

**PENSIONS AND  
LIFETIME SAVINGS  
ASSOCIATION**

# **SECOND STATE PENSION AGE REVIEW: PLSA RESPONSE**

13 MAY 2022



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## **ABOUT THE PLSA**

Our mission is to help everyone achieve a better income in retirement. We work to get more people and money into retirement savings, to get more value out of those savings and to build the confidence and understanding of savers.

We represent the defined benefit, defined contribution, master trust and local authority pension schemes that together provide a retirement income to 20 million savers in the UK and invest £1 trillion in the UK and abroad. Our members also include asset managers, consultants, law firms, fintechs and others who play an influential role in the governance, investment, administration and management of people's financial futures.

## EXECUTIVE SUMMARY

- ▶ We believe the value of the state pension should be set at a level to protect pensioners from poverty and to ensure they do not fall behind a minimum level as a proportion of national average earnings. This is regardless of the generation in which an individual retires. Any changes should not disproportionately affect otherwise disadvantaged groups.
- ▶ Any changes to age must be considered in relation to changes in level and other considerations associated with the whole pension system; the State Pension is one of five pillars of the modern retirement system. A fixed proportion of life in retirement is a reasonable expectation to maintain.
- ▶ The UK will already have one of the highest State Pension ages in the OECD when it reaches 67 in 2028. (The average state pension age in the OECD will not reach this level until between 2044 and 2046.) However, as we understand that the Government's stated intent is to maintain about a third of expected adult life supported by the State Pension, the PLSA believes that it is appropriate to have no further increases in State Pension age. Instead there should be a period of stability, at minimum until further conditions are met.
- ▶ For any increase to the State Pension Age 15 years notice should be provided.
- ▶ Any changes to the State Pension Age could be conditional on assessment of the average proportion of healthy life (and life) to be lived in retirement, to maintain equal treatment across generations. This should also begin to reflect the capacity for work in later years, notwithstanding the changing nature of work potentially supporting longer working lives.
- ▶ The PLSA believes that retaining a single State Pension age is best to avoid confusion amongst savers, but the Government should be open to ideas to increase flexibility to retire early, in certain circumstances.

## Answers to Consultation Questions

### Introduction

Pensions adequacy is a key policy priority for the PLSA in 2022, and we will be actively considering the State Pension in depth. The State Pension makes up the majority of most people's retirement income<sup>1</sup> and as we will consider it in respect of different cohorts and generations, and its interaction with private saving levels. We would welcome the opportunity to continue to share our conclusions as we reach them in the months while the review is considering written responses.

### 3.1. Intergenerational fairness

#### **As people are living longer, how do we ensure the costs of State Pension are shared fairly across generations?**

If all generations can be sure of having a fixed proportion of their expected adult life receiving State Pension and the pension level is constant in real terms, and the age dependency ratio (working population v. pensioners) also remains constant, this will ensure that the the costs are shared fairly.

People need an adequate income in retirement and it needs to be fair across socio-economic groups and generations. We believe the value of the state pension should be set at a level to protect pensioners from poverty and to ensure they do not fall behind the average income level in society. A key question of how to define poverty as current measures in common usage vary between £8,000 (destitution) and £18,000 (relative poverty). The current value of a full new State Pension is £9,628 but we feel a strong case could be made for setting it somewhat higher, eg at the Joseph Rowntree Foundation Minimum Income Standard / Retirement Living Standards Minimum<sup>2</sup> level of £10,900. Clearly affordability issues will also be a key consideration.

#### **What factors relating to intergenerational fairness should be considered when determining the State Pension age?**

The factors worth considering in respect of intergenerational fairness are the proportion of life receiving the State Pension, the level of State Pension, and average wage.

When looking at other OECD countries there is a difference between how gains in life expectancy are linked to retirement ages. Some countries, link years gained to state pension age on a one-on-one basis and others increase by two thirds for every year of life expectancy

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<sup>1</sup> Independent Review of the State Pension age: Smoothing the Transition (2017)

<sup>2</sup> <https://www.retirementlivingstandards.org.uk/>

gained<sup>3</sup>. The latter has the advantage of allowing for time in retirement to increase proportionately with general life expectancy.

We believe that certain thresholds in terms of proportion of life and in respect of healthy life expectancy gaps narrowing need to be met before any further increases can occur. Changes should take account of the average proportion of healthy life to be lived in retirement to maintain equal treatment across generations. We believe that the value of the state pension should be set to protect pensioners from poverty, regardless of their generation. Please also see our answers to question 3.4 for wider discussion of fairness across and between different generations and socio economic groups.

