PENSIONS POLICY INSTITUTE

PPI

Retirement income and assets: do pensioners have sufficient income to meet their needs?

The PPI is grateful for the support of the following sponsors of this project:

Sponsorship has been given to help fund the research, and does not necessarily imply agreement with, or support for, the analysis or findings from the project.

A Discussion Paper by Daniela Silcock, Sean James and John Adams

Published by the Pensions Policy Institute

ISBN - 978-1-906284-08-4
www.pensionspolicyinstitute.org.uk

Retirement income and assets: do pensioners have sufficient income to meet their needs?

Introduction

This report is the first in a series of reports looking at the evolution of needs for income during the course of retirement and the roles that different income and assets could play in helping pensioners to meet their needs for retirement income. The project has the overall aim of providing independent evidence to inform debate about the role of different types of income and assets in funding retirement.

Recent pension policy developments in the UK have mostly been targeted at the accumulation of assets to fund retirement income, for example, the introduction of auto-enrolment, compulsory employer contributions and personal accounts. There has been some research on the use of assets in retirement, however most of the research has examined particular assets in isolation. The HM Treasury review of annuitisation considered only private pension assets; previous PPI work has considered the potential role of property in supporting retirement; DWP research has focussed on possible needs in retirement.

There is a need for a holistic consideration of the evolution of financial needs during the course of retirement and the roles that different sources of income and assets could have in meeting these needs, combined, as well as in isolation.

This report examines how the income needs of pensioners could be measured, and explores how pensioners' needs for retirement income vary over time and for different individuals and households. This report also looks at the sources of income which pensioners use in retirement and how the levels of income tend to change for pensioners during retirement.

Finally, this report uses scenarios that illustrate the potential outcomes of several possible variations of need in retirement, such as the onset of disability, residential care and widowhood, and analyses how different baskets of assets and income may be able to fund pensioners who experience varying needs in retirement. In this report pensioner refers to any person over State Pension Age (SPA) (currently 65 for men and 60 for women).

Chapter 1 discusses the most common approaches to measuring pensioners' needs for retirement income and examines how needs vary across different types of households.

Chapter 2 analyses the way income needs change for people after SPA, focussing especially on the effects of age and health on income needs.

Chapter 3 investigates the main sources of income for pensioners and analyses the implications that different types of income have for the level of income pensioners receive. It examines how income sources change as people age and how sources vary across different household units.

Chapter 4 uses hypothetical individuals and couples to examine how different baskets of assets and income might be able to fund different needs in retirement.

Further reports in this series will examine the role of housing assets and the role of pensions and other savings in funding retirement. A final concluding report will draw out the overall findings from the retirement income and assets project as a whole.

Summary of Conclusions

While many measurements of the income needs of pensioners are focused on the minimum income a pensioner would require in order to meet their basic needs, many people feel that they would like to have a standard of living similar to the one that they experienced in their working life, in order to be satisfied with their income in retirement.

The main calculations of the minimum income required to meet basic needs tend to conclude that a single pensioner needs around £120 per week (after housing costs)[1] in 2008 earning terms, and the calculations of what income a median-earning pensioner would require to achieve an adequate standard of living in retirement (based on expectations) tend to conclude that they would require around £250 per week (before housing costs)[2] in 2008 earnings terms.

The level of income that a pensioner household unit requires in order to meet their needs or expectations in retirement could vary between different households. The main variations are between single and multi-occupant households and between single male and female pensioner households.

It is not possible to calculate a single level of income that would be suitable for all pensioners to meet their needs or expectations in retirement, though minimum and desired income measures can provide a useful guide. The level of income required by any pensioner may be dependent on their desired standard of living in retirement, the structure and location of their household and their health needs.

Expenditure variations across household units indicate that:

- Households with more than one person in them are more likely to spend money on goods associated with leisure activities.
- Single pensioners may have more income needs for care inside or outside the home than pensioner couples.
- Male and female pensioners have different spending patterns across categories of expenditure including personal goods and services, transport, motoring, clothing and footwear.

As well as varying across household units, income needs also vary during retirement due to a combination of needs, expectations and spending preferences.

- Pensioners tend to spend a large proportion of income on leisure and recreation in the early years of retirement (ages 65 to early 70s).

[1] It is useful to look at income after housing costs have been subtracted because it shows more clearly the income that is available for spending
[2] Replacement rate income tends to be calculated in before housing costs terms

- Pensioners tend to decrease spending during the middle years of retirement (around ages 75 to 85) as a result of losses in mobility.
- Spending tends to increase again around age 85 as a result of the need for health related expenditure.
- Pensioners tend to reduce spending once more around age 90 as the need for spending on health, fuel, food and housing becomes paramount but expenditure on other goods drops off as a result of either mobility, preferences or the need to conserve income.

It is possible that pensioner households who receive the average level of income for their age group could find it difficult to meet both of the spending peaks in early and later retirement as pensioners' income tends to decrease during retirement. Most of the pensioners modelled in this research see a drop in their income in later retirement as their pension income fails to keep its value in real (earnings) terms. Even higher income pensioners may not be able to meet all of their spending preferences solely from income if they aim to have a standard of living similar to that they had in their working life.

The findings from the PPI modelling undertaken for this report suggest that:

- None of the individuals modelled, even those on median to high earnings, are able to meet a replacement rate calculated to replicate working-life living standards in retirement[3] solely from their pension income though they may be able to meet their replacement rates for some or all of their retirement by using their savings and/or releasing equity from their homes.

- Pensioners who earned at median to high levels during their working life and have complete (private or occupational) pension saving records, could find it easier to meet many of their needs in retirement from income alone.

- Pensioners may find it easier to maintain similar consumption levels in retirement to those they experienced in working life if they have a combination of assets and savings to use in retirement as well as income from state and private pensions.

- Pensioners may find it easier to meet changes in needs and expenditure preferences if they conserve their income during some of the years of their retirement and spend more than their average yearly income during others. They may also wish to supplement their pension income with income from assets and savings during times where greater expenditure may be needed to meet changes in needs or preferences.

