could affect the pre-retirement and post-retirement income of individuals who have different earnings levels.

This chapter investigates the impact of working longer and not working longer on 3 hypothetical individuals who have different earning levels and saving histories during their working life. The three individuals are outlined in boxes 5-7. The working patterns provided in the boxes are a 'baseline' scenario for each individual. The analysis examines the outcomes of different patterns of work, and then compares them to the baseline scenarios to see the impact of different working patterns on people's incomes.

Box 5: Low earning man - baseline scenario

- He is born in 1963 and begins work at age 22.
- When working, he earns at the 30th percentile of age-specific earnings for men.
- While working, he contributes to a DC pension at the average level of 9% of gross earnings (employee and employer contributions).¹⁹¹
- He retires in 2030, at his State Pension Age (SPA) of 67 under current proposed policy.¹⁹²

Box 6: Median earning woman - baseline scenario

- She is born in 1963 and begins work at age 22.
- When working, she earns at median age-specific earnings for women.
- Between the ages of 30 and 35 she takes time out of work to care for her children.
- When she returns to work, she works part-time for two years at 50% of full-time earnings, and then resumes full-time work.
- While working, she contributes to a DC pension at the average level of 9% of gross earnings (employee and employer contributions).
- She retires in 2028, two years prior to her SPA of 67 under current proposed policy and takes her private pension.¹⁹³

¹⁹¹ Average contributions to a DC occupational pension in 2010, 9% total average contribution made jointly by employer and employee, www.ons.gov.uk/ons/rel/pensions/occupational-pension-scheme-survey-annual-report/2010-annual-report/art-opss2010.html#tab-Chapter-4--Contributions-to-schemes

¹⁹² The Government announced in the Chancellor of the Exchequer's Autumn statement 2011 that they would raise the State Pension Age to 67 between April 2026 and April 2028

¹⁹³ In 2010, 35% of women between ages 55-59 had already left the labour market (ONS Pension Trends Ch4 2011). This means that currently many women do not work up until their SPA.

Box 7: High earning man - baseline scenario

- He is born in 1963 and begins work at age 22.
- When working, he earns at the 70th percentile of age-specific earnings for men.
- While working, he contributes to a DC pension at the average level of 9% of gross earnings (employee and employer contributions).
- He retires in 2030, at his SPA of 67 under current proposed policy.

Box 8: Uses and limitations of hypothetical case study analysis

Hypothetical case studies are useful for looking at how certain individuals may fare under certain assumptions, however these case studies should not be considered predictions of how any particular income group will fare in the future. Each hypothetical individual has a specific history of working and saving behaviour and the behaviour and experiences of any individual in future may be very different from those of the case study individuals.

The assumptions in these case studies are based on the state and private pension and state benefits system as it exists at the time of publishing this paper. The state and private pensions landscape may experience changes in future that are not accounted for in the assumptions in this paper.

The scenarios in the boxes above represent the baseline scenarios all other alternative scenarios will be compared against

Each individual will be considered under alternative scenarios, under which their working patterns, ages of taking their pension and ages of retirement are varied. The income that individuals receive both before and after State Pension Age (SPA) in each of these alternative scenarios will be compared to the incomes they receive under their baseline scenario.

Box 9: Individual modelling assumptions

- In order to illustrate how levels of income could differ between different scenarios, all individuals are assumed to purchase a single life, level annuity with their private pension saving. While the method people use to take income from pension savings may look very different in future, an annuity provides a good way to measure the income in different scenarios against each other, rather than as an actual projection of income.
- Everyone takes their tax free lump sum and does not use it to provide a secure income in retirement (this is the most common event in practice).
- The current state pension system and the current system of working-age benefits are both in place rather than Universal Credit and/or single-tier state pension.
- The baseline scenarios assume the SPA rises to age 66 by 2020 and rises from age 66 to age 67 between 2026 and 2028 as announced in the Chancellor of the Exchequer's Autumn 2011 statement.

How might retiring early impact on an individual's income?

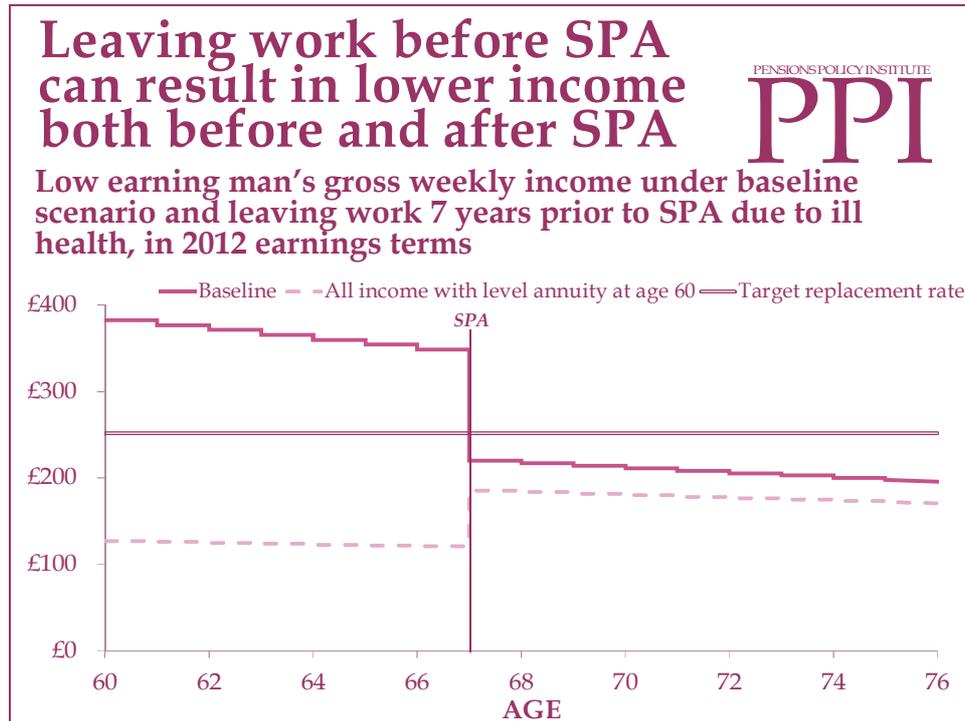
The following analysis assumes that the **low earning man** retires at age 60, 7 years before his State Pension Age (SPA) of age 67, due to a health problem which means he is no longer capable of working. The analysis assumes two different scenarios:

