

When Should the State Pension Age Increase to 66? The NAPF response to the Call to Evidence, August 2010

Introduction

1. **The National Association of Pension Funds (NAPF) is the leading voice of workplace pensions in the UK. We speak for 1,200 pension schemes with some 15 million members and assets of around £800 billion. NAPF members also include over 400 businesses providing essential services to the pensions sector.**
2. The NAPF fully supports the Coalition Government's objective to achieve a more equitable state pension for both current and future pensioners. The State Pension system has an important role to play in providing an adequate retirement income for the UK's pensioners and in providing a solid foundation on which to base private pension saving.

Executive Summary

The NAPF recognises the need to establish a state pension system which is sustainable in the long term. Trends in longevity mean the costs of providing the state pension will rise in the future. Accelerating the rate at which the State Pension Age (SPA) will increase is one way to contain the cost of providing the state pension.

The NAPF believes the Government must consider the impact these changes will have both on individuals and their retirement savings plans and also pension schemes whose benefits are also linked to state pensions. In particular, NAPF recommends that:

- Individuals must be given enough time to adjust their retirement ages and to make any additional savings to fill the gap in their income. An increase in SPA for men in 2016 would give them only six years to prepare. Six years is simply not long enough.
- The accelerated increase in SPA to 66 should not occur any earlier than 2020 and it should increase at the same time for men and women.
- The increase should occur over a two year period from 2020 to 2022. The increase in SPA for men and women to 68 will occur in three tranches, each lasting two years. The proposal to accelerate the increase in SPA to 66 is no less significant. A two-year phasing-in period would help mitigate the impact of this change on the cohort of individuals most likely to be affected.
- The Government should also introduce measures to help people remain in work for longer. The Government must not, however, simply consider the age at which the state pension is paid, but also the level at which it is paid. We recommend the Government should introduce a new Foundation Pension,

paid at £8000 a year. This would lift 2 million pensioners out of means testing.

Introduction

3. The NAPF recognises the need to establish a State Pension system which is sustainable in the long term. Trends in longevity mean that the cost of providing the State Pension will rise in the future. Escalating the rate at which the State Pension Age (SPA) will increase is one way to contain the future costs of the state pension.
4. But we cannot ask pensioners to work longer in exchange for an inadequate state pension. We welcome this Government's commitment to restore the link between earnings and the Basic State Pension from April 2011 and to introduce the "triple guarantee". But in our view this does not go far enough. The UK has one of the lowest state pensions in the developed world as even the Pensions Commission acknowledged, it is also one of the most complicated.

A new state pension settlement: The Foundation Pension

5. In our report *Fit for the Future: NAPF's Vision for Pensions*, we proposed the creation of a Foundation Pension.

The Foundation Pension

- The Foundation Pension would combine the current basic state pension and state second pension to form a single, universal, flat-rate benefit.
- The FP would be worth £8,000 a year – around a third of male median earnings. A full Foundation Pension would be earned after 30 years of NI contributions.
- It would be paid on an individual basis to everyone over state pension age.
- Once in payment it would increase annually in line with the triple guarantee.

No-one would be left worse off as a result of the introduction of the Foundation Pension, and many pensioners would receive an increase in their weekly income of £25 a week. The Foundation Pension could lift around 2 million pensioners out of means testing. To help pay for a more generous state pension foundation, SPA would need to rise beyond the currently planned age 68 to age 70. However, our research shows that people are willing to work longer if they know that, in exchange, they will receive a more generous State Pension. 57% of respondents said they would be willing to work an extra 2 years in exchange for the more generous Foundation Pension. Younger people were most likely to be prepared to work the extra years, but even amongst those closest to retirement (55-64), 58% said they would be prepared to work longer in return for a higher state pension.¹