### **Is it reasonable to give people a fixed period of notice for State Pension age changes, and if so what period?**

People should be given a fixed period of 15 years of notice for each increase to the State Pension age. Savers need sufficient time to adjust their work and retirement plans, particularly given the fixed ten year connection between normal minimum pension age and the state pension.

### **3.2. Changes in the nature of work**

#### **How have changes to the types of jobs people do affected working lives?**

The nature of some work has clearly moved from primary to tertiary sectors and this could help extend working lives, as is referenced in the Call for Evidence.

In the first State Pension review, evidence was shown of the gap in life expectancy between different types of occupations with a 3.9-year gap between male professionals and male routine workers, and a 3.1 year gap for females between the two<sup>4</sup>. This therefore, in effect, worsens the existing male life expectancy gap at 65, which is already 4.3 years.

Table A: Life expectancy at age 65 by NS-SEC class, 2007 to 2011 (ONS)

	Male Expectancy	LifeFemale Expectancy	Life
Higher Managerial and Professional (HMP)	20.3	22.5	
Lower Managerial and Professional (LMP)	19.3	21.9	
Intermediate	18.7	21.7	
Small Employers Own Account Workers (SEOAW)	18.7	21.9	
Lower Supervisory and Technical (LST)	18.0	20.1	

<sup>3</sup> Pensions at a Glance 2021 - OECD and G20 Indicators (OECD Library)

<sup>4</sup> Independent Review of the State Pension age: Smoothing the Transition (2017)

Semi-Routine	17.5	20.4
Routine	16.4	19.4
Unclassified	14.8	18.3
England and Wales	18.2	20.6

Although the ONS assessment of occupations takes account of physical demands, riskiness and health concerns related to the work, it is not adjusted for income levels and educational attainment. This suggests that the life expectancy gap and healthy life expectancy gap may not be impacted due to the nature of work alone.

There are theoretical arguments to suggest that the less physically demanding the work across a whole population on average, the more able people will be to work longer, but this does not take into account other factors, such as diminishing cognitive abilities, which may also have an effect.

We should also consider the proportion of life that is healthy, and therefore could enable longer worker; if healthy life expectancy at retirement age is unchanged then this should be taken into account when considering total years in retirement funded by the State. The proportion of people who have difficulties with activities of daily living increases with age. The percentage of people with at least one difficulty increases from 16.4 per cent at age 65 to around half of those aged 85. By people's late 80s, over one in three people have difficulty undertaking five or more activities of daily living<sup>5</sup>. For this reason it is not just healthy working lives, but also healthy retired lives, that are important to assess the appropriateness of the State Pension age and level.

### **What are the anticipated future changes to the workplace? How could this impact on people's working lives?**

Remote working is likely to allow more tertiary and quaternary workers to work later into their lives and balance work life with family commitments, but there has also been low wage growth and increasing mental illness in recent years which may have the opposite effect on the attractiveness and ability to stay in work for longer. Also, as we have raised elsewhere, the length of healthy retirement is also likely to impact on people's ability to work for longer in the future, regardless of any future changes to the workplace.

Increasing flexibility, particularly remote working, in some roles may also make it easier and more desirable to chose a phased retirement, for example by continuing part-time work. The first State Pension age Review identified that younger generations were much more prepared to work beyond age 65 where there was flexibility to decrease days and hours<sup>6</sup>.

<sup>5</sup> the\_health\_and\_care\_of\_older\_people\_in\_england\_2017.pdf (ageuk.org.uk)

<sup>6</sup> Independent Review of the State Pension age: Smoothing the Transition (2017)

According to the Health and Safety Executive, work related stress and mental illness was increasing even prior to the global pandemic, but then increased dramatically during the it<sup>7</sup>. This suggests that there is likely to be, longer term, an continued trend towards increasing work-related stress and mental illnesses, even after the shock of the pandemic.

Wage growth has been weak in the last 15 years and there have also been periods of real term decreases in total pay<sup>8</sup>. If this trend were to continue, this would make it harder for people to save for adequate private and occupational pension provision to meet the Retirement Living Standard's minimum of £10,900 p.a. for a single person outside of London<sup>9</sup>.

### **What factors do people consider when making decisions about when to retire?**

As noted in the last State Pension age Review, key factors include affordability, health, family and redundancy from work between the ages of 50 and 64<sup>10</sup>.

Pension Freedoms have made it possible for people to start withdrawing from the Labour force and using private pension to retire from the Normal Minimum Pension Age (NMPA) of 55 (increasing to 57 in April 2028). For those with reasons to withdraw from the labour force early before this age, assessing their budget in retirement will be key. Helping savers to picture their future lifestyle, and their required budget for this, especially where they are trying to do so ahead of State Pension entitlement is very complex, which is one of the reasons why we have encouraged the adoption of the Retirement Living Standards<sup>11</sup>.