- the low earning man purchases a level annuity,
- the low earning man purchases an enhanced annuity on the basis of his health problems. The enhanced annuity offers an uplift of 19%¹⁹⁴ from the rate he would have received from a level annuity.

The low earning man's total gross state and private pension income under these scenarios is compared to the total gross state and private pension income under his baseline scenario in which he retires at his SPA of age 67 in 2030.

¹⁹⁴ Industry estimate of average uplift

Chart 20¹⁹⁵



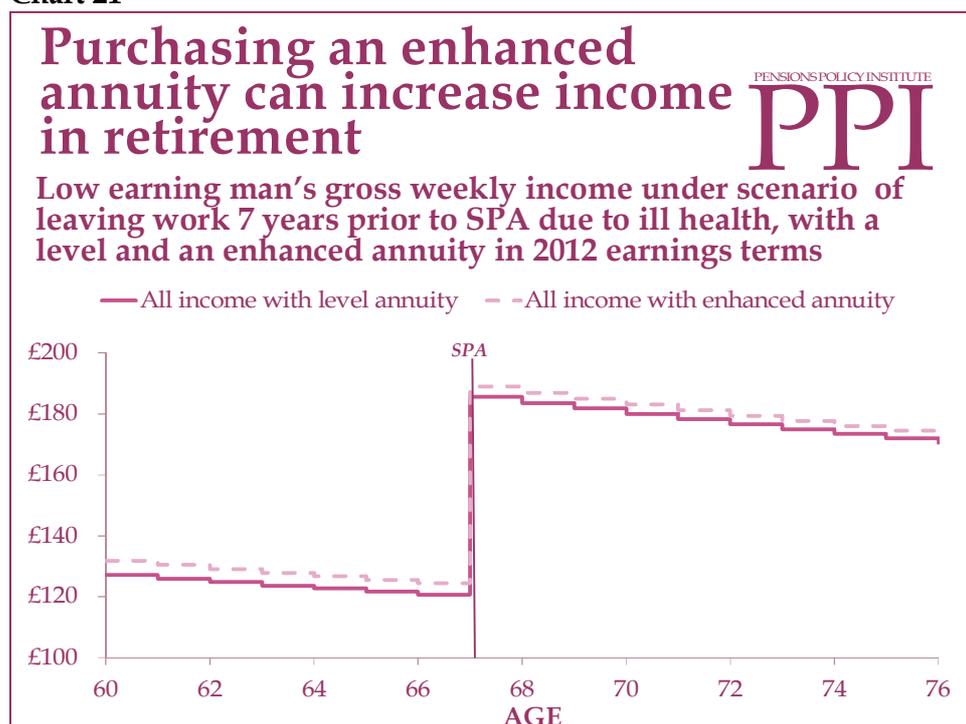
Leaving work before State Pension Age can result in lower income both before and after State Pension Age

When the low earning man is able to remain in work until his SPA of age 67 in 2030 he is able to save into his pension for longer than in the scenarios in which he has to leave work 7 years before SPA due to health reasons. Working and saving for those extra 7 years means his total gross state and private pension income at the point of retirement would be £220pw, bringing him within around £30 of his target replacement rate of around £250pw when he reaches his SPA of age 67 (Chart 20).

Under an alternative scenario, he is assumed to leave work at age 60 on grounds of ill-health. Between age 60 and his SPA of age 67, his income is considerably lower than in the baseline scenario at around £125pw. His weekly income at the point of retirement increases to around £190pw under this scenario once he can claim his state pension, which is around £60 short of his replacement rate.

If instead, the man shops around and purchases an enhanced annuity, his private pension income at the point of retirement would be around £3 higher per week than when he purchases a level annuity, an uplift of 19%, which brings him slightly closer to his replacement rate (Chart 21).

¹⁹⁵ PPI Individual Model

Chart 21¹⁹⁶

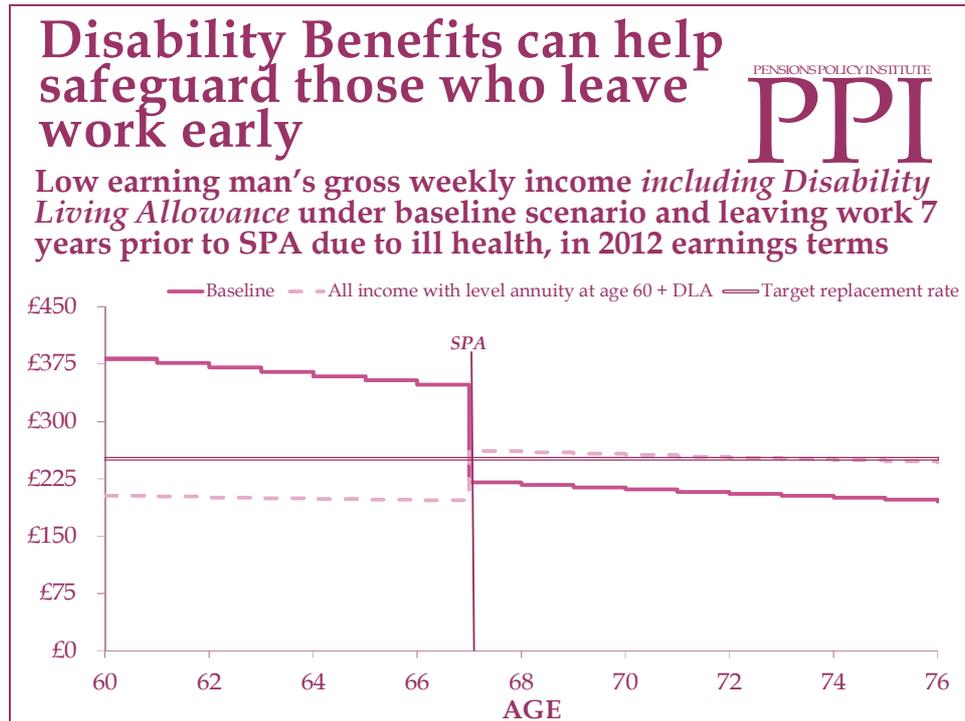
Receiving disability benefits can help those who leave work early to achieve a more acceptable standard of living