[3] Pensions Commission replacement rate, (Table 13), Pensions Commission (2004)

- Working part or full-time after State Pension Age can increase pensioner income which can be used to boost expenditure during the years in which is it is earned, or can be saved and used later in retirement to meet changes in needs and spending preferences. Working part time after SPA can be a way to ease the transition into receiving a lower income in retirement.

- Acquiring a disability in retirement could reduce available income depending on the severity level of the disability and the level of state benefits which pensioners receive as a result of their disability. Acquiring a high severity disability in retirement could incur a very high level of costs which pensioners may not be able to afford on their own. Pensioners with one or more disabilities may need to depend on family, or receive state support in the form of Local Authority or NHS care, depending on the level of costs incurred by their disability.

- Pensioners in couples are likely to have a higher level of available income than single pensioners. Living expenses, including housing, and the costs of disability are likely to be lower per person in pensioner couples than for single pensioners. Pensioners in couples also have the possibility of benefiting from a partners higher pension entitlement.

- Pensioners who have lost a partner are likely to have a higher income than pensioners who were never partnered but have the same income and earnings history, due to receiving entitlement from their partner's state pension and possibly their private or occupational pensions.

Chapter one: What income needs do people have after State Pension Age?

There are several ways of approaching a measurement of the needs and expectations that people might have after State Pension Age (SPA). There are also different approaches to calculating the level of income that pensioners could require in order to meet their needs or expectations. This chapter discusses the most common approaches to measuring needs and calculating required or expected income levels, and examines how needs vary across different types of household units.

There are two main approaches to calculating the income needs of pensioners

There are several ways to approach a calculation of 'income needs'. One of the main ways of measuring income needs is to assess the minimum income level which an individual requires to meet their basic needs and achieve a minimum standard of living, though a minimum standard of living may seem unacceptable to many pensioners who are used to a higher standard of living.

Measures of basic minimum income include:

- The Government's 'poverty lines'
- Guarantee Credit
- A Minimum Income Standard
- Lists of necessary items

Alternatively, measurements are also approached by assessing how much income people feel that they need in order to achieve a standard of living which they find acceptable. For people in retirement, satisfaction with income is often measured by whether an individual is able to achieve the same (or a similar) standard of living to the one which they experienced during their working life. This could be measured by looking at whether people are able to replicate the consumption levels they experienced during working life when they are in retirement.

Measures of acceptable or expected standard of living include:

- Replacement rate
- Expenditure

Table 1 sets out some possible minimum acceptable income calculations for pensioners in the UK. These calculations are based on both basic minimum income measures and measures which focus on replicating standards of living from working life.

Table 1[4]: Possible minimum income measures for pensioners in 2008 values, income per week

Minimum income measure	Individual pensioner	Pensioner couple
Government's relative poverty line[5] (AHC)[6]	£122	£211
Guarantee Credit[7] (AHC)	£124.05	£189.35
Minimum Income Standard[8] (AHC)	£113.27 (male) £124.04 (female)	£183.72
Replacement rate (between 50 - 80% of income during working life)[9] (BHC)[10]	60% high earners - £433 70% median earners - £264 80% low earners - £192	
Expenditure	£151.30 – 185.00 (BHC) 2007[11]	£337.70 (AHC)[12]

There are several ways of measuring basic income needs
Although this paper attempts to classify needs for the purpose of identifying the income needs of those over SPA, identifying the difference between needs and wants is inevitably subjective. However there is a social consensus in the UK that 'needs' refers to more than just the basic food and shelter that an individual requires in order to survive. Whether households have the minimum income that they need is often measured by whether or not they are considered to be in poverty or social exclusion. The Government defines social exclusion as '*a short–hand term for what can happen when people or areas have a combination of linked problems, such as unemployment, discrimination, poor skills, low incomes, poor housing, high crime and family breakdown. These problems are linked and mutually reinforcing.*'[13]

Studies on the effects of social exclusion on people's health and quality of life have lead researchers to conclude that the ability to participate socially and culturally, gain skills, and see friends and family are essential elements of a minimally acceptable standard of living in the UK. People who cannot afford to participate socially, or do not have an income sufficient to maintain a minimum acceptable standard of living, could be considered to be in poverty or social exclusion.

4 PPI Research
5 DWP (2008a) 2006/07 figures uprated by Sept RPI
6 After Housing Costs
7 www.thepensionservice.gov.uk/pensioncredit/age65.asp, 2008/2009 rates
8 JRF (2008)
9 Pensions Commission (2004) p. 135
10 Before Housing Costs
11 ONS (2008a), only available in BHC figures
12 JRF (2008) data from 2008 Expenditure and Food Survey, only available in AHC figures
13 www.cabinetoffice.gov.uk/social_exclusion_task_force/context.aspx

