

PENSIONS POLICY INSTITUTE

PPPI

RAISING STATE PENSION AGE:
AN UPDATE

Raising State Pension Age: An update

Introduction	2
Summary of conclusions	4
Chapter 1: Feedback on <i>Are We Ready?</i>	5
Chapter 2: Impact of labour market changes	16
Appendices	18
Acknowledgements and contact details	23
References	24

A Discussion Paper by Alison O'Connell
Published by the Pensions Policy Institute
© October 2003
www.pensionspolicyinstitute.org.uk

Introduction

In September 2002, the Pensions Policy Institute (PPI) published its first discussion paper *Raising State Pension Age: Are We Ready?* The paper examined the possible justification for raising state pension age (SPA) and the practical transition issues in so doing.

The original paper was launched because, although most of the proposals made to reform state pensions involved an increase in state pension age, the particular issues involving SPA had not been thoroughly aired. The 2002 PPI paper therefore gathered the arguments around raising SPA into one place in order to encourage informed debate.

The paper concluded that¹:

1. Raising State Pension Age is a legitimate – and timely – subject for debate.
2. Startling longevity improvements suggest a significant hike in SPA is overdue.
3. Raising SPA allows a higher Basic State Pension at higher ages, clarifying its role as insurance against living longer than expected.
4. Raising SPA should be a strong signal for today's younger workers to be prepared to work longer.
5. Raising SPA does not significantly alter the distribution of state pension money between income groups.
6. Any announcement of plans to raise SPA would need to be accompanied by activity to ensure other policies will be effective in time.

A year on, and the debate has continued. There has been further research and comment on the issue, and on state pension reform more generally.

New events suggesting an upwards drift in the age at which people will stop working, so consistent with an increase in SPA include:

- Department for Work and Pensions proposals to raise the age at which a private pension can be taken from 50 to 55, the pension age for public sector workers from 60 to 65 and the eligibility age for pension-related means-tested benefits from 60 to 65².
- Department of Trade and Industry proposals to encourage working at older ages by outlawing age-discrimination³.
- The NAPF's proposals for reforming state pension, including a future increase in SPA to 70⁴.
- The raising of normal pension age by some occupational schemes.

¹ See Appendix 1 for more details

² DWP (2002 GP)

³ DTI (2003)

⁴ NAPF (2002)

- The proposal from a working group in Germany that the statutory retirement age should be increased from 65 to 67 between 2001 and 2035⁵. Italy is considering a rise from 60 to 65 and other countries are already making such changes⁶.
- The suggestion by Adair Turner of the Pensions Commission that the future macro-economics of pension provision are likely to require an increase in average retirement age⁷.

The government has decided against raising SPA⁸. This decision was commended by the House of Commons Work and Pensions Select Committee⁹ but the Committee also recommended that the issue of raising SPA be kept under review.

This paper adds to the one year old analysis on raising SPA. It summarises the feedback gathered by the PPI in the course of discussions on the subject – in seminars, in the media, with pension experts and with politicians. In making conclusions, this paper asks: are we now ready to raise state pension age, and if not, should we be?

For those not familiar with the subject, the following will be useful background:

SPA in the UK is currently 65 for men and 60 for women. Between 2010 and 2020, the SPA for women will increase, so that by 2020, SPA will be 65 for everyone.

SPA is not 'retirement age'. There is no official retirement age, but employers can currently set normal retirement ages for employees.

Raising SPA would be a policy for the long term, so that people have a chance to prepare. If SPA were to be raised, it is most likely to take effect after the year 2025. The oldest people likely to be affected by an increase in SPA are currently around age 40.

Proposals have been made to raise SPA to 67 or 70 over the next 25-30 years. Another option is a schedule of future SPA increases, planned to maintain a constant length of state pension receipt, given expected average longevity.

⁵ German Federal Ministry for Health and Social Security (2003)

⁶ Turner J. (2003)

⁷ Turner A. (2003)

⁸ DWP (2002 GP)

⁹ House of Commons Work and Pensions Select Committee (2003) p. 53

Summary of conclusions

This paper concludes that, although the UK is not ready to raise State Pension Age yet, it should be kept as a live policy issue. The state pension system needs to be reformed. Raising SPA could be one of the trade-offs involved to make state pensions better in the long-term. The increasing emphasis on changing work practices to make working at older ages more likely may make raising SPA possible. Pensions policy, social security policy for people below SPA and labour market policy need to be considered together.

Are we ready to raise SPA in the UK?

The answer to this question has to be 'not yet'. The policy is not universally popular and not well understood.

Should we be ready to raise SPA in the UK?

There are strong reactions against raising SPA, discussed in Chapter 1. The strongest argument against is that it disadvantages manual workers more than non-manual. But any actual disadvantage could be mitigated in other ways, if it were decided that raising state pension age was right for other reasons.

There are also advantages to raising SPA. It may be the only way to sustain a better state pension in future, and it fits with the potential for longer working lives as we live longer. Raising SPA is also consistent with other initiatives and trends that are encouraging later working, discussed in Chapter 2.

So, what do we need to do to get ready?

As a rise in SPA would be more acceptable as part of improvements to the state pension system, the first step must be to work out how state pensions should be reformed, and what part raising SPA might play in a reformed system. The PPI has started a process to analyse reform models, incorporating possible options for the state pension age¹⁰.

If it were decided to raise SPA then state income supplements need to be available to support those people with no other income available before the new SPA. A better understanding of the likely future patterns of work and income at older ages is therefore needed.

Expected changes in work practices (anti-age discrimination, retraining, more part-time working) should help to make later working lives a reality. Raising SPA would be a more popular policy if the potential positive impact of such changes could be demonstrated.

The PPI hopes that this paper contributes to the continuing debate.