The previous analysis showed the low earning man's income without the additional disability benefits he may be entitled to. This is because disability benefits are assumed to be spent on the additional care and support needed by those with disabilities and cannot necessarily be considered as disposable income. For illustrative purposes, Chart 22 shows the low earning man's weekly income with the addition of Disability Living Allowance (DLA) of around £70pw.¹⁹⁷

¹⁹⁶ PPI Individual Model

¹⁹⁷ DLA care component, £73.60, with no mobility component, This is roughly equivalent to the average DLA award for 60-64 year olds, according to DWP data, February 2011 - DWP tabulation tool, <http://83.244.183.180/100pc/tabtool.html>

Chart 22¹⁹⁸

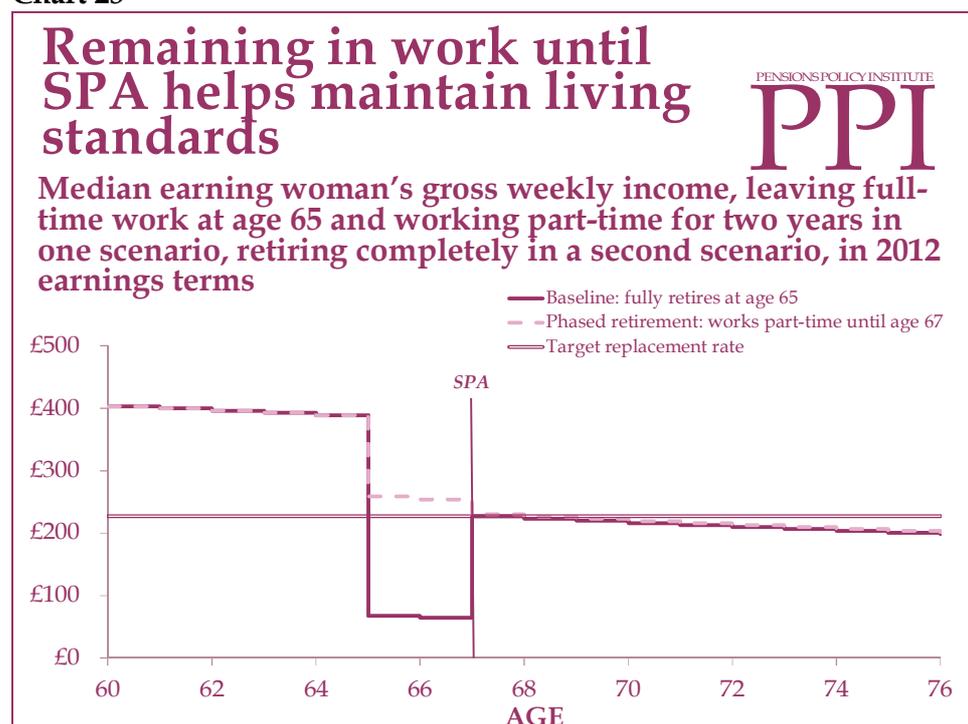


The addition of DLA brings the low earning man's total gross state and private pension income above his target replacement rate for the first 7 years after he reaches SPA and claims his state pension. However, the additional income that he receives through the DLA is paid to meet additional costs, such as care and support. While the income from disability benefits cannot necessarily be considered as disposable income, it is important to consider the effect on his income. If the low earning man did not receive disability benefits he may need to pay for his care and support with his other income thereby reducing his ability to spend on other living costs and reducing his standard of living. Therefore, disability benefits can play an important role in safeguarding against further reductions in income for those who have to leave work early due to health problems.

Remaining in work until State Pension Age can help to maintain living standards up until retirement

The following analysis assumes that the median earning woman leaves full-time work at age 65, and works part-time until she reaches her SPA of age 67. She takes her private pension at age 65 in order to supplement her income and takes her state pension at age 67. Her income in this scenario is compared to her income in her baseline scenario in which she leaves work at age 65 and takes her private pension (taking her state pension at age 67).

¹⁹⁸ PPI Individual Model

Chart 23¹⁹⁹

In the median earning woman's baseline scenario, she gives up work completely at age 65 and takes her private pension. Her total gross state and private pension income of around £70pw drops below her target replacement rate of around £230pw by around £160pw for two years until she is able to claim her state pension. She may therefore experience a drop in living standards for two years before her SPA, unless she is able to supplement her income from other sources.

In the alternative, phased retirement scenario, in which she works part-time she is able to use her private pension to supplement her earnings in order to maintain a standard of living closer to the one she had in full-time working life until she reaches her SPA, at which point she is able to claim state pension and use it as a substitute for her earnings (Chart 23).