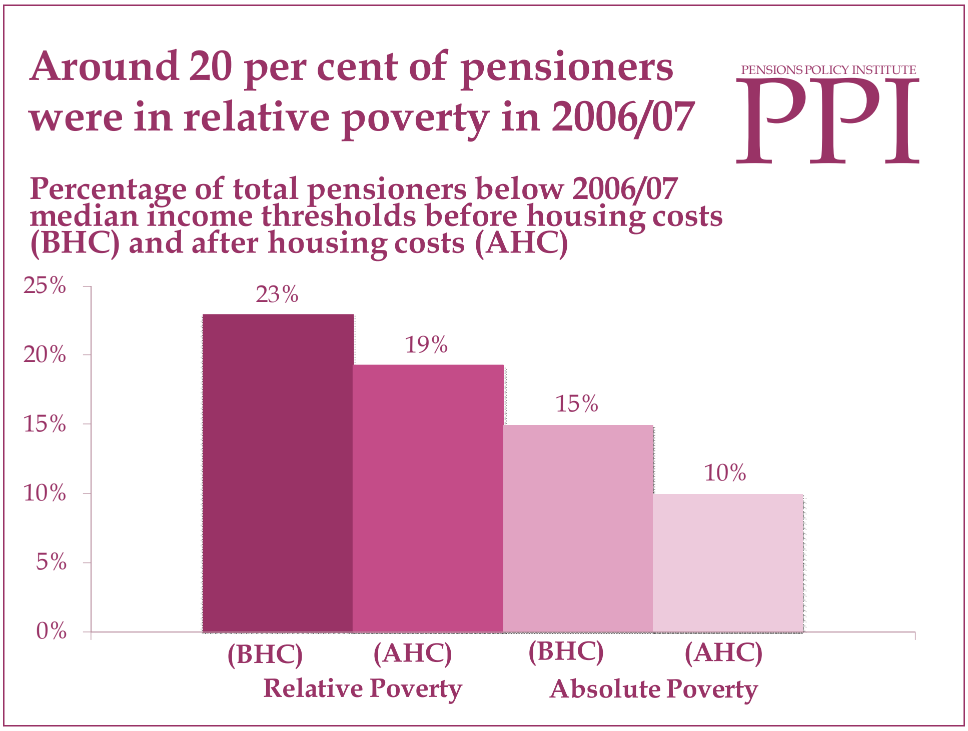
The poverty line

The Government considers a household to be in poverty if they cannot afford a minimum decent standard of living, or are in danger of social exclusion due to their income.

- **Relative poverty**[14] – a household is considered to be in relative poverty (Chart 1) if their income is below 60% of the median income of households in the UK. The relative poverty line therefore fluctuates with changes in national income and it measures people's income in relation to the standard of living in the UK at any given time. For 2008 the relative poverty line after housing costs (AHC) is £122 per week for single pensioners and £211 per week for pensioner couples.[15] The relative poverty line is not based on a thorough assessment of what households need, but is useful for making consistent comparisons between groups, over time and across countries. However, relative poverty line amounts are similar to those calculated by the Minimum Income Standard as representing pensioners' income needs. 19% of pensioners were in relative poverty (AHC) in 2006/07.
- **Absolute pove**rty – a household is considered to be in absolute poverty if their income falls below 60% of the 1998-99 median income held constant in real terms.[16] This measure is useful for looking at how poverty changes against a fixed real-terms threshold. 10% of pensioners were in absolute poverty (AHC) in 2006/07.

[14] DWP (2008a)
[15] DWP (2008a) p. 18, RPI uprated to 2008
[16] House of Commons Hansard, Written Answers for 02 June 2008,

Chart 1[17]



Pension Credit

In an effort to reduce pensioner poverty, the Government provides a 'guarantee' that pensioners will not have to live on an income below a certain level. By topping up Basic State Pension with Guarantee Credit (the first element of Pension Credit) the Government is attempting to ensure that in 2008, all pensioners will receive at least a minimum income of £124.05[18] per week (£189.35 per week for a couple).[19] People who have saved for their retirement may also receive further income in the form of Savings Credit (the second element of Pension Credit) of up to £19.71 per week (£26.13 per week for a couple).[20]

The income received from BSP and Pension Credit is separate from other benefits which cover housing costs (including council tax)[21] and disability, and pensioners who receive Pension Credit could be eligible for other benefits as well. Pension Credit is a means-tested benefit that is generally taken up by about two thirds of the people who are entitled to it.[22] Non-take-up of Pension Credit can cause pensioner households to fall below the guarantee level.

[17] Data from DWP (2008a) tables: 6.1tr, 6.2tr

[18] In 2009/10 this rate is expected to be £130.00 for a single pensioner, £198.45 for a pensioner couple, subject to any change in the 2009 budget.

[19] Not all pensioners will necessarily receive the minimum amount of £124.05 per week. Some pensioners may not claim Pension Credit even if they are entitled to it and some pensioners may not be eligible for full Pension Credit because of the value of their capital.

[20] PPI (2008b)

[21] But not including water rates

[22] Age Concern (2008) Figure is for overall Pension Credit (PC) take-up, the take-up of the Guarantee Credit element of PC is slightly higher

A Minimum Income Standard[23]

A Minimum Income Standard uses feedback from members of the public as a basis for looking at people's minimum needs in retirement. Participants are asked to determine what they consider to be a minimum acceptable standard of living to form the basis of the minimum income standard. Recent research for the UK suggests that: *'A minimum standard of living in Britain today includes, but is more than just, food, clothes and shelter. It is about having what you need in order to have the opportunities and choices necessary to participate in society.'*[24] The participants agreed that a minimum standard must not provide only the basic requirements of survival but the things necessary to have some choice in purchases and *'the resources required to enable social participation.'*[25]

Table 2:[26] Minimum Income Standard (MIS) for Pensioners in pounds per week for 2008

MIS Category	Single Female Pensioner	Single Male Pensioner	Couple Pensioners
Food	£39.01	£32.94	£53.25
Alcohol	£2.95	£3.06	£7.40
Tobacco	£0.00	£0.00	£0.00
Clothing	£6.13	£3.70	£9.93
Water rates	£4.71	£4.71	£5.56
Council tax	£13.33	£13.33	£17.77
Household insurances	£1.61	£1.61	£1.65
Fuel	£9.63	£9.63	£10.62
Other housing costs	£2.85	£2.85	£3.61
Household goods	£9.65	£9.65	£11.12
Household services	£5.04	£5.04	£9.07
Childcare	£0.00	£0.00	£0.00
Personal goods and services	£11.91	£9.52	£23.65
Motoring	£0.00	£0.00	£0.00
Other travel costs	£4.65	£4.65	£4.65
Social and cultural participation	£25.91	£25.91	£43.21
Rent/mortgage interest	£52.30	£52.30	£64.43
Total needed per week before housing costs	£189.67	£178.90	£265.92
Total needed per week after housing costs[27]	£124.04	£113.27	£183.72

[23] For information on the Minimum Income Standard and the history of Budget Standards see Appendix 1
[24] JRF (2008) p. 14
[25] JRF (2008) p. 15
[26] Source: Minimum Income Standard For Britain, sponsored by The Joseph Rowntree Foundation, www.minimumincomestandard.org
[27] Housing costs are rent/mortgage and council tax