¹⁰ See O'Connell (2003) for more detail

Chapter 1: Feedback on *Are We Ready?*

In discussions of the points put forward in the original PPI paper on raising SPA, four main arguments were made against the policy:

1. The politicians' reaction: *The problem we have now is that people don't work until they are 65, never mind trying to get them to work after age 65*
2. The typical *vox pop* reaction in the media: *I don't want to work until I'm 70*
3. The argument used by government for not raising SPA now, reflecting the concerns of social commentators and older people's interest groups: *Manual workers die younger, so raising SPA discriminates against lower income groups*
4. The sidestep: *What we really need is flexible retirement*

These four arguments will now be examined in more detail.

1. The politicians: *The problem we have now is that people don't work until they are 65, never mind trying to get them to work after age 65*

This argument is a preference for short-term rather than long-term action to encourage economic activity at older ages. Raising SPA can only affect the current under-40s, that is, tomorrow's older people¹¹. The government's focus on working later is targeted at today's over 50s. But there is an argument for consistent actions on both the short- and long-term. People who work after SPA tend to be those who worked up to SPA¹².

It should also be taken into account that people seem to be working later anyway, and that trend may well continue because of other factors.

- **A trend may have started for people to work later.** The economic activity rate for people at or over state pension age has fluctuated between 7.7% and 8.2% since 1994, but in 2002 increased to 8.8% and in 2003 to 9.1% (Chart 1). One estimate is that this figure could rise to 13% by 2020¹³.

¹¹ See O'Connell (2002) p. 19

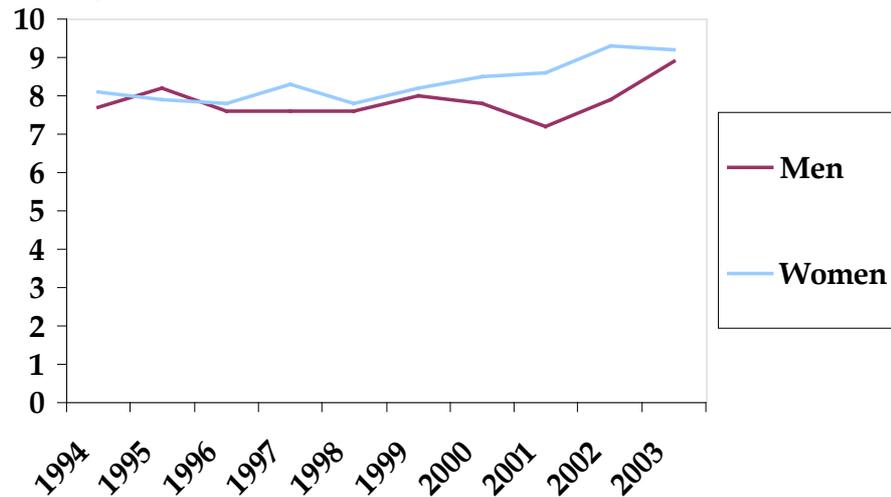
¹² Smeaton & McKay (2003)

¹³ Future Foundation for Saga, September 2003

Chart 1¹⁴

People are working later

Percentage of people aged SPA and over who are 'economically active'



- **Working later may become more likely as employers increasingly seek older workers,** as the workforce ages. There is expected to be a shift of 10% of the potential workforce from the under 50s to over 50s in the next 20 years¹⁵. Anti-age discrimination legislation and other measures may encourage employers to get better at employing older people.
- **Working later may also be a consequence of less generous occupational schemes.** The average private pension in future generations may be relatively less compared to the private pensions of people retiring now¹⁶. The normal pension age in many occupational schemes may increase, for younger workers, given the future cost pressures of such schemes. As many schemes have a normal pension age of 60¹⁷, any increase is likely to be a catch-up to current SPA, not an extension beyond it. Examples are in Appendix 2. Personal pensions are also likely to be paid at later ages in future as the minimum age at which personal pensions can be taken is proposed to increase from 50 to 55.

¹⁴ Data for Spring quarters (March–May) from Labour Force Survey in *Labour Market Trends* September 2003. 'Economically active' refers to people in work or looking for work.

¹⁵ Barham (2002)

¹⁶ Curry and O'Connell (2003)

¹⁷ O'Connell (2002) pp. 21-22

2. The vox pop: *I don't want to work until I'm 70*

This comment formed the basis of much media reporting of the policy and questioning of the original paper. Some of the comment is based on a misunderstanding of how state pension age relates to the age of retirement. Raising SPA does not have to mean that everyone will work up to that new SPA, as there are other sources of income available for people who stop work before SPA.

Media commentary also reflects of course, that many people do not like work, yet know they are likely to need the income from work in later life. So what people say about wanting to give up work has to be interpreted carefully. Although most people say they do not want to work later, there is some acceptance that SPA might be raised.

Raising SPA does not have to mean that everyone will work up to that new SPA. There is much less real linkage between state pension age and age of retirement than people generally expect there to be.

- **Most people stop working before SPA**, although 40% of women and 60% of men are still employed by age 60. After age 65, around 10% of people work¹⁸. The median age of withdrawal from the labour force is 62.6 years for men and 60.4 years for women¹⁹.
- **SPA does not cause a 'cliff-edge' of retirement.** In the year of reaching SPA employment levels drop 10% for women, and 17% for men²⁰. Although this is the biggest drop in any one year of age, it is not the case that SPA marks a sudden cessation of work for most people.

There are other sources of income for people who stop work before SPA. Concerns about raising SPA, for people who want to stop working early, are tied up with concerns about having money to live on after they stop work. Any financial gap between when people stop work and when they receive state pension could be filled by private pensions, savings or benefits.

- **Raising SPA could allow a better use of small pension savings** than is the case currently. If SPA were raised, and a higher state pension paid later, people may find they only need to use their savings to fill the gap between stopping work and the new SPA. Currently they have to buy an open-ended annuity to last for life. A fixed term annuity, payable only until the new SPA, could be a better use of small savings. For the same purchase price, an annuity at age 60 for 10 years could provide more than twice as much income as an annuity for life²¹.