However, in neither the baseline nor the phased retirement scenario does she remain above her target replacement rate throughout her retirement as, during retirement, her income declines in earnings terms. She may have needed to save for longer in her private pension or contributed a greater proportion of her earnings in order to remain at or above her target replacement rate throughout her retirement.

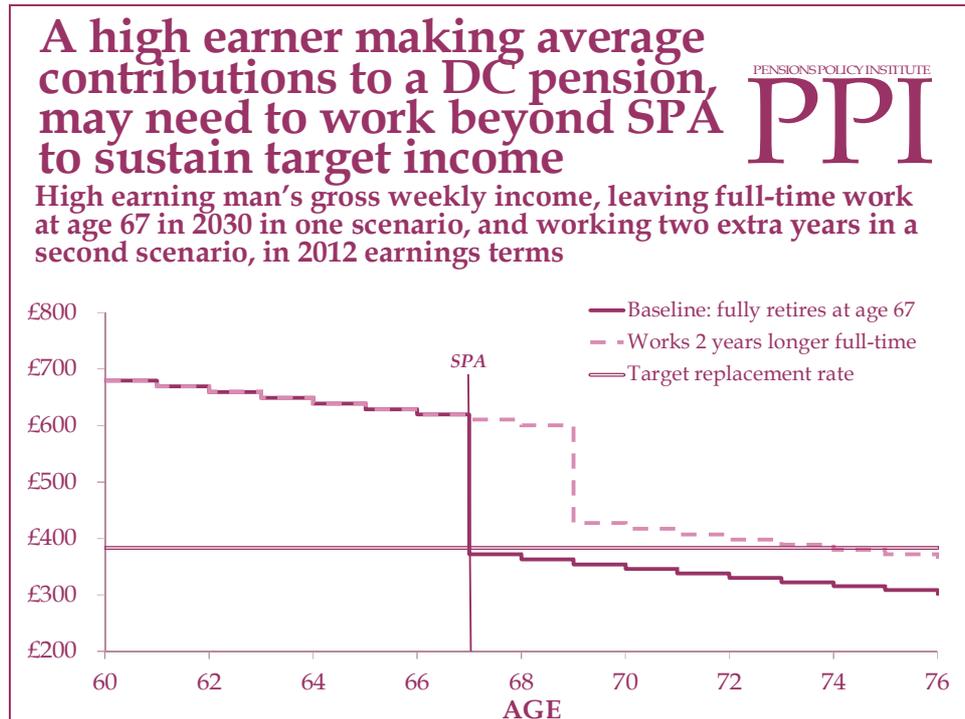
¹⁹⁹ PPI Individual Model

How long might someone need to work in order to replicate working life living standards in retirement?

The following analysis assumes, in the baseline scenario, that the high earning man works full-time until his State Pension Age (SPA) of age 67 in 2030 and then retires completely from work.

In an alternative scenario, the high earning man is assumed to work and save for 2 years after his SPA and take his state and private pensions at age 69.

Chart 24²⁰⁰



A high earner, contributing at average levels of salary into a DC pension may need to work beyond State Pension Age in order to meet and sustain his target income during retirement

If the high earner retires at his SPA of age 67 after contributing to his private (DC) pension (with his employer) at average levels for a DC occupational pension (of 9% of his total salary) his total gross state and private pension income will just miss his target replacement rate of around £380pw at retirement, by around £10pw, though the value of his income will continue to reduce in relation to his target replacement rate, in earnings terms, throughout his retirement (Chart 24).

Working full-time and saving for an extra two years, until age 69, allows the high earning man to remain above his target replacement rate for a further 7 years, until age 75, thereby being able to replicate working life living standards well into his retirement. High earners who are

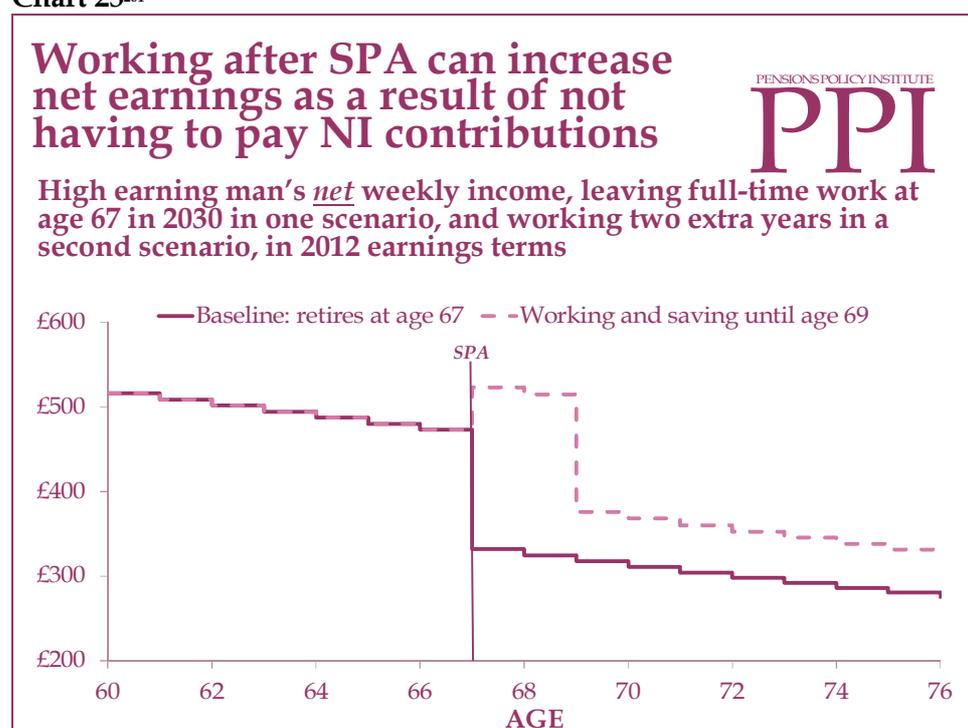
²⁰⁰ PPI Individual Model

contributing at average levels to their pension may need to work after SPA in order to ensure that they can sustain living standards for longer in retirement.