The last State Pension age Review noted that there was a strong correlation between the age most people withdraw from the labour force/retiring and the State Pension age. This is probably due to both the large proportion of retirement income provided by the State Pension for most people but also due to the “anchoring” behavioural effect of the State Pension age. It is therefore important to assess the degree to which the Normal Minimum Pension Age and/or the State Pension Age (the former fixed at ten years earlier than the latter) in and of itself prompts retirement, especially in the absence of understanding the complexity of retirement income needs.

### **3.3. Sustainability and affordability**

#### **What is the most sustainable and affordable way of managing the cost of State Pension in the longer term? What are the advantages and disadvantages of potential options?**

The UK government has made more progress than many other OECD countries in making the State Pension sustainable for the long term.

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<sup>7</sup> <https://www.hse.gov.uk/statistics/causdis/stress.pdf>

<sup>8</sup> <https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/employmentandemployeetypes/bulletins/averageweeklyearningsingreatbritain/latest>

<sup>9</sup> <https://www.retirementlivingstandards.org.uk/>

<sup>10</sup> Independent Review of the State Pension age: Smoothing the Transition (2017)

<sup>11</sup> <https://www.retirementlivingstandards.org.uk/>

Given the ‘black swan’ events that we have experienced in recent times, such as the global pandemic and the cost of living crisis, there is a strong case for suspending plans to make more changes to the State Pension age. The long term effects on life expectancy, particularly healthy life expectancy, cost of living and future of working are unknown.

As noted in our response to question 3.1, we believe the value of the state pension should be set at a level to protect pensioners from poverty and to ensure they do not fall behind the average income level in society. We feel a strong case could be made for setting it somewhat higher, eg at the Joseph Rowntree Foundation Minimum Income Standard / Retirement Living Standards Minimum level of £10,900<sup>12</sup>. Clearly affordability issues will also be a key consideration.

For example, the triple lock is a vital increase mechanism, but it could in the future be adapted to tracking earnings once it reaches a minimum poverty avoidance income level, such as the PLSA’s minimum Retirement Living Standard of £10,900 pa<sup>13</sup>.

The interaction of State Pension and state welfare benefits has also got to be considered, as increasing the State Pension age on financial sustainability grounds may be disadvantageous and counter-productive. If people retire earlier than the State Pension age and spend all their private and occupational pension provision in the period before they can draw their State Pension, there is a risk that they may be dependent on other State support and welfare benefits. There is already some evidence to suggest this is likely to happen. According to the PPI, the number of people aged 65 on means-tested benefits rose by over 130,000 with rises in SPa<sup>14</sup>. Therefore, before any further increases in State Pension Age is introduced, modelling should be undertaken to assess the saving, if any, overall to the State from increasing the age at any time.

### **3.4. Metrics for setting State Pension age**

#### **Is it reasonable for people to expect to spend a fixed proportion of their adult life in receipt of State Pension?**

The Government established in 2013 that people should expect to spend “up to one third of their adult life in retirement”<sup>15</sup>. We believe this is a reasonable position to take in light of the long years of national insurance and tax contributions made by individuals, and by the fact as workers they have already supported previous generations in retirement. In addition, although, on average, people live around 20 years after State Pension Age, in practice, many die much younger, or have illnesses or disabilities that making continued work not possible.

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<sup>12</sup> 2021 figure, <https://www.retirementlivingstandards.org.uk/>

<sup>13</sup> <https://www.retirementlivingstandards.org.uk/>

<sup>14</sup> <https://www.pensionspolicyinstitute.org.uk/media/4008/20220112-spa-age-uk-rt-write-up-final.pdf>