¹⁸ Smeaton & McKay (2003)

¹⁹ DWP (2002 GP) p. 17

²⁰ Smeaton & McKay (2003)

²¹ PPI analysis

- **Non-pension state social security benefits will continue to be paid at all ages** for specific reasons of low income. The availability of Jobseekers Allowance, Incapacity Benefit and Disability Living Allowance would have to be extended to the new SPA.
- **Non-state pension benefits could be extended for people nearing SPA.** Currently, the means-tested Guarantee Credit (GC) is payable to people aged 60 and over. This means that men with low income aged between 60 and 65 receive the same level of minimum income as people over SPA, which is higher than the minimum income available to people under age 60 from Income Support. The availability of such a benefit to people who cannot work five years prior to SPA could be maintained as SPA increases, in order to provide an additional safety-net. However, it is planned to increase the minimum age for GC to 65²².

What individuals say about wanting to give up work has to be interpreted carefully. Most young people say they would like to retire before SPA, but when they reach the age where serious financial planning starts (usually around age 50), they expect to work later.

- **Most people do not begin to work out their possible future retirement circumstances until after age 50.** In response to the question *Have you worked out how much you will need to retire comfortably?* 46% of people in work and aged over 50 said *Yes*, but only 18% of workers aged between 25 and 50 did so²³.
- **Older people expect to retire later than younger people.** In response to the question *When would you like to retire if you could?* 17% of people in work and aged between 25 and 50 said *over 60* and 67% of them said they would like to retire *between age 50 and 60*. Of older workers, aged between 50 and 60, 31% said *over 60* and 54% said *between age 50 and 60*²⁴.
- **Statements of desirability of retirement age should be interpreted carefully.** It is unlikely that younger people who say they want to retire early will in fact do so. Because people think less about their future financial circumstances at younger ages, it is likely that people adjust their retirement plans as they age and realise the economic reality and/or find themselves wanting to make positive choices about working longer.

²² DWP (2002 GP) p. 101. The increase in the age for eligibility for GC is planned to be coincident with raising SPA for women (between 2010 and 2020). GC is one of the two parts of the Pension Credit, and used to be called Minimum Income Guarantee (MIG). See also page 14.

²³ CIPD (2003). See also Rowlingson (2002).

²⁴ CIPD (2003). See also Smith & McKay (2002).

Although most people say they do not want to work later, there is some acceptance that SPA might be raised. Most people do not like the idea of raising SPA, but the people affected by the policy seem to mind less than those who would not be. Raising SPA seems to be more acceptable if it is part of a package of increased state pension benefits. However, we do not know whether people would prefer to pay more taxes in order to retain the current SPA.

- **Younger people are happier with raising SPA than older people.** In answer to *Do you agree or disagree that people should have to wait until they are 70 to get their state pension, if the pension would be far larger as a result?*, 26% agreed. There seems to be a strong slant by age: 45% of 18-29 year olds agreed, 30% of those aged 30-34, but only 17% of 50-59 year olds²⁵. But older people would not be affected by the increase in SPA.
- **Raising SPA seems more acceptable if it is linked to enhancing the state pension.** In answer to the question *Do you agree or disagree that people should have to wait until they are 70, instead of 60 or 65, to get their state pension?* 12% agreed, less than half the proportion agreeing to the question linking a rise in SPA to an improvement in the level of state pension²⁶. This seems to support the general idea in the original PPI paper, and other proposals, that raising SPA would only be done as an integral part of reform to solve the problems in state pensions; in particular to make state pensions adequate.
- **Public opinion on alternative ways to improve pensions has not been tested.** People may prefer to pay more taxes and keep SPA at 65, or the reverse.

²⁵ You.Gov research October 2002. Answers on a 5-point scale; figures given are those agreeing strongly and slightly.

²⁶ You.Gov research October 2002.

3. Government and concerned interest groups: *Manual workers die younger, so raising SPA discriminates against lower income groups*

This point explains why SPA should not be raised without supporting policies to protect lower-income groups. There is no doubt that there is a difference in life expectancy between social classes, but the implications for SPA are not obvious. The general improvements over time in healthy life expectancy may be more relevant than the widening gap between groups. Many more people are now capable of working after SPA than was the case when the state pension system was designed.

Therefore, the differences in healthy life expectancies should not be used to dismiss raising SPA out of hand. If it were decided to raise SPA, then more thought would be needed on how to support any individuals who would be adversely affected by the change, and on how to make a later working life more possible and attractive for all income groups.

There is no doubt that there is a difference in life expectancy between social class. However, the real size of the difference, and the extent to which it is widening, needs to be clarified.

- **There is a difference in life expectancy by social class.** The gap in average life expectancy at birth between manual men and non-manual men is 3.5 years; for women it is 2.8 years. This represents just under 5% and 4% respectively of the life expectancy of an average man or woman²⁷.
- **The gap in life expectancies between social classes can be exaggerated by focusing on extremes.** Social Classes are graded from I (professional) through II, III Non-manual, III Manual, and IV to V (unskilled). By 'the life expectancy gap', it is sometimes meant the number of years that life expectancy for people in Class I exceeds that for people in Class V. On this definition, the gap between Class I and V life expectancy at birth is 7.4 years for men and 5.7 years for women²⁸.

But only 5% of people are in Class I and the number of unskilled men (Class V) has reduced dramatically, also to around 5%. This means that focusing on the I to V comparison ignores 90% of people. This is why it has been suggested (by the ONS) that the difference between the two groups - 'non-manual' (I - III N) and 'manual' workers (III M-V) - is a more appropriate measure²⁹.

²⁷ Appendix 3

²⁸ Donkin et al (2002). For men life expectancy at birth is 78.5 years Class 1 and 71.1 years Class V. For women: 82.8 and 77.1 years.

²⁹ Donkin et al (2002)

- **There has been a gradual widening of the difference in life expectancy between manual and non-manual men since the 1970s.** The latest figure for the life expectancy difference at birth between manual and non-manual men is 3.5 years, compared to the early 1970s when the difference was 2.1 years. The trend for women is not clear, but the difference appears to have narrowed since the late 1980s³⁰.

The implication of the socio-economic life expectancy gap for SPA is not straightforward. Other differences between people cause more of a difference in life expectancy.