Saving for bequest or future needs
Being able to afford to save in small amounts (£10 per week) is often considered to be an essential part of a minimum budget standard for pensioners, as it allows pensioners to have money for emergencies, funeral costs and celebrations (such as birthdays or Diwali), however there is not much data on the average amount that pensioners tend to save while in retirement.[28]

Pensioners on higher incomes tend to be more likely to save some of their income than those with lower incomes though there is little data on whether the savings are mainly for future expenditure or for bequest.[29] Although the majority of pensioners put their own needs before saving for bequest, people over the age of 80 are more likely to prioritise saving for bequest than people of other ages.[30] People who live in social housing and people with incomes of less than £100[31] per week on the whole do not save and do not expect to ever be able to save up anything to bequest.[32] While some saving for bequest could take place after people have reached State Pension Age, the majority of bequests include savings and assets that have been at least partially accumulated before retirement.[33]

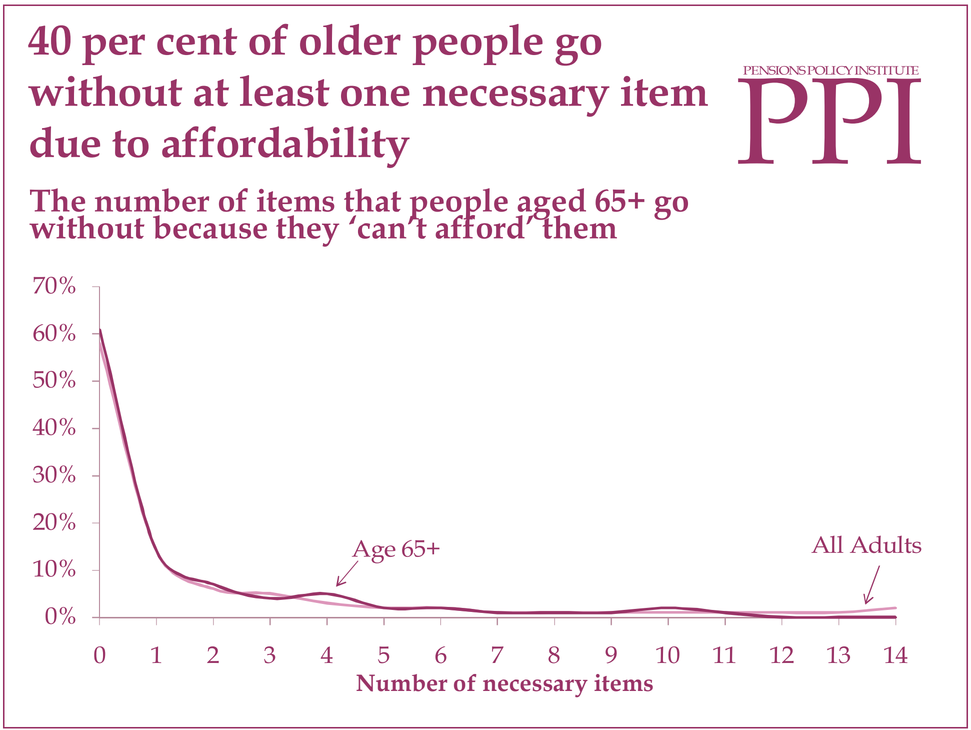
Measures of minimum needs are not always income based
Measures of whether an individual has what they need or are in poverty are not always directly income based, for instance, some studies determine whether a household is in poverty based on whether they can afford a list of essential items.[34] Poverty can also be measured by whether people *feel* poor, perhaps because of great drops in income or because their income may be much lower than the average income in their community.[35]

Needs can be measured by whether pensioners have certain necessary items
The Poverty and Social Exclusion survey (PSE) measures poverty by whether people can afford a list of 35 goods and activities that survey participants believe *'no household or family should be without in Britain'*.[36] Items in the list include: regular savings of £10 per month for rainy days/retirement; friends or family round for a meal; fresh fruit and vegetables daily; and a television.[37] By this measure, people who cannot

[28] Age Concern (2006)
[29] DWP 2006a p. 47
[30] Rowlingson, McKay (2005)
[31] 2005 figure
[32] Rowlingson, McKay (2005)
[33] Rowlingson, McKay (2005)
[34] JRF (2000)
[35] JRF (2007b)
[36] Gordon *et. al*. (2000) p. 40
[37] For a full list see Gordon *et. al*. (2000) p. 43

afford two or more of the necessary items are considered to be in poverty.[38]

Chart 2[39]



Around 40% of pensioners go without at least one of the necessary items because of affordability (Chart 2). 14% report going without one of the necessary items and 7% report going without two. Around one to two percent report going without between five and 11 items.

Retirement needs can be measured relative to working life

Poverty lines and minimum income standards are a useful guide for looking at the minimum level of income people require to provide for their most basic needs. However many people will not feel that they have enough income to meet their needs if they are not able to provide themselves with a similar standard of living in retirement to the one which they were accustomed to in their working life. One way to measure whether people may be experiencing a similar standard of living after SPA is to see how levels of consumption change after people retire.

The majority of people feel that their standard of living in retirement should be similar to the standard they experienced in their working life in order to feel that they are having their needs met, though the levels of

[38] The DWP have commissioned work to draw up a new survey of necessary items that pensioners need, http://www.dwp.gov.uk/mediacentre/pressreleases/2008/oct/stat161008.asp
[39] Data from Kellard *et. al.* (2006) p. 41

income this requires may be far higher than the poverty line or minimum income standard.[40]

For people on median earnings, two thirds of replacement income (after subtracting income tax) in retirement could allow for similar consumption levels to those experienced during working life.[41] The reason that pensioners may not need 100% replacement income in order to maintain similar consumption levels is that for many pensioners, expenses are lower in retirement than they were during working life, partly due to lower taxes and National Insurance.[42] Retired people also tend to save less of their income (in pensions for example), and are less likely to be paying off mortgages, accumulating assets/investments or supporting dependents. Some pensioners also spend less on goods related to employment, like transportation.[43]

The Pensions Commission determined that for people on a low income, a replacement rate of 80% or above may be necessary to provide pensioners with a minimum acceptable level of income. This is because people on a low income may not have put much of their income in working life towards savings and asset accumulation in the same way people on average to high earnings might have done and because an 80% replacement rate of a very low income may come out below the poverty line.[44]

A replacement rate approach indicates a target income level at the point of retirement. However, even if an individual meets their replacement rate target income level at the point that they retire there is no guarantee that their standard of living will be maintained throughout the duration of their retirement. This is because some elements of retirement income do not keep their value in real terms because it is either indexed to prices (which tend to increase more slowly than earnings) or are not indexed at all (e.g. Level annuities.)