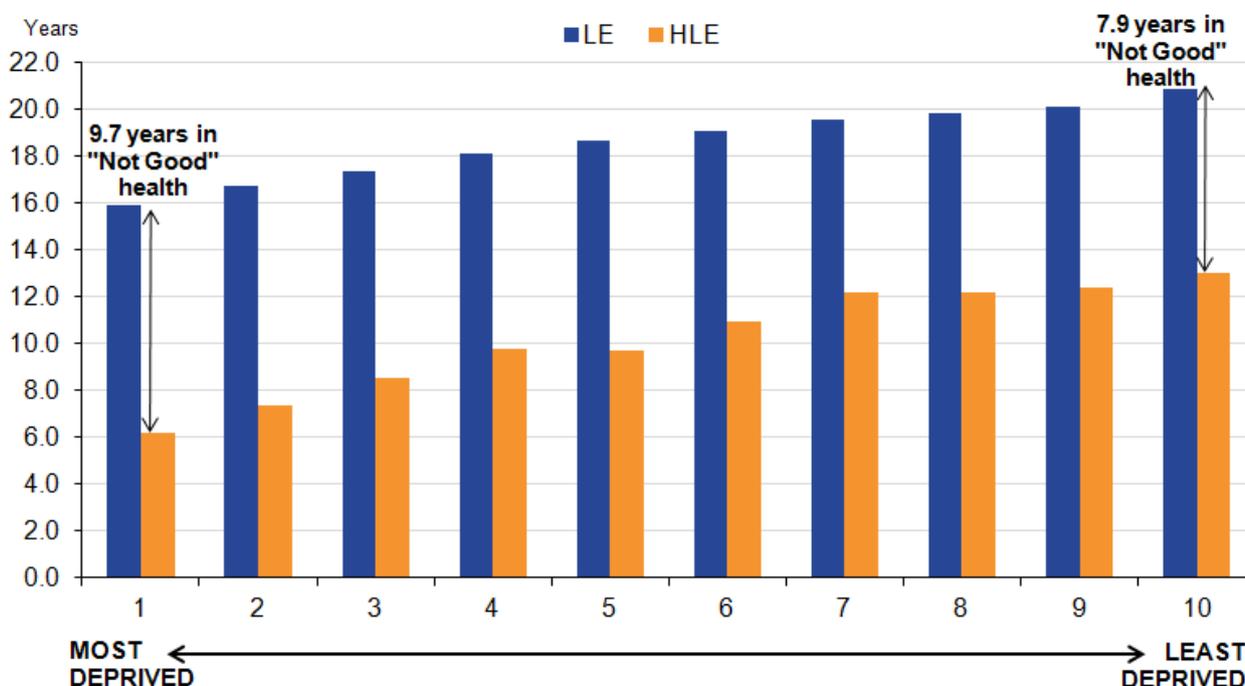
<sup>15</sup> Ibid.

Moreover, the State Pension makes up the vast proportion of most people’s retirement income and, in effect, by connecting proportion with the eligibility for and overall composition of the State Pension retirement as a phase of life is protected<sup>16</sup>.

Maintenance of one third of expected adult life in retirement can be achieved by increasing State Pension age by 8 months for every year increase in life expectancy, as the Government’s Actuarial Department found in the last review and as also already done in some OECD countries<sup>17</sup>. For countries with a one-to-one link, the increase was observed to be too aggressive, as it implied that all longevity improvements were passed into the retirement age, and so steadily reduced the share of adult life spent in retirement.

It may also prove reasonable to put in place a coefficient that centres around healthy living from age 65 onwards. In some OECD countries the health gap between different socio-demographic groups has been increasing whilst in others it has been narrowing. The UK is identified by the OECD as a country where the trend data for a health gap is unclear. It should be considered whether a condition for increasing the State Pension age further should be only where there is a clearly identifiable long-term trend of health gaps narrowing<sup>18</sup>. This would ensure that certain socio-economic groups are not disadvantaged from any increases in age.

Chart A: Healthy life expectancy and life expectancy for men at age 65 by national deciles of area deprivation, England 2012 to 2014 (ONS)



<sup>16</sup> Independent Review of the State Pension age: Smoothing the Transition (2017)

<sup>17</sup> Pensions at a Glance 2021 - OECD and G20 Indicators (OECD Library)

<sup>18</sup> Ibid.

For example, data from the ONS on Healthy Life expectancy (from birth) between 2018-2020 shows both regional disparity and a downward trend in most regions of the UK.

Healthy life expectancy, and the gaps between years of life in healthy and unhealthy condition, need to be taken into account when deciding State Pension age to ensure that the single age is set fairly across generations.

**Are there options for taking account of differences in circumstances when setting State Pension age in future? What are the advantages and disadvantages of these options, and how could they operate within the current pensions framework?**

We believe that there should be a single State Pension age for all, but particularly were it to increase any higher than currently planned, we believe that there should be some flexibility introduced to allow people to receive it earlier. This could be protective of some of the unintended consequences we noted earlier in our response, such as increasing claims for means tested benefits for those approaching retirement age and poorer outcomes for certain socio economic groups.