- **The manual worker life expectancy disadvantage is smaller than the disadvantage suffered by other groups.** Although manual workers have a life expectancy around 3 years shorter than non-manual workers, men die 5 years younger than women and smokers die around 7 years younger than non-smokers³¹.
- **There are complex inter-related effects from different factors.** It is not manual work itself that causes all the differences in health or mortality. For example, psychosocial wellbeing (including autonomy in the workplace, and the quality of social relations) seems to be a major factor associated with health differentials³².

Smoking is also an important factor. The socio-economic difference in smoking behaviour drives much of the current and future gap in health and life expectancies by socio-economic group³³. Inequalities in healthy life expectancy will persist if this difference in smoking persists³⁴.

³⁰ Appendix 3

³¹ Appendix 3. Smoking differential from discussions with pricing actuaries in the insurance industry.

³² Marmot & Wilkinson (2001)

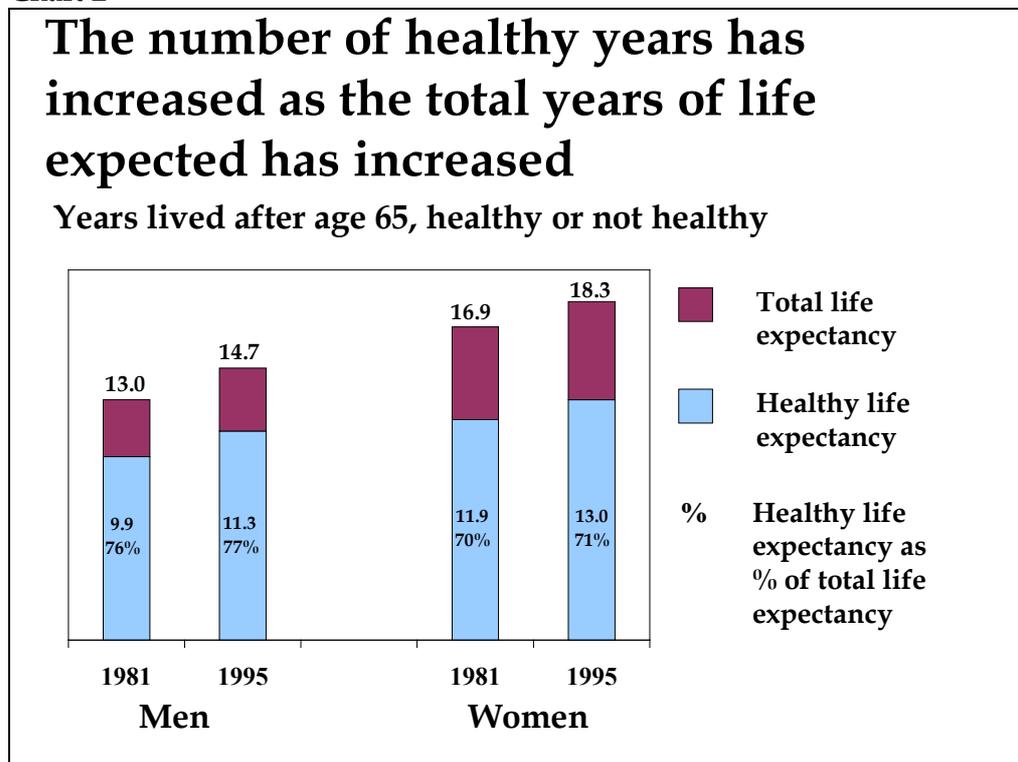
³³ PPI analysis from General Household Survey, 2001. The odds of a person smoking are almost twice as great for someone in the manual group compared to in the non-manual group.

³⁴ Evandrou & Falkingham (2002)

Despite the widening gap, life expectancy has improved significantly for everyone and the number of healthy years has increased. A realistic increase in SPA from 65 to 67, or even to 70, would be within the average 'good health' period.

- **Life expectancy is improving for all social classes.** Although the socio-economic gap in life expectancy is widening, life expectancy has improved continuously. People in the manual group now have a better life expectancy than people in the non-manual group did in the 1970s³⁵.
- **On average, health appears to be improving, so an increase in SPA would be within a period of good health.** There is much debate about whether the increased years after 'retirement' are getting more or less healthy. It is usually said that 'healthy life expectancy has increased but not by as much as total life expectancy'. But there are fewer years in poor health than in good health after age 65. In fact, as the number of years of life after age 65 has been increasing, a slightly higher percentage of those years are in good health (Chart 2).