¹ Fit for the Future: NAPF Vision for Pensions. NAPF, March 2010

Minimising effects on individuals

6. In line with current policy, any changes in SPA should aim to be the same for both men and women. While SPA for men is already 65, for women it is currently rising from 60 to 65 over a ten-year period. (Between April 2010 and April 2020, women's SPA will rise incrementally in a one-month on, one-month off fashion.) Given the scale of the change, no future change to women's SPA should be introduced before 2020. To introduce the increase for men in 2016 and women in 2020 would not only be unfair, but also run the risk of legal challenge.
7. Given that current evidence suggests many individuals may find it difficult to find work between the ages of 65 and 66², the Government should ensure that no increase in SPA is introduced which does not allow those who are affected by the changes enough time to make additional retirement saving. It has been estimated by the Pensions Policy Institute (PPI) that single pensioners need at least £6,200 a year to meet minimum standards of living. To ensure that all individuals have at least this amount in extra savings, they will need at least 10 years notice period. In our view the proposal to give men only a 6 year notice period to prepare for the increase in SPA is too short. This suggests there should be no change in the male SPA before 2020.
8. In light of both the above points, we would urge the Government to phase in the accelerated increase in SPA to 66 for both men and women between 2020 and 2022, as it will be important to protect the individuals most likely to be affected by the faster increase.
9. However, many people may not be able to stay in work until they reach State Pension Age because of ill-health or simply because the job market cannot accommodate them. The Government should consider, as part of its cost-benefit analysis, the impact increasing SPA to 66 at a faster rate would have on means tested benefit spending. Individuals who are unable to work until SPA may fall back on other means tested benefits such as incapacity benefit prior to reaching SPA.
10. Any increase in SPA should only take place if measures are introduced to help people work longer. Today, average retirement age for men is 64.5 and for women it is 62.³ The Government should look closely at examples provided by other countries with higher retirement ages and at experiences in the UK which indicate the cultural, economic and legal factors needed to encourage a move

² The percentage of individuals in full-time and part-time employment from age 65-69 is only 20%.

³ ONS Pension Trends, "Labour Market and Retirement," December 2009.

towards higher retirement ages. This should include a sample of employer and individual attitudes.

Effects of increasing SPA on pension schemes

11. Increasing SPA for individuals who already have pensions in payment could have adverse effects on many pension schemes, especially Defined Benefit (DB) schemes. Many DB pension schemes provide “bridging” pensions as an option on retirement, as a way to make up income until an individual receives his or her State Pension. Individuals receive an additional payment on their pension prior to reaching SPA. Payments made after reaching SPA are actuarially reduced.
12. The PPI estimates that the group of individuals who will be most affected by a faster increase in SPA to 66 are the cohort of individuals aged 50-59.⁴ Current rules allow individuals to take their pension at age 55 (prior to April 2010, the minimum age was 50). This means that some individuals who are already in receipt of bridging pensions would receive their additional payment for up to an extra year, thus adding to scheme liabilities.
13. This problem could be mitigated by carefully amending the Pensions Act 1995 to say that, when SPA has been relied upon by occupational pension schemes in connection with discretionary benefits such as bridging pensions already granted, trustees can choose to use the SPA as set out in new legislation, or SPA as set when the decision was made.

Answers to Specific Questions

What evidence concerning changes in life expectancy and the changed economic context should be taken into account when bringing forward the increase in state pension age to 66?

14. The trend towards working longer is an inevitable one. The Pensions Commission itself paved the way in its first report and the concept of working longer is now widely accepted as a necessity. In the UK today there are already more people over retirement age than there are under the age of 16. And in the future, the population of those over state pension age is set to rise by 32%. In contrast, the working age population will increase by only 14%.
15. Increasing life expectancy and the demographic shift towards an older population will, on the surface, be good news for those individuals who will choose to work for longer. With the working age population in decline, any labour market activity needed to stimulate economic growth will need to be filled by older workers.

⁴ PPI briefing note 53, “Could increases in State Pension Age be brought forward?” 2009.

16. However, for a faster increase in SPA to 66 to have a positive affect on extending working lives, the Government must be proactive in tackling other issues such as health inequalities and employment practices, as the Marmot Review of Health Inequalities recently identified. While average life expectancy across the UK is rising, the figures hide the fact that people living in the poorest neighbourhoods in England will, on average, live seven years less than people living in the richest neighbourhoods. According to ONS figures, the lowest life expectancy at age 65 in parts of Scotland is 15.7 years⁵. This is almost 10 years lower than life expectancy in wealthy parts of London. As these figures are an average, there will be individuals in some parts of the UK living for only a few years after age 65.
17. For these individuals, a faster increase in SPA to 66 would be unfair. If SPA increases more quickly than life expectancy for a particular social class, some individuals may not live long enough to receive their State Pension and they would receive the State Pension for a disproportionately shorter time than individuals in a different social class.