Needs can be measured through spending patterns

The amount of income that a household needs could be analysed in terms of the average expenditure of a typical household unit. While the typical expenditure of the average household unit may include some unnecessary spending, it allows for the need people have to make choices in their purchases, in order to feel some degree of autonomy. Discretion regarding spending choices is considered to be an important element of social inclusion.[45] The current average expenditure for a pensioner couple is £337.70[46] per week after housing costs.

[40] Pensions Commission (2004)
[41] Pensions Commission (2004)
[42] Pensions Commission (2004)
[43] Pensions Commission (2004)
[44] Pensions Commission (2004)
[45] JRF (2008)
[46] JRF (2008) data from 2008 Expenditure and Food Survey

Perception is important

Whether a household or individual has an income that meets their needs cannot always be defined by a figure or a percentage. People may feel poor if they are surrounded by households with higher levels of income than their own or if they experience great drops in income, even though these may not take them below a recognised poverty line. People whose income is similar to the levels they experienced in childhood or working life, or of those in their community, generally report satisfaction with their economic resources, even if their income is low enough to be restrictive.[47]

Income needs vary across different types of household units

Different types of households have different income needs. Larger households have higher income needs but need less income per person. Equally, whether a household is located in a rural or an urban setting may affect their need for transport (urban households will generally have more access to public transport) and may impact on the price of goods that they purchase as households in rural areas may have less access to large discount shops than households in more urban areas.

The rest of this chapter will focus on the ways in which income needs for pensioners break down between different types of household units and how the need for social participation affects the need for income in retirement. Chapter 2 will examine the implications of changes in age and health status for pensioners' income needs.

Single pensioners are more likely to be on a low income than pensioners living with other people

Expenditure patterns vary between different types of household units such as lone male and female households or pensioner couple households (Table 3) and these patterns may be somewhat indicative of how needs differ between households. However, it may be dangerous to rely too strongly on expenditure patterns to determine the needs of a particular group. Households may spend in different amounts because they may have different levels of income available to them, for instance, single pensioner households are more likely to be on a low income than pensioner households with two or more members,[48] some expenditure may be unnecessary, and some households may spend some or all of their income without actually meeting all of their needs.

[47] JRF (2007b)
[48] DWP (2008b)

Table 3:[49] Percentage of people over age 65 who live in households that spent something in the following categories in 2001 by household type

Expenditure Category	Lone Males	Lone Females	Couples	Other	Total
Food	100	99	100	100	100
Household services	95	99	100	99	99
Fuel, Power and Lighting	97	96	98	97	97
Household goods	87	91	98	99	95
Leisure services	88	87	96	97	93
Leisure goods	85	88	96	94	93
Personal goods and services	63	80	91	91	85
Motoring expenditure	56	27	84	79	66
Clothing and footwear	27	47	63	68	56
Alcoholic drink	57	32	65	65	56
Fares and other transport costs	26	42	31	54	36
Miscellaneous spending	14	12	17	29	17
Tobacco	22	10	14	33	16
Number of respondents	246	633	1371	321	2571

Expenditure variations across household units indicate that:

- Households with more than one person in them are more likely to spend money on goods associated with leisure activities.
- Single pensioners may have more income needs for care inside or outside the home than pensioner couples.
- Male and female pensioners have different income needs across categories of expenditure including personal goods and services, transport, motoring, clothing and footwear.

Households with more than one person in them may be more likely than households with a single inhabitant to spend money on leisure goods, leisure services, and motoring costs. 'Other' households and single females may be more likely than single males and couples to spend money on fares and other transport costs. These variations could be a result of differential rates of car ownership as well as different levels of access to social networks and activities, though they may also be attributable to age differences between couples and single pensioners.[50] In

[49] Table reproduced from Kellard *et. al.* (2006) p. 23
[50] Kellard *et. al.* (2006)

2005, around 30% of single pensioners had access to a car, whereas 80% of pensioner couples had access to a car.[51]

Single female pensioners tend to spend more than male pensioners on clothing and personal goods, a trend which is also reflected in the Minimum Income Standard (Table 2). This may be partly attributable to female pensioners spending on more varieties of personal goods and because women's clothing and footwear tends to cost more than men's.

Pensioner couples on the whole spend less on care than single pensioners.[52] Pensioner couples tend to be able to remain independent (without needing to move in with other family members or enter residential care) for longer than single pensioners. This may be due to couples providing each other services and support that would otherwise need to be purchased.[53]

Social participation is important for maintaining health and represents an income need

The ability to participate socially is important for mental and physical health,[54] and being unable to participate socially is directly correlated with a low quality of life, which intensifies the longer any period of social detachment continues.[55] There is also some evidence that remaining mentally and physically active in older age is important for maintaining good health and could actually slow down the ageing process and delay or prevent the onset of dementia.[56] Many pensioners may be in danger of becoming socially detached because of barriers to social participation, though these barriers are not always income related.[57] 10% of pensioners report experiencing social detachment at some point over the last six years.[58]

The majority of pensioners cite the inadequacy of local services as their reason for not using them;[59] however affordability may be an issue for some pensioners on low incomes. 2% of pensioners are unable to afford to take part in celebrations on special occasions, to attend weddings or funerals, or to visit friends or family.[60] 4% of pensioners in poor health and 4% of pensioners over the age of 75 cannot afford to visit friends and family.[61]

[51] DfT (2006), data based on Household Reference Persons over the age of 65
[52] Kellard *et. al.* (2006), Zaidi and Burchardt (2005)
[53] Kellard *et. al.* (2006), Zaidi and Burchardt (2005)
[54] JRF (2008)
[55] IFS (2008)
[56] Age Concern (2005), p. 41
[57] Other barriers include: lack of social networks; communication and literacy; neighbourhood or community barriers; as well as cultural barriers, JRF (2007a)
[58] IFS (2008)
[59] JRF (2007a)
[60] Kellard *et. al.* (2006)
[61] Kellard *et. al.* (2006)

Engaging in social participation represents a cost to pensioners, however that cost will differ between individual pensioners depending on their current access to services, their existing social networks, and their health status and age. It would be difficult to identify a single amount of income which could provide all pensioners with the levels of social participation they require to maintain their optimal physical and mental health, however the Minimum Income Standard has provided £25.91 per week (Table 2) for pensioners to use on social participation.