Chart 2³⁶



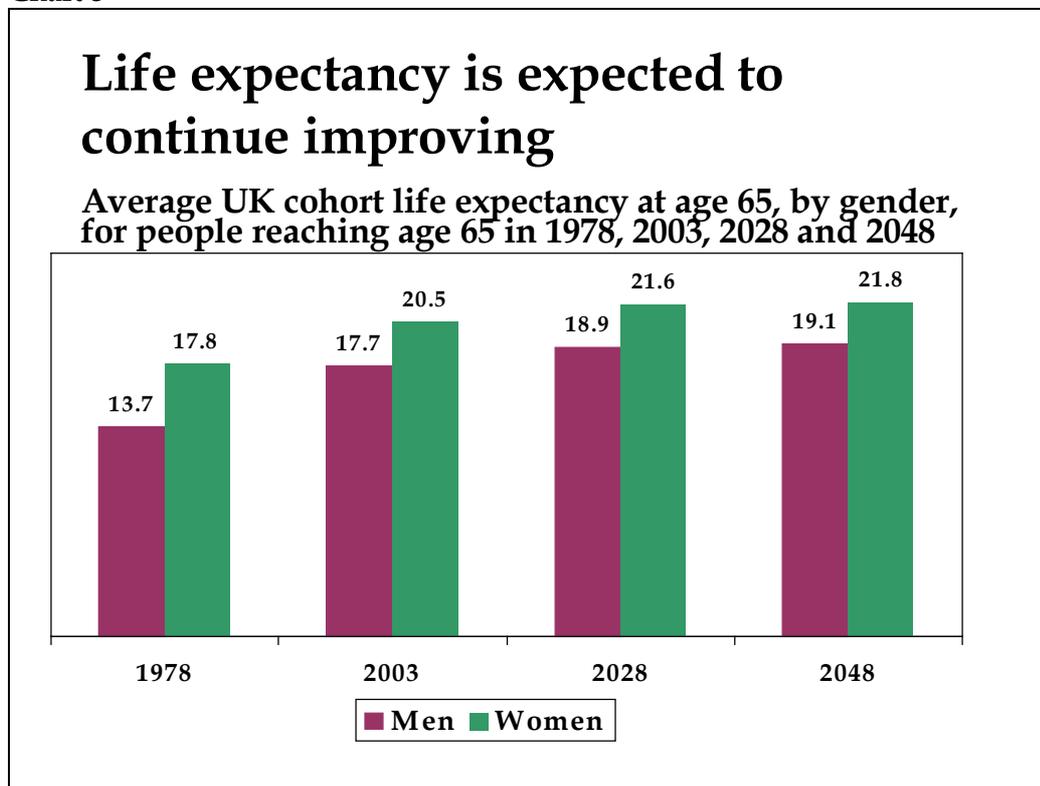
³⁵ Appendix 2

³⁶ Appendix 2. 'Healthy' is in good or fairly good health, some years of which may be with a limiting long-standing illness.

The state pension system has not changed to reflect the fact that many more people are now capable of working after SPA. The number of people able to do so is likely to increase, and the socio-economic gap in life expectancy is expected to narrow.

- **90% of people now live to age 65 to collect their state pension.** When the current form of state pensions was being planned, in the 1940s, only two-thirds lived to 65³⁷. Given also the improvements in health, it is not the case that the current SPA marks an age at which most people are unable to work.
- **Life expectancy is expected to continue improving.** The rate at which it improves may slow³⁸, but it may not. Over the last 25 years, the length of time a man reaching age 65 can be expected to live has increased by 4 years. A further increase of at least one year is expected over the next 25 years (Chart 3).

Chart 3³⁹



- **The gap in life expectancies between social classes is expected to narrow in future.** Healthy life expectancy from age 65 by social class is an indicator in the annual poverty and social exclusion report, and therefore a government target for improvement. By the time any change to SPA could be fully implemented, the overall health of people then aged 65-70 is likely to be better than is the case today, and inequalities are expected to have narrowed.

³⁷ See O'Connell (2002) pp.6-11

³⁸ For example, as assumed in DWP (2002 GP) following Government Actuary's Department projections

³⁹ From Government Actuary's Department, 2001 - based projections

The differences in healthy life expectancies should not be used to dismiss raising SPA out of hand. If it is thought appropriate to raise SPA for other reasons (to reflect the economic consequences of general longevity improvements and/or to improve the level of state pension benefits) then the implications, and the potential to manage them, need to be better understood.

- **The policy decision is whether healthy life expectancy has improved enough on average for an increase in SPA to be justified, taking into account the other means that could be used to support those who would be worse off by the change.** The risk in not raising SPA is that the state pension system overly favours healthy younger pensioners at the expense of older pensioners more likely to be poorer and in poor health. There are people in their sixties now who could not work until they are 70; but the issue to tackle is whether most of today's 40 year olds would be healthy enough to carry on working relatively longer.
- **There should be no actual financial disadvantage on raising SPA for any individual, provided supporting measures are taken.** As a rise in SPA would be phased in, over, say, a ten year period in the future, no one would be disadvantaged overnight. If SPA is part of a programme to reform state pensions, the average outcome, over a lifetime, may be better for most people.
- **For people with income problems before SPA, non-pension social security benefits could be extended.** Raising SPA does not mean people on low incomes have nowhere to turn. It means an increase in the age at which a low income problem stops being a social security issue and becomes a pension issue. Raising SPA could be part of a package of pension reform that takes older pensioners off means-tested benefits. Although this is likely to mean more means-testing before SPA, this could be a more acceptable balance than the current system of extensive means-testing of most pensioners⁴⁰.
- **The overall impact of raising SPA needs to be better understood.** Estimates of the proportion of people eligible for state social security or pension support at each age would need to be made. For example, in the original PPI paper, the costing calculations⁴¹ assumed that the average labour force participation rate for 65-69 year olds rises gradually but remains slightly below the current rate for 60-64 year olds. The likelihood of this outcome will depend on the availability of suitable work for older people, considered in the next chapter.

⁴⁰ And the very oldest pensioners are most likely to be means-tested. See PPI Briefing Note Number 6.

⁴¹ By John Hawksorth of PricewaterhouseCoopers. NAPF (2002) included a costing by the Government Actuary's Department for the cost of extra Incapacity Benefit and Jobseekers Allowance prior to a SPA of 70.

4. The sidestep: *What we really need is flexible retirement.*

Most people would agree that flexibility in the age of retirement, and choice over working part-time before full retirement, are desirable. Such flexibility is a separate issue from raising state pension age, as SPA itself is not a barrier to flexible retirement.

- **It is possible to earn while receiving state pension.** However, working part-time while taking a private pension from the same employer is currently prevented by tax rules, employers' conditions and occupational scheme rules. These barriers will be removed by recent government proposals⁴².
- **There is already flexibility to take state pension later than SPA.** It is planned to increase the level of the incentive to defer, that is the additional state pension received when it is finally taken. The new incentive to defer taking state pension is unlikely to be a compelling reason for many people to change their retirement behaviour. However, if the new incentive is promoted actively then more people than the current 2% a year who do defer may consider doing so⁴³.
- **Allowing state pension to be taken earlier than SPA does not work in a means-tested environment.** Many people do stop work below SPA, supported by other state social security benefits or private pensions. The facility to take state pension earlier for a lower pension (for life) causes problems, because there is extensive means-testing in the state pension system. Should someone who opts to take a reduced state pension at a younger age and then needs a means-tested income at a later age receive the full means-tested minimum income or the lesser amount consistent with his or her choice?
- **Taking state pension younger than SPA may not be in people's best interests.** Although most people do opt to take a reduced pension as early as possible, it may not turn out to be in their best interests, as it means a reduced pension for life. In the US, the earliest age for taking state pension is 62, which is the age at which the largest number of people choose to take state benefit. But the benefit is then 20% lower compared to the full benefit if taken from age 65⁴⁴.