Working after State Pension Age can increase net income as a result of not having to pay National Insurance contributions

Part of the reason that people can replicate working life living standards in retirement on lower incomes than they had in working life is because people over SPA are not required to make National Insurance contributions. Therefore, the previous charts have shown illustrations of gross state and private pension income in retirement in comparison to gross target replacement rates. In order to illustrate the way in which not having to pay National Insurance contributions can benefit those who work after SPA, Chart 25 shows the high earning man's net weekly income under a scenario in which he works for two years after his SPA of age 67.

Chart 25²⁰¹



If the high earning man works for two years after his SPA, his net weekly income is around £190pw higher at his SPA of age 67 than it is under the scenario in which he retires at age 67. He also benefits after he has left work; at the point of retirement (age 69) his net state and private pension income is around £60pw higher than it is under the scenario in which he retires at age 67, as a result of saving for an extra two years into his private pension and deferring his state pension (Chart 25).

²⁰¹ PPI Individual Model

How might rises in State Pension Age affect the individual's retirement income?

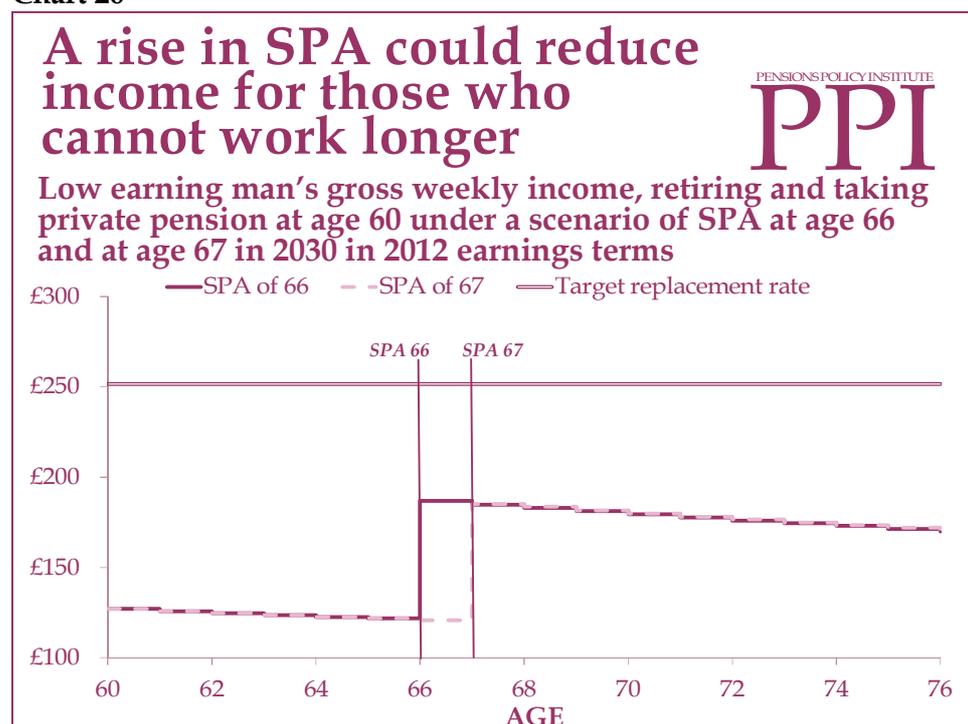
The following scenarios explore the potential impact of rises in the State Pension Age (SPA) on the hypothetical individual's income. The scenarios explore potential variations in retirement income for two individuals under the previous legislation in the Pensions Act 2007, under which their SPA would have remained at age 66 in 2030 (rising to 67 between 2034 and 2036), and under the proposed policy which increases their SPA to age 67 by 2028.²⁰² The aim of these scenarios is to demonstrate how the income of individuals might be affected by the proposed rise in SPA of one year, both if they do or do not work longer to compensate.

How might someone who needs to leave work early due to health problems be affected by rises in the State Pension Age?

The following analysis assumes that the low earning man's SPA does not rise to age 67 as under current proposals but instead remains at age 66 in 2030 (not rising to 67 until 2036) as under previous legislation.

The analysis compares the low earning man's income before and after his SPA with the income he receives under the baseline scenario in order to illustrate the potential impact SPA rises may have on the income of someone who is unable to adjust their working patterns to compensate for rises in SPA and cannot work up until their SPA.

²⁰² The Government announced in the Chancellor of the Exchequer's Autumn statement 2011 that they would raise the State Pension Age to 67 between April 2026 and April 2028

Chart 26²⁰³

A rise in State Pension Age could reduce income for those who cannot work longer

Under a scenario in which the low earning man's SPA is one year higher, at age 67, he needs to wait an extra year for his state pension. The rise in SPA does not reduce the income he receives from his private pension because in both scenarios he takes it at age 60 when he is no longer capable of work due to his health problems. However, later eligibility for SPA does mean he needs to live for one year longer on income from his private pension and state benefits, without the benefit of state pension to top his income up and bring him closer to his working life replacement rate.

Therefore, the rise in SPA of one year means that the low earning man must live for a further year on a total gross state and private pension income of around £120pw, which is around £130pw less than his target replacement rate income of £250 per week, until he starts to receive his state pension which brings him to within £70pw of his replacement rate, at age 67 (Chart 26).