What evidence should the Government consider when deciding the notice period for individuals affected by a change to the timing of the state pension age increase to 66?

18. The decision to increase SPA at a faster rate will impact different sets of individuals in different ways. As noted above, the group of people who will probably be most affected by the accelerated increase will be those currently aged 50-59.
19. Women included in this cohort of individuals will have already been affected by the equalisation of women's State Pension Age. For these individuals, a faster increase to 66 will shift their State Pension Age forward once more. It will be important to consider the impact this could have on these individuals' retirement plans and on their emotional well-being. Phasing the increase in SPA over a period of months or years would give this group longer to prepare financially.
20. Phasing the increase over a longer period of time would also give individuals more time to adjust their retirement plans and therefore could result in more people working for longer. About 80% of men aged 50-59 and 60% of men aged 60-64 are employed, but this number drops to 20% for men aged 65-69⁶. This suggests there is little correlation between SPA and when individuals actually retire.
21. It is also important to note that 20% of the 50-59 aged cohort is already retired and many more will retire in the next few years. People may retire early because

⁵ ONS, "Life Expectancy at birth and at age 65 by local areas in the United Kingdom, 2006-2008", October 2009.

⁶ PPI briefing note 53, "Could increases in State Pension Age be brought forward?" 2009

they can afford to, but many more retire early for ill-health reasons. These individuals may find it difficult to cope with the faster increase in SPA, especially if they experience difficulties re-entering the job market.

22. The increases in SPA which have already been legislated for in the Pensions Act 2007 will be phased in over three 2-year periods. These changes were also introduced with a 13 year notice period. We believe the proposed faster increase of SPA to 66 will be no less significant for individuals. The notice period for these changes should be as long as possible.

What evidence should the Government consider to ensure no group is disproportionately impacted by the level of the state pension age and any change to the timing of the state pension age increase to 66?

23. It will be important to protect the cohort of individuals likely to be most affected by the proposed faster increase in SPA to 66. A phased introduction, in conjunction with a long notice period, would be the best way to mitigate the affects of the increase.

24. The Pensions Act 2007 set out a timetable for the increase in SPA from 65 to 65 over a two year period. NAPF recommends that the Government take a similar approach to this increase. In this scenario, the increase in SPA for women from 60 to 65 would continue from 2020 with men joining the stream at 2020 so that all men and women reach SPA of 66 by 6th April 2022.

Date of Birth	Date of Retirement
6 th April 1955 to 5 th May 1955	6 th May 2020
6 th May 1955 to 5 th June 1955	6 th July 2020
6 th June 1955 to 5 th July 1955	6 th September 2020
6 th July 1955 to 5 th August 1955	6 th November 2020
6 th August 1955 to 5 th September 1955	6 th January 2021
6 th September 1955 to 5 th October 1955	6 th March 2021
6 th October 1955 to 5 th November 1955	6 th May 2021
6 th November 1955 to 5 th December 1955	6 th July 2021
6 th December 1955 to 5 th January 1956	6 th September 2021
6 th January 1956 to 5 th February 1956	6 th November 2021
6 th February 1956 to 5 th March 1956	6 th January 2022
6 th March 1956 to 5 th April 1956	6 th March 2022

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Annex A

In February 2010, NAPF surveyed 1,248 members of the public as part of our annual Workplace Pensions Survey.

If a guaranteed state pension worth £8,000 per year was offered, respondents said they would save more into their own arrangements. In 27% of cases, this was just £0-£24, but 12% said that they would save £200 or more per month extra while another 16% said that they would save between £100 and £200 extra per month.

Figure 1 Would you be prepared to work 2 years longer if it meant you get a guaranteed state pension of £8,000 per year compared to £6,800?