⁴² DWP (2002 GP) and see also DWP (2003 Action)

⁴³ See PPI Briefing Note Number 4 for more details

⁴⁴ The full benefit age of 65 is due to increase to age 67. The benefit taken at age 62 will then be 30% lower than the full benefit. Information from John Turner, Public Policy Institute, AARP and Gustman and Steinmeier (2002).

Chapter 2: Impact of labour market changes

Age discrimination in employment and vocational training will become unlawful in the UK from 1 October 2006⁴⁵ under legislation planned by the Department of Trade and Industry (DTI) following the EU Employment Discrimination Directive.

Either the setting of compulsory retirement ages for employees will be made unlawful, or there will be a 'backstop' age of 70 (or higher) at which employers could require employees to retire without having to justify their decision.

There will be no direct impact on state pensions, and possibly little impact on occupational pensions. But the legislation is expected to increase the proportion of older people in work.

There are many other initiatives encouraging this trend. If the labour market does change to embrace more working at older ages, then raising SPA should become more acceptable. Raising state pension age is clearly not only a pension policy issue, but an example of the need for pensions policy and labour market policy to be considered together.

No impact on state pensions

The age discrimination legislation does not impact directly upon state pensions or State Pension Age. The EU Directive *does not apply to social security and social protection schemes*⁴⁶ in member states. This is consistent with the principle of subsidiarity in wider social security policy.

Possibly little impact on occupational pensions

The EU Directive allows occupational pension schemes to set ages for admission and entitlement to retirement benefits:

*Member States may provide that the fixing for occupational social security schemes of ages for admission or entitlement to retirement or invalidity benefits, including the fixing under those schemes of different ages for employees or groups or categories of employees, and the use, in the context of such schemes, of age criteria in actuarial calculations, does not constitute discrimination on the grounds of age, provided this does not result in discrimination on the grounds of sex*⁴⁷.

The DTI acknowledges that a normal pension age, where full scheme benefits are payable without reduction or enhancement, is required for the operation of Defined Benefit (DB) schemes⁴⁸.

⁴⁵ DTI (2003) p. 5, Paragraph 1.2

⁴⁶ EU Directive 2000/78/EC, Paragraph 13

⁴⁷ EU Directive 2000/78/EC, Article 6

⁴⁸ DTI (2003) p. 23, Paragraph 4.14

However, provision in the rules of a DB scheme for pension accrual to cease at normal pension age where the member remains in service after that date could be outlawed – unless the provision could be *objectively justified*⁴⁹.

There are a number of other practices in the operation of occupational pensions that may become unlawful from 2006. Such practices may include age-related contributions to Defined Contribution (DC) schemes or different benefits payable upon death while in service depending upon whether the member dies before or after normal pension age⁵⁰.

Expected rise in older worker employment

The reforms are expected to result in increased participation rates for older and younger workers⁵¹. However, there are no targets for the success of the proposals to help some estimation of the likely future activity rates for older people.

More than legislation may be required. Changes in employer attitudes toward older workers, and activity rates, do not necessarily follow legislative change. Australia, Canada, Finland, France, New Zealand and the US all have age discrimination legislation, but only New Zealand has lower unemployment among the over 55's than the UK⁵².

The general positive trend is also being encouraged by other government initiatives, such as Age Positive and Pathways to Work (helping people off Incapacity Benefit)⁵³. Organisations such as the Third Age Employment Network and the Employers Forum on Age are sources of analysis and support⁵⁴.

There is now more discussion of the labour market practices that will help longer working lives, such as lifelong training, flexible working and work-life balance.

Despite misgivings about whether employers are ready for the age-discrimination legislation⁵⁵, and whether it will go far enough⁵⁶, the fact that there is to be legislation at all is an advance. It recognises that working at older ages should be developed. If the legislation and other changes in labour market practices succeed in increasing the effective retirement age, then there might be more support for raising state pension age in future. Raising state pension age is clearly not only a pension policy issue, but an example of the need for pensions policy and labour market policy to be considered together.

⁴⁹ Draper (2003)

⁵⁰ Draper (2003)

⁵¹ DTI (2003)

⁵² OECD (2003) Statistical Annex

⁵³ DWP (2003 PW)

⁵⁴ See Grattan (2003) www.taen.org.uk; www.efa.org.uk; and www.agepositive.gov.uk

⁵⁵ IRS (2003)

⁵⁶ TAEN Newsletter Summer 2003

Appendix 1: Points made in *Are We Ready?*

The following repeats the conclusions of the original PPI paper of September 2002:

1. **Raising State Pension Age is a legitimate - and timely - subject for debate.**
 - There are enough valid reasons for raising SPA that the UK should be ready to consider it now.
 - The analysis and commentary in this paper are directed towards helping to build a fact-based consensus around a decision on whether or not to raise SPA.
 - This paper also suggests that the SPA issue should prompt debate with the aim of achieving long-term consensus on the role and level of the Basic State Pension (BSP).
2. **Startling longevity improvements suggest a significant hike in SPA is overdue.**
 - Many more people are living to collect their state pension: 90% compared to around 66% when the current social security system was set up around 1950.
 - People are living longer after collecting state pension: around 8 years longer than in 1950.
 - Benchmarking suggests a new SPA in the region of 72-75, so a catch-up in one step may not be practical. Further longevity improvements are forecast, so further increases in SPA may follow.
3. **Raising SPA allows a higher Basic State Pension at higher ages, clarifying its role as insurance against living longer than expected.**
 - It is hard to justify raising SPA for cost reasons alone. On current policy, state spending on pensions is projected to increase by only around 1 percentage point of GDP over the next 50 years.
 - But for no additional cost, the level of state pension benefit could be increased if SPA were raised. Raising SPA to 70 could free up resources to increase BSP by nearly 50% by 2030.
 - Alternatively, raising SPA allows the BSP to be increased by more at older ages: by up to 70% at ages 75 and over, at no extra cost.
 - Further increases could take older pensioners off means-tested benefits, for a small temporary extra cost. State pension resources would then be focused on giving a meaningful BSP to older pensioners, instead of a small amount to all.
 - Raising BSP at older ages clarifies the role of the BSP as a guaranteed insurance against poverty caused by living longer than expected. This role is increasingly relevant as longevity continues to improve.