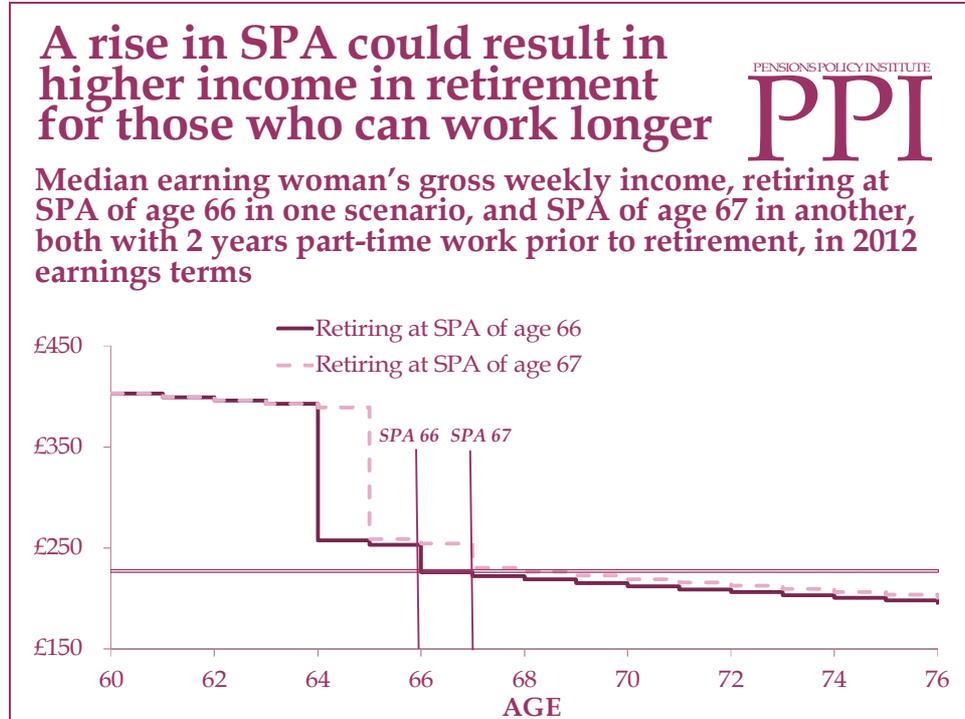
How might a State Pension Age rise affect the income of someone who is able to adjust by working longer?

The following analysis assumes that the **median earning woman** works full-time until age 64. At age 64 she takes her private pension and then works part-time for two years before retiring at her SPA of age 66 and taking her state pension.

²⁰³ PPI Individual Model

Her income under this scenario is compared to her income under a variant scenario in which she leaves full-time work at age 65, and from age 65 takes her private pension and works part-time until she reaches her SPA of age 67.

Chart 27²⁰⁴



A rise in State Pension Age could result in higher income in retirement for those who can work longer

Under the scenario in which the median earning woman's SPA is one year lower, at age 66, she works for a year less than in the scenario in which her SPA is at age 67. Working for one year less has the effect of reducing her income both at the point of retirement and beyond. Though her income drops below her target replacement rate in earnings terms from the year after retirement in both scenarios, she still has a higher income during the extra year she works before reaching her SPA at age 67 and receives a weekly state and private pension income of around £7pw higher throughout her retirement as a result of working and saving into her private pension for one year longer (Chart 27).

²⁰⁴ PPI Individual Model

Conclusions

The modelling analysis explored the impact of working longer and not working longer on 3 hypothetical individuals who have different income levels and saving histories during their working life. The modelling analysis found that:

- Leaving work before State Pension Age (SPA) can result in lower income both before and after SPA.
- Shopping around and purchasing an enhanced annuity could increase income in retirement for people with health problems
- Disability benefits can play an important role in meeting income needs for those who have to leave work early due to health problems.
- Remaining in work until SPA can help to maintain living standards up until retirement
- A high earner, contributing at average levels of salary into a Defined Contribution pension may need to work beyond SPA in order to meet and sustain his target income during retirement.
- Working after SPA can increase net income as a result of tax treatment.

The analysis explored how changes in behaviour in response to a rise in State Pension Age can affect income both before and after retirement:

- As expected, a rise in SPA could reduce income for those who cannot work longer.
- But a rise in SPA could result in higher income both before and after retirement for those who can work longer.

Appendix: modelling analysis

This appendix describes the assumptions and methodology for the modelling in this report. The first part, presented in chapter 3, uses a dynamic model of earnings and pension saving to illustrate what current levels of working and saving might mean at an aggregate level for respondents of the English Longitudinal Study of Ageing (ELSA).

The second part, presented in chapter 4, uses PPI's Individual Model to consider a number of more detailed case studies. Both models were developed with grants from the Nuffield Foundation.

General assumptions

The following assumptions are used in all modelling work in this report:

- Long-term increases in the retail prices index (RPI) of 3.2%;
- Long-term increases in the consumer prices index (CPI) of 2%;
- Long-term annual earnings growth of 4.7% in nominal terms;
- Short-term economic assumptions for RPI, CPI and annual earnings growth in line with Office for Budget Responsibility projections.²⁰⁵
- Expected investment returns of 6% in nominal terms, before charges, corresponding to a mixed equity/bond fund;
- Annual management charges of 1.0% of assets under management for DC schemes;
- When auto-enrolled, individuals and their employers are assumed to contribute at least at the minimum levels required under automatic enrolment legislation (a combined contribution of 8% of band salary)
- Auto-enrolled employees are assumed to enter schemes with NEST charges (0.3% annual management charge, 1.8% contribution charge).

These assumptions are the result of consultation with the PPI's modelling review board, which consists of a number of experts in the field of financial modelling.

Further assumptions, specific to different modelling and scenarios are outlined in later sections.