Pensioners who are experiencing social exclusion, poor health or other barriers to social participation could require higher income than the one provided in the Minimum Income Standard in order to enable them to participate socially. While £25.91 may provide low income pensioners with the minimum income necessary to participate socially, pensioners accustomed to a higher income and higher levels of social participation may require higher levels of income to achieve what they would consider to be an adequate level of social participation.[62]

Younger pensioners often have more access to transport than older pensioners

Access to appropriate transport is an important element of being able to participate socially. The cost of transportation is often a barrier to social participation for pensioners[63] and pensioners who have the use of a car or van may be more likely to be engaged in social participation.[64] Younger pensioners are more likely to have access to a car or van than older pensioners. 84% of younger pensioners report having access to a van or car while only 61% of older pensioners report having access.[65]

Pensioners who have limitations on their mobility will often require transport to the homes of family and friends or day centres, and for social activities such as restaurants, theatre, and cinema or museum trips. The costs of transport will differ between individual pensioners and different household units. Pensioners in rural areas may have more need to have their own cars or to take taxis if they wish to access social activities and community resources. Free bus fare for pensioners has dramatically reduced the cost of travel for pensioners who have access to bus services,[66] but some pensioners in poor health or in isolated or rural areas may still be reliant on cars or taxis if they wish to travel.

The Minimum Income Standard provides pensioners with £4.65 per week (£20 per month) for taxi usage and no money for fares as bus service is free for pensioners. This amount assumes that pensioners are generally

[62] Pensions Commission (2004)
[63] Age Concern (2006), many focus group participants reported being unable to afford transport costs which prevented their socialising
[64] DWP (2006a)
[65] DWP (2006a)
[66] JRF (2008), pensioners have free bus fare across the UK from April 2008

able to access their local bus services or to walk to their destination. The costs of transport for pensioners who own cars or vans, some older pensioners with decreased mobility, or pensioners in poor health may be higher than that provided in the Minimum Income Standard.

Conclusion
While many measurements of the income needs of pensioners are focused on the minimum income a pensioner would require in order to meet their basic needs, many people feel that they would like to have a standard of living similar to the one that they experienced in their working life, in order to be satisfied with their income in retirement.

The main calculations of the minimum income required to meet basic needs tend to conclude that a single pensioner needs around £120 per week (After housing costs)[67] in 2008 earning terms, and the calculations of what income a median-earning pensioner would require to achieve an adequate standard of living in retirement (based on expectations) tend to conclude that they would require around £250 per week (Before housing costs)[68] in 2008 earnings terms.

The level of income that a pensioner household unit requires in order to meet their needs or expectations in retirement could vary between different households. The main variations are between single and multi-occupant households and between single male and female pensioner households.

This chapter has highlighted that it is not possible to calculate a single level of income that would be suitable for all pensioners to meet their needs or expectations in retirement, though minimum and desired income measures can provide a useful guide. The level of income required by any pensioner may be dependent on their desired standard of living in retirement, the structure and location of their household and their health needs.

[67] It is useful to look at income after housing costs have been subtracted because it shows more clearly the income that is available for spending
[68] Replacement rate income tends to be calculated in before housing costs terms

Chapter two: How do income needs change after State Pension Age?

Pensioners' needs for income will often change during their retirement. When people reach State Pension Age (SPA), they are generally likely to be healthier and more mobile than they will be during later stages of their life. Changes in health, mobility and the structure of the household could lead to needs changing and affect expenditure in areas such as transport, health, care, and housing related costs (such as fuel and power). This chapter analyses the ways in which income needs could change for people after SPA, focussing especially on the effects of age and health on income needs.

Older pensioners are more likely to have lower incomes and spend less
Overall, pensioners tend to spend less as they age,[69] however reductions in spending could be a result of a fall in income as well as being due to changes in income needs as pensioners age. People over age 75 are more likely to be on a low income than pensioners overall, 25% of pensioners in households where the head is age 75 or over are in the bottom fifth quintile of the income distribution versus 16% of pensioners living in households where the head is under age 75.[70] However, the reduction in mobility caused by age and disability could also present people with fewer opportunities to spend income, and there are correlations between reduced spending and receipt of disability benefits.[71] Spending as a proportion of income is lower for pensioners over 80 than it is for pensioners overall (Table 4).[72]

[69] DWP (2006a)
[70] DWP (2008b) (AHC 2006/07 figures)
[71] DWP (2006a)
[72] DWP (2006a)

Table 4:[73] Percentage of people who live in households that spent something in the following categories in 2001 by Age

Expenditure Category	65 to 69 years old	70 to 74 years old	75 to 79 years old	80 years old and over	Total
Food	100	100	100	100	100
Household services	99	99	99	99	99
Fuel, Power and Lighting	97	97	97	98	97
Household goods	97	96	95	91	95
Leisure services	99	99	88	80	93
Leisure goods	95	94	93	87	93
Personal goods and services	90	86	83	80	85
Motoring expenditure	80	70	58	50	66
Clothing and footwear	66	61	53	39	56
Alcoholic drink	65	59	53	42	56
Fares and other transport costs	37	36	36	35	36
Miscellaneous spending	23	19	12	11	17
Tobacco	19	21	13	10	16
Number of respondents	788	688	565	530	2571

Spending on goods and services associated with social and leisure activities decreases with age. But spending on fuel, power and lighting increases with age. Both of these changes in spending patterns could be related to the trend for mobility to decrease as people age, which leads to people spending more time in their homes.[74] The decrease in mobility that people experience as they age may not necessarily always be a result of health deterioration, as some of it could be attributable to the natural increase in frailty that accompanies ageing, however health changes are a significant element of why people's income needs change as they age.