- 4. Raising SPA should be a strong signal for today's younger workers to be prepared to work longer.**
 - Raising SPA should only affect people today in their 40s or younger who should be able to adjust work and savings plans.
 - Raising SPA will reinforce other policies encouraging greater workforce participation at older ages in future. Not raising SPA appears to contradict these policies.
 - Raising SPA may prompt occupational schemes to increase normal pension age, which would help relieve some of the current cost pressure on such schemes.
- 5. Raising SPA does not significantly alter the distribution of state pension money between income groups.**
 - Life expectancy and health prospects are improving for all socio-economic groups, although lower-income people on average are unhealthier and die younger.
 - However, any relative financial disadvantage to lower-income groups on raising SPA is hard to quantify.
 - Inequalities have always been inherent in the pension system. The socio-economic disadvantage is no worse than men, who die younger on average, receiving fewer years of pension than women.
 - If other policies are in place to support those potentially vulnerable to any future increase in SPA, it would seem unreasonable not to raise SPA only because of redistributive concerns.
- 6. Any announcement of plans to raise SPA would need to be accompanied by activity to ensure other policies will be effective in time.**
 - Communication of a decision to raise SPA is difficult because the issue tends to arouse immediate emotional responses. Clarity is important on who will be affected, when the change will take place and the reasons for the change.
 - Further research is necessary into the trends in those factors about which we know little, but are important for an increased SPA to be workable. These include the future health, caring and job prospects of people over 65.
 - The government needs to ensure that policies to help older people take suitable jobs, and to support those that cannot, are effective before any SPA change takes place.
 - The government will need to check that the private and occupational scheme sectors will be ready for a change in SPA.

Appendix 2: Examples of scheme pension age increases

The following are examples of recent scheme normal pension age (NPA) increases.

Axa	<ul style="list-style-type: none"> • New pension age of 62 for those UK employees with a current NPA of 60. Employees may continue to retire at age 60 but with a reduced pension. • Equalises NPA with some other schemes in company • Unions agreed 62 as new NPA; negotiated down from original plan of 65 • Employee contributions increased to 2.5% for those employees previously paying nothing and to 5% for those previously paying 3%. Employer contributions also increased.
Honda	<ul style="list-style-type: none"> • New pension age of 62 for those employees age 55 or under • The DB pensions scheme retained, but closed to all new employees • Employer contribution to be increased by 2% to 9.5%. Employees will have to increase their contributions by 0.5%.
Woolworths	<ul style="list-style-type: none"> • New pension age of 65 for new employees. Employees can retire at the original age of 60 but with a reduced pension. • New employees have to complete one year's service before joining the scheme. A stakeholder pension is available for the first year. • Union has supported the age increase as part of a package that retains the DB scheme • Existing members to increase their contributions from 5% to 7% to retain current benefit levels for a pension at age 60. New members will pay a rate of 6% for the new pension age of 65.
Public sector	<ul style="list-style-type: none"> • New pension age of 65 for all new employees from 2006 • Accrued pension rights by existing staff are protected and will continue to reflect a pension age of 60 • Future rights for current employees will be subject to transitional arrangements to be negotiated in 2004 • TUC and public sector unions oppose the proposal

Appendix 3

Life expectancy by social class, 1972-1999, for men and women, and life expectancy gaps by social class and gender (in years)⁵⁷

		1972-76	1977-81	1982-86	1987-91	1992-96	1997-99
Life expectancies							
Men	At birth						
	Non-manual	71.0	72.5	73.5	74.5	75.8	77.3
	Manual	68.9	69.9	70.7	71.3	72.6	73.8
	All	69.2	70.0	71.4	72.3	73.9	75.0
	At 65						
	Non-manual	13.1	14.0	14.2	14.7	15.6	16.8
	Manual	12.3	12.3	12.7	13.0	13.9	14.6
	All	12.3	12.7	13.1	13.5	14.6	15.4
	Women	At birth					
Non-manual		77.5	78.3	78.7	80.5	80.9	81.4
Manual		74.9	75.9	76.9	77.2	78.0	78.6
All		75.1	76.3	77.1	77.9	79.3	79.7
At 65							
Non-manual		17.4	17.8	18.0	19.8	19.2	19.8
Manual		16.5	16.7	16.9	16.7	17.3	17.4
All		16.2	16.7	16.9	17.2	18.0	18.4
Difference in life expectancy between non-manual and manual							
At birth	Male	2.1	2.6	2.8	3.2	3.2	3.5
	Female	2.6	2.4	1.8	3.3	2.9	2.8
At 65	Male	0.8	1.7	1.5	1.7	1.7	2.2
	Female	0.9	1.1	1.1	3.1	1.9	2.4
Difference in life expectancy between genders							
At birth		5.9	6.3	5.7	5.6	5.4	4.7
At 65		3.9	4.0	3.8	3.7	3.4	3.0

⁵⁷ Donkin et al (2002)

Life expectancy (total years lived) and healthy life expectancy (the number of those years in good or fairly good health, some of which may be with a limiting long-standing illness): years lived after age 65, 1981-1995⁵⁸

	1981	1995	Increase, years	Increase, %
Men				
Total life expectancy	13.0	14.7	1.7	13%
Healthy life expectancy	9.9	11.3	1.4	14%
HLE as % LE	76%	77%		
Women				
Total life expectancy	16.9	18.3	1.4	8%
Healthy life expectancy	11.9	13.0	1.1	9%
HLE as % LE	70%	71%		

These estimates are on a 'period' basis so they underestimate the life expectancy of a 'cohort', as in Chart 3. For further explanation see O'Connell (2002) Appendix 1.