One option would be to introduce the same level of flexibility for drawing the UK State Pension early as there is already for delaying receiving of the State Pension, ie allowing people to take it 3 years earlier, probably relying on an actuarial reduction as is seen in the United States. Care would have to be taken with this approach to ensure that people are not locked into poverty, especially in desperate or hardship circumstances. For this reason it may be reasonable to limit entitlement to early drawing of the State Pension where other sources of income are not readily available. (It might be necessary to choose a level of proven retirement income before allowing early taking of the State Pension, eg. the Retirement Living Standards Minimum level.)

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

The current projection model is too sensitive to short term changes and less sensitive to long term trends.

According to the PPI, ONS population projections are based on current and short-term mortality trends blended with longer-term trends. Shorter-term mortality is heavily affected by recent events. Longer-term trends are based on the best extrapolation and best estimate, so this needs to be taken into consideration when making decisions based on these figures<sup>19</sup>. A metric that takes into account both short term and longer-term trends in better balance, and one that also considers healthy life expectancy, would be preferable.

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<sup>19</sup> <https://www.pensionspolicyinstitute.org.uk/media/4008/20220112-spa-age-uk-rt-write-up-final.pdf>

### **Are there other metrics which are relevant or more suitable to help determine State Pension age in future, and if so, what metrics?**

Currently our view is that healthy life expectancy from age 65 (and life expectancy from 65) are the best metrics to use, as they are more robust data sets and give a clearer indication of the true length of time receiving State Pension/retirement (and how healthy that retirement is likely to be).

It is possible that a coefficient could be designed that allowed for an increase in State Pension age based on both life expectancy and healthy life expectancy, and where healthy life expectancy gaps are seen to be narrowing or low.

Thresholds in respect of healthy life expectancy, and affordability of providing minimum levels of retirement income, alongside the proportion of life in retirement should all be met before allowing any further increases in State Pension age.

### **What factors do other countries consider when determining State Pension age?**

Other OECD countries determine State Pension age on the basis of longevity, healthy life expectancy and contributions record.

In the 2021, OECD publication of *Pensions at a Glance*, it was noted that many countries had taken some limited action towards increasing state pension ages, with on average the pension age set to increase from 64.2 years to 66.1 years<sup>20</sup>. As noted above, this is often less action than the UK has already planned – where the State Pension Age will rise to 67 in 2028.

In answering this question, we have focused on two OECD countries with high pension ages, the Netherlands and Denmark, because they have private pension systems that are more comparable to the UK system. We have also selected them to spotlight as they represent economic and cultural similarities, though we have sought to summarise the contrasts with the UK system to highlight possible opportunities and challenges.

#### *Netherlands*

The Old Age Pension pension amounts to a percentage of the statutory minimum wage at the time. The amount a pensioner will receive generally depends on two factors, relationship status and how long they have lived/worked in the Netherlands <sup>21</sup>.

The Netherlands modified the link between retirement age and life expectancy. For each year of life expectancy gains at age 65, the pace of the increase in the retirement age applying to the basic pension will be eight months in 2025 rather than the initially foreseen one year increase<sup>22</sup>. The one-to-one link was too fast, as it implied that all longevity improvements were passed into the retirement age, hence steadily reducing the share of adult life spent in

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<sup>20</sup> Pensions at a Glance 2021 - OECD and G20 Indicators (OECD Library)

<sup>21</sup> <https://business.gov.nl/regulation/pension/>

<sup>22</sup> Pensions at a Glance 2021 - OECD and G20 Indicators (OECD Library)

retirement. At the same time, the increase of the retirement age from 66 and 4 months to 67 was postponed from 2021 to 2024.

As a result, based on current life-expectancy projections, the retirement age for someone entering the labour market at age 22 now will reach 69, and will no longer be 71 years as previously predicted by the OECD<sup>23</sup>.

### *Denmark*

In Denmark, from January 2022, those who have been contributing/ or credited for at least 42 years before the age of 61 will be able to receive a benefit equal to the basic pension amount up to three years before the normal retirement age of 67<sup>24</sup>.

The State Pension age in Denmark is rising to 69 for those born on or after 1 January 1967, and therefore it is our view that having a system of early retirement for those with credits is a useful mitigation to this otherwise high age.

### **3.5. Additional information**

**Do you have any other comments which relate to the Terms of Reference of this review, that you wish to share?**

The PLSA is looking at pensions adequacy as a whole this year, which will include the interaction of State Pension with private and occupational pensions in the overall framework to enable people to achieve an adequate income in retirement. We will look at this interaction across different socio-economic cohorts and generations. We would be happy to share our further thoughts with this review, as they are developed in the coming weeks and months.

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<sup>23</sup> Pensions at a Glance 2021 - OECD and G20 Indicators (OECD Library)

<sup>24</sup> <https://lifeindenmark.borger.dk/pension/state-pension>

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