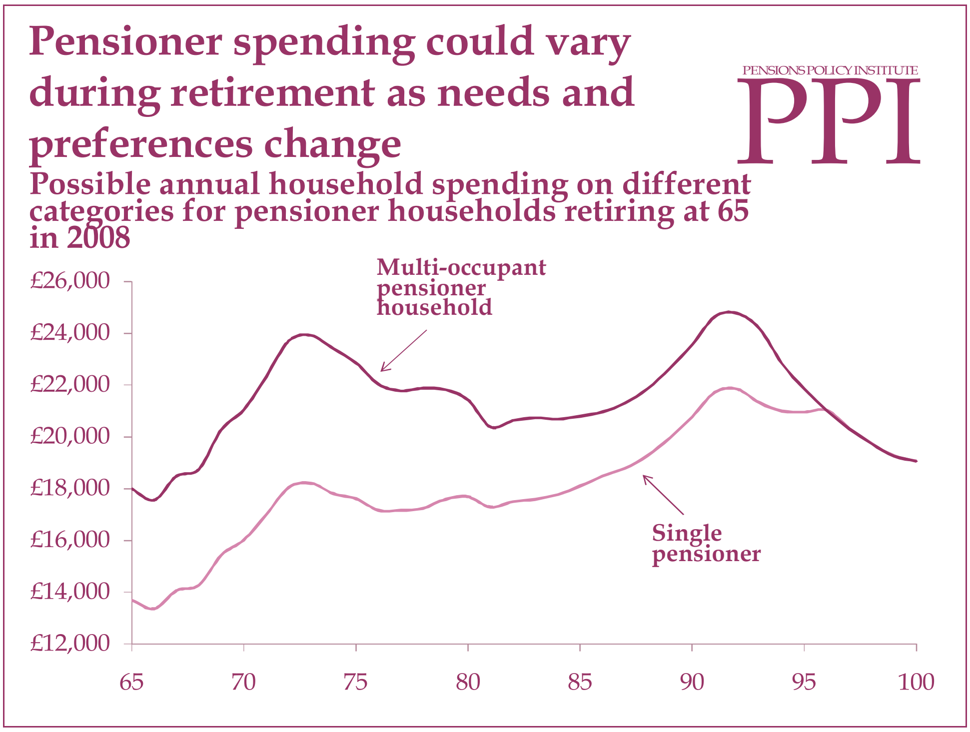
Despite increases in spending on fuel, people tend to spend a smaller proportion of their overall income as they age. This may be a result of decreases in mobility and opportunities to spend though it could also in some part be attributable to pensioners saving more as health needs become more pressing in order to fund future health related costs, funeral costs, or to give as bequest.

[73] Table reproduced from Kellard *et. al.* (2006) p. 21
[74] Age Concern (2006)

Pensioner spending can vary during retirement as needs change
Needs for income to fund health care costs and costs associated with ageing generally increase during the later years of retirement, however for some pensioners spending could increase and decrease at several points during retirement as a reaction to both income needs and people's expectations for their retirement. For some pensioners spending can be highest both in the early and late stages of retirement, with a dip between the ages of 75 and 95. Chart 3 shows what a spending cycle could look like for a pensioner retiring at 65, based on spending preferences and needs as they change during retirement.

Chart 3 shows annual spend in cash terms, allowing prices to increase each year with inflation, for a 65 year old retiring in 2008. It is shown in cash terms in order to represent how the peaks and troughs may appear to an individual during retirement.

Chart 3[75]



When people first retire they are likely to be more healthy and mobile than at later stages of retirement, and many pensioners wish to spend their first years of retirement enjoying their leisure time by eating at restaurants, attending the theatre and going on holidays.[76] On average, 40% of total spending by people aged between 65 and 75 is on goods associated with recreation and culture, such as hotels, transport and restaurants.[77]

[75] Life Trust, cebr (2008), data assumes 2.5% inflation (altered from original data which assumes 2.3%)
[76] Life Trust, cebr (2008)
[77] Life Trust, cebr (2008)

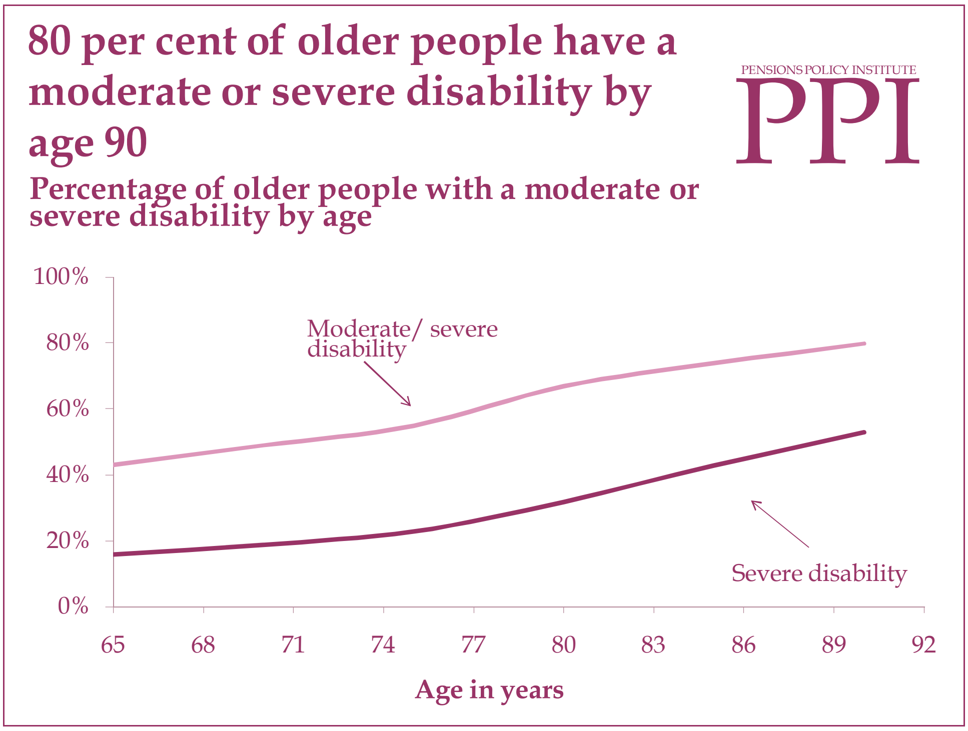
Pensioner spending can drop off as people become older and less mobile, after the age of 75, and then increase again in older age as people acquire health problems and need to spend more on housing, fuel, power and food. However as people reach age 95 and beyond, total spend tends to decrease as spending on items such as clothing, leisure and transport tends to drop off dramatically.