Analysis of the English Longitudinal Study of Ageing

The English Longitudinal Study of Ageing (ELSA) is an on-going longitudinal study of a range of social indicators of people aged over 50 in England. Chapter 3 of this report presents aggregated analysis of deterministic projections based on current earnings and savings levels in the ELSA Wave 3 dataset, 2006 made using a dynamic micro-simulation model.

This analysis is based upon data and a set of assumptions regarding future behaviour that may not be fully representative. **As a result of this, the results should not be taken as forecasts of future levels of income adequacy.**

²⁰⁵ OBR (2012)

Method and assumptions

This section provides a brief description of the method and assumptions used in this modelling. The main assumptions are then summarised in Box A1.

The individuals considered in the modelling set out in Chapter 3 work are those in the ELSA Wave 3 dataset, aged between 50 and SPA²⁰⁶, belonging to a Benefit Unit²⁰⁷ that has at least one member still in work. This sample consists of approximately 3000 individuals.

The financial data has been adjusted to make it consistent with 2011 earnings levels, which is taken as the base year for the model. In subsequent years of the projection, individuals are aged and their earnings increased in line with average earnings growth. Pension saving is also projected as outlined in Box A1.

In each year of the projection, potential retirement incomes for each individual are calculated, based upon the value of state pension entitlement, and current and deferred private pension entitlement. These are then converted into Benefit Unit incomes, by matching individuals with their partners, so that Pension Credit, Housing Benefit and Council Tax benefit entitlement can be estimated.

Following this, potential Benefit Unit retirement incomes are compared to either a Minimum Income Standard, or a target replacement rate based on working life incomes. Benefit Units that have potential retirement incomes above this level are then assumed to retire. Couples are assumed to retire at the same time based on a comparison of joint potential retirement income against either the pensioner couple Minimum Income Standard, or a target replacement rate based on joint working life income.

Individuals in Benefit Units that do not reach the required adequacy level are assumed to continue working and saving until they do. Whilst it is Benefit Unit incomes that are tested against the income adequacy level, the results are presented at an individual level.

²⁰⁶ This refers 65 for men and 60 for women.

²⁰⁷ In this analysis, a benefit unit is considered to consist of either a single adult or a couple living in the same household.

Box A1: Baseline dynamic modelling assumptions

- Individuals currently in work are able to continue working and saving until their savings reach the target level.
- Individuals currently contributing to a private pension continue to do so at the same rate that they are currently contributing.
- Individuals not currently contributing to a pension, but who will be eligible for auto-enrolment, begin saving at the minimum contribution rates required under legislation.²⁰⁸
- Individuals do not access any private pension savings until the target retirement income level has been achieved.
- Individuals saving in DC schemes are assumed to purchase a single life, level annuity after taking their 25% tax-free lump sum.
- Where appropriate, DB members are assumed to convert 25% of their pension into a lump sum.
- Individuals receive their state pensions at their SPA as legislated in April 2012, and proposed policy.²⁰⁹
- The current state pension system is assumed to be in place.
- Target replacement rates are calculated as a percentage of gross working life income as set out by the Pensions Commission modelling. No target replacement rates are assumed to be below the Minimum Income Standard level.
- The Minimum Income Standard used in income testing has both the rent and council tax components removed due to variation in these across the ELSA dataset. For this reason, both Housing Benefit and Council Tax benefit have been removed from Benefit Unit incomes for this analysis.
- State pension entitlement not in payment is not recorded on ELSA. We have estimated entitlement, assuming all individuals receive the full amount of BSP. Average S2P/SERPs entitlement, based on PPI Aggregate Model projections is assigned to individuals by contracted out status.
- Members of a couple are assumed to retire at the same time based upon a comparison of joint income working life income against either the Minimum Income Standard for pensioner couples, or a target replacement rate based on potential joint retirement income.

Data

The model makes use of financial variables taken from the ELSA Wave 3 dataset. The most important variables considered for each individual concern:

- Earnings
- Pension contributions
- Current and deferred pension entitlement

²⁰⁸ Contributions are phased in between 2012 and 2019 to reach 8% minimum total contributions on band earnings by 2019 - between £5,715 and £38,185 (2010/11 earnings terms)

²⁰⁹ The Government announced in the Chancellor of the Exchequer's Autumn Statement 2011 that they would raise the State Pension Age to age 67 between April 2026 and April 2028.

The required data is not always available. There are two main cases where values have been estimated. The first is that where DC contribution rates are missing, the average has been assigned.

Secondly, ELSA contains no data on the level of deferred pension entitlement. In order to estimate this, broad assumptions on average contribution levels, investment returns and accrual rates were used in conjunction with available data on pension type, dates of scheme membership and current gross salary. Where scheme membership and salary data were unavailable, values were randomly assigned using a 'hot-decking' procedure based on the financial wealth quintile of the individual. This method is similar to that used by the IFS in their paper *Estimating Pension wealth of ELSA Respondents*.²¹⁰

In addition to this, approximately 1% of the individuals included in this modelling have some form of pension entitlement from a former spouse. This has not been included in the analysis.

Sensitivity to assumptions

Table A1 demonstrates the change to the target replacement rate results to changes to two of the assumptions made in the analysis:

- Individuals are assumed to convert 100% of their pension into income, rather than taking 25% as a lump sum, which is not used to secure an income in retirement as in the baseline modelling.
- Individual estimated S2P/SERPs entitlement is doubled. As outlined in Box A1, individuals are assigned average S2P/SERPs entitlement based on PPI Aggregate Model projections. This is likely to underestimate entitlement for some high earners, that aren't assumed to be contracted out.
- The assumption that individuals in a couple retire in the same year is relaxed. The alternative to this is that the first person to reach SPA in the couple is able to retire as soon as an income test is satisfied based upon their potential retirement income with their partner's working life income. The second person must then wait until they reach SPA before being income tested and able to retire. This assumption can make it easier for the first member of the couple to reach SPA achieve income adequacy in retirement at that age, but can lead to couples where one member is unable to ever achieve income adequacy in retirement.
- The assumption that individuals can continue to work to SPA. For many this may not be realistic. As an alternative we have modelled each individual retiring 2 years before their SPA. As in this sensitivity retirement is 'forced', only the impact on those able to reach the target replacement rate by SPA is considered.