⁵⁸ Kelly et al (2000)

Acknowledgements and Contact Details

Alison O’Connell is grateful for suggestions and input from many people in support of this paper, including:

Chris Curry
Federico Di Pace
Adrian Gallop
Patrick Grattan
Charlotte Reeks
Stewart Ritchie
John Turner
Lawrence Wakeham
Sally West

The author takes responsibility for any remaining errors and omissions.
© Pensions Policy Institute, 2003

The Pensions Policy Institute is an educational charity promoting the study of retirement provision through research, analysis, discussion and publication. The PPI takes an independent view across the entire pensions system.

The PPI is funded by donations and benefits-in-kind from a range of organisations. To learn more about the PPI, see www.pensionspolicyinstitute.org.uk

To contact the PPI please call, email or write to
Alison O’Connell, Director
Pensions Policy Institute
King’s College
Waterloo Bridge Wing, Franklin Wilkins Building
Waterloo Road
London, SE1 9NN

Tel no. 020 7848 3751
Email alison@pensionspolicyinstitute.org.uk

References

- Barham C. (2002) *Patterns of economic inactivity among older men*, Labour Market Trends. June 2002, Office for National Statistics
- Chartered Institute of Personnel and Development (CIPD) (2003) *Age, Pensions and Retirement: Attitudes and Expectations*, Survey Report March 2003
www.cipd.co.uk/download/registered/age_complete_210303.pdf
- Curry C, O'Connell A. (2003) *The Pensions Landscape* London: Pensions Policy Institute
- Department for Work and Pensions (DWP) (2002 GP) *Simplicity, security and choice: Working and saving for retirement* Cm 5677 London: The Stationery Office
www.dwp.gov.uk/consultations/consult/2002/pensions/index.asp
- Department for Work and Pensions (DWP) (2003 Action) *Working and Saving for Retirement: Action on Occupational Pensions*
www.dwp.gov.uk/consultations/consult/2002/pensions/actionplanfull.pdf
- Department for Work and Pensions (2003 PW) *Pathways to work: Helping people into employment – The Government's response and action plan* Cm 5830 London: The Stationery Office
www.dwp.gov.uk/publications/dwp/2003/pathways2work.pdf
- Department of Trade and Industry (DTI) (2003) *Equality and Diversity: Age Matters, Age Consultation 2003*
www.dti.gov.uk/er/equality/responses_report.pdf
- Donkin A, Goldblatt P, Lynch K. (2002) *Inequalities in life expectancy by social class 1972-1999*. *Health Statistics Quarterly* 15. Autumn 2002, Office for National Statistics
- Draper M. (2003) *Are we crossing older workers?* Pensions Week, 11 August 2003
- European Union Directive (Council Directive 2000/78/EC of 27 November 2000 establishing a general framework for equal treatment in employment and occupation
www.europa.eu.int/comm/employment_social/fundamental_rights/pdf/legisln/2000-78_en.pdf
- Evandrou M, Falkingham J. (2002) *Smoking behaviour and socio-economic status: a cohort analysis, 1974 to 1998*, *Health Statistics Quarterly* 14. Summer 2002, Office for National Statistics
- German Federal Ministry for Health and Social Security (2003) *Achieving Financial Sustainability in the Social Security System – The Commission Report*
www.mea.uniannheim.de/mea_neu/pages/files/topics/KomBerichtKurzEnglisch.pdf
- Government Actuary's Department (GAD) (2002) *Interim 2001 - based principal projections*
www.gad.gov.uk/Population/index.asp
- Grattan P. (2003) *Work after 60 – choice or necessity, burden or benefit?* Third Age Employment Network (TAEN)
www.taen.org.uk/index.htm

Gustman A, Steinmeier T. (2002) *The Social Security Early Entitlement Age in a Structural Model of Retirement and Wealth* NBER Working Paper No. W9183

House of Commons Work and Pensions Select Committee (2003) *The Future of UK Pensions Volumes I-III: Report and Proceedings of the Committee* HC 92-I-III London: The Stationery Office

IRS Employment Review (2003) *Legislation comes of age*, 15 August 2003
www.irsemploymentreview.com

Kelly S, Baker A, Gupta S. (2000) *Health life expectancy in Great Britain, 1980-96, and its use as an indicator in United Kingdom Government strategies*, Health Statistics Quarterly 07 Autumn 2000, Office for National Statistics

Marmot M, Wilkinson R.G. (2001) *Psychosocial and material pathways in the relation between income and health: a response to Lynch et al.* British Medical Journal 322 pp.1233-1236.

National Association of Pension Funds (NAPF) (2002) *Pensions – Plain and Simple*
www.napf.co.uk

O’Connell A. (2002) *Raising State Pension Age: Are we Ready?* London: Pensions Policy Institute

O’Connell, A. (2003) *A Guide to State Pension Reform* London: Pensions Policy Institute

OECD (2003) *Employment Outlook: 2003 Towards More and Better Jobs* www.oecd.org

Office for National Statistics (ONS) (2003) *Labour Market Trends, September*
www.statistics.gov.uk/downloads/theme_labour/LMT_September03.pdf

Rowlingson J. (2002) *Private Pension Planning: The Rhetoric of Responsibility, The Reality of Insecurity*, Journal of Social Policy 31,4: 623-642

Smeaton D, McKay S. (2003) *Working after State Pension Age: Quantitative Analysis* DWP Research Report 182

Smith A, McKay S. (2002) *Employers’ Pension Provision 2000*, Policy Studies Institute for the Department for Work and Pensions

Third Age Employment Network (TAEN) (2003) *Newsletter*, Summer 2003

Turner A. (2003) *The Macro-economics of Pensions*, Lecture to the Actuarial Profession, 2nd September 2003 www.pensionscommission.org.uk

Turner J. (2003) *Raising the Pensionable Age in US Social Security: An International Perspective* Public Policy Institute, AARP www.aarp.org