²¹⁰ Banks, Emmerson, Tetlow (2005)

Table A1: Results of sensitivity analysis

Figures given in brackets represent change from the baseline results and percentages may not sum due to rounding. Each assumption has been changed in isolation. Figures are rounded to the nearest 5%. *Represents less than 5%.

Achieve target replacement rate by age	Baseline results	Change from baseline arising from			
		Not taking lump sum	Doubling estimated S2P/SERPs entitlement	Change in treatment of couples	Retiring 2 years before SPA
By SPA	40%	45% (+5%)	40% (+*%)	50% (+10%)	35% (-5%)
1-5 years after SPA	10%	10% (+*%)	10% (+*%)	5% (-5%)	
6-10 years after SPA	5%	5% (+*%)	5% (+*%)	5% (-*%)	
11+ years after SPA	45%	35% (-10%)	40% (-*%)	40% (-5%)	

Table A2: Range of results from sensitivity analysis

Achieve target replacement rate by age	Range of results
By SPA	40% - 50%
1-5 years after SPA	5% - 10%
6-10 years after SPA	5% - 5%
11+ years after SPA	35% - 45%

Individual modelling

The PPI’s individual model uses individual characteristics and working patterns to project retirement income from private pensions, state pensions and other benefits for hypothetical individuals.²¹¹

Box A2 outlines the assumptions that apply to all individual modelling work carried out in this project.

Box A2: Individual modelling assumptions

- All individuals are assumed to purchase a single life, level annuity with their Defined Contribution private pension savings.
- Everyone takes their tax free lump sum and does not use it to provide a secure income in retirement (this is the most common event in practice)
- The current state pension system and the current system of working-age benefits are both in place rather than Universal Credit and/or single-tier state pension.
- The baseline scenarios assume the SPA rises to age 66 by 2020 as set out in the Pensions Act 2011 and rises from age 66 to age 67 between 2026 and 2028 as announced in the Chancellor of the Exchequer’s Autumn 2011 statement.

²¹¹ For more information on the Individual Model, see PPI (2003) *The Under-pensioned*

Individuals modelled

This research investigates the potential impact of future work and retirement patterns on individuals.

Detailed assumptions have been made about the individuals' working and saving behaviours. These are described in boxes A3-A5, including the assumptions made under any alternative scenarios.

Box A3: Low earning man

- He is born in 1963 and begins work at age 22.
- When working, he earns at the 30th percentile of age-specific earnings for men.
- In 2003, aged 40 he and his employer begin contributing into a DC scheme at the average rate of 9% of gross pay (combined).
- Under the baseline scenario, he retires in 2030, at his SPA of 67 under current proposed policy.²¹²
- He is then considered under two alternative scenarios:
 - He is forced into early retirement, aged 60 due to disability. He takes his private pension at this age, also receiving Employment and Support Allowance until he reaches SPA of 67.
 - He is forced into early retirement, as in the first alternative scenario, but the planned rise in SPA from 66 to 67 between 2026 and 2028 does not take place, so he reaches his SPA of 66 in 2029.

²¹² The Government announced in the Chancellor of the Exchequer's Autumn statement 2011 that they would raise the State Pension Age to 67 between April 2026 and April 2028

Box A4: Median earning woman

- She is born in 1963 and begins work at age 22.
- When working, she earns at median age-specific earnings for women.
- Between the ages of 30 and 35 she takes time out of work to care for her children.
- When she returns to work, she works part-time for two years at 50% of full-time earnings, and then resumes full-time work.
- While working, she contributes to a DC pension at the average level of 9% of gross pay (employee and employer contributions).²¹³
- Under the baseline scenario, she retires in 2028, two years prior to her SPA of 67 under current proposed policy and takes her private pension.²¹⁴
- She is then considered under two alternative scenarios:
 - After ceasing full-time work at age 65, she works two years part-time at 50% of full-time earnings in order to supplement her private pension income. She stops working at her SPA of 67.
 - The proposed rise in SPA from 66 to 67 does not take place. Under this scenario, the Median Earning Woman stops full time work aged 64, rather than 65. She takes her private pension at this age and works part-time at 50% of full-time earnings for two years until she reaches her SPA of 66.

Box A5: High earning man

- He is born in 1963 and begins work at age 22.
- When working, he earns at the 70th percentile of age-specific earnings for men.
- When in work, he and his employer contribute to a DC pension at the average level of 9% of gross pay (employee and employer contributions).
- Under the baseline scenario, he retires in 2030, at his SPA of 67 under current proposed policy.
- Under an alternative scenario he continues to work until age 69, two years after his SPA. He defers his state pensions and delays taking his private pension until retirement at this age.

²¹³ Average contributions to a DC occupational pension in 2010, 9% total average contribution made jointly by employer and employee, www.ons.gov.uk/ons/rel/pensions/occupational-pension-scheme-survey-annual-report/2010-annual-report/art-opss2010.html#tab-Chapter-4--Contributions-to-schemes

²¹⁴ In 2010, 35% of women between ages 55-59 had already left the labour market (ONS Pension Trends Ch4 2011). This means that currently many women do not work up until their SPA.

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Contact: Niki Cleal, Director

Telephone: 020 7848 3744

Email: info@pensionspolicyinstitute.org.uk

Pensions Policy Institute
King's College
26 Drury Lane
London WC2B 5RL

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