These trends are likely to change over time as healthy life expectancy increases for pensioners.[78] If older people are spending more time in good health, and subsequently acquiring illnesses and losing mobility at a later age, the periods of increase in spending may move upwards along the age range. Higher spending on leisure during the first years of retirement may also increase as a result of increased expectations from the next generation of pensioners (currently 46 – 65 year olds) who may intend to engage in more travel and leisure activities than their parent's generation.[79]

Changes in health can cause pensioners to need more income
As people age they are more likely to acquire a low, moderate or severe disability (Chart 4). The onset of disability may often be associated with an increase in costs, though acquiring a disability may also reduce costs in areas such as leisure activities and motoring expenditure. The specific level of increase in income needs that is associated with disability could vary depending on the type of disability that an individual acquires. The costs associated with the onset of disability generally increase as the severity level of the disability increases.

[78] IFS (2008)
[79] Standard Life (2009)

Chart 4[80]



There are different approaches to measuring the cost of disability to individuals and household units although there are limitations to how accurate any measure can be. Many existing measures use data on the expenditure of people with disabilities to determine the extra costs of disability, however these measures are not generally able to determine what people would spend if they had adequate resources or different budgetary preferences.[81]

Though some studies do attempt to measure what people would spend if they had adequate resources, it may be difficult to translate these results into conclusive data regarding the cost of disability, as study participants may have different interpretations of the difference between needs and wants.[82] Studies which look at the expenditure patterns of people with disabilities as a basis for determining the cost of disability may not be capable of accounting for the reductions in non-disability related expenditure which some people on low incomes may make in order to finance the added costs of disability.[83]

There is no consensus on how to measure the size of the extra costs of disability, though there is a consensus that disability does incur some

[80] Data from Kellard *et. al.* (2006) p. 63-64
[81] DWP (2005)
[82] DWP (2005)
[83] For a full discussion on the potential problems with calculations of the cost of disability see DWP (2005) p. 27-31

extra costs which may not be fully covered by state benefits.[84] This report uses an expenditure based approach to measuring costs in order to illustrate how incurring extra costs as a result of disability may affect income and needs in retirement.

The additional costs associated with disability depend on the type and level of severity

Using data on expenditure, it is possible to estimate what the extra costs of disability may be as a percentage of average income.[85] This paper applies these percentages to 2008 income levels in order to estimate the extra costs incurred by different levels of disability (Table 5). The actual costs of disability will vary between pensioner households and will depend on their level and type of disability.

Table 5:[86] Possible extra weekly costs per household unit of low, medium and high severity disability[87]

	Individual pensioner	**Pensioner Couple with one or both disabled**
Average Weekly Income 2008/09	£199.13	£419.8
Low severity disability	£46.57	£25.19 - £28.39
Medium severity disability	£137.40	£83.96
High severity disability	£260.86	£155.33

Disability could require expenditure on care and personal goods and could increase living costs

Acquiring a disability could incur costs in several different areas of expenditure, depending on the type and the severity level of the disability. Disabilities which are associated with the greatest increase in costs are those associated with transport and personal care, including the cost of food preparation and help with eating.[88] As well as costs for care, disability could incur expenditure on personal goods such as incontinence pads and information in Braille[89] and goods and services such as extra or special clothing/shoes, special foods, domestic help/gardening and increased livings costs because of the need for: aids and adaptations to the home; mobility aids; altered transportation requirements; additional personal and health care needs.[90] The onset of health problems may also

[84] DWP (2005)
[85] Zaidi and Burchardt (2005)
[86] Costs of disability calculated using percentages of mean income as cost of disability, Zaidi and Burchardt (2005) p. 103 uprated by 2008/09 RPI and using 2006/07 mean income, (see DWP (2008b) table 2.1 for average income 06/07). For full calculations see Appendix 2.
[87] Table 5 represents a range of different levels of disability, but costs for any particular pensioner or pensioner couple may be higher or lower depending on the severity level of their disabilities.
[88] DWP (2005) p. 21
[89] Zaidi and Burchardt (2005)
[90] Age Concern 2005, p. 10

increase costs in areas which are not directly related to health or disability, such as laundry and heating.[91]

Some of the increased costs can be met by benefits, the most common being Disability Living Allowance (DLA) and Attendance Allowance (AA). DLA care component and AA will pay people with disabilities up to £67.00 per week, depending on the level of severity of their disability.[92] These benefits are not means tested which means that they are available to anyone with a qualifying disablement regardless of their current income. Pensioner couples may also qualify to receive Carers Allowance, if one partner provides care to the other, of up to £50.55 per week (in 2008) which can further mitigate the costs of disability that couples face.

Local Authorities can provide services such as home help and day care or can support the funding of residential care, however this care is usually means tested so people above a certain income or asset level may be required to pay for all or part of the care which the State provides. People may also receive extra help from family, friends and community groups once they are disabled. As help comes from many different sources it can be difficult to conclusively determine the extra cost of a disability to an individual or to the state.

Individual pensioners tend to face higher costs when disabled than pensioners in couples. Couples may face lower costs when disabled as a result of unpaid care being provided by their partner and because pensioner couples may be able to share equipment and disability related-resources when both members have a disability.

If people need to move into a care home because of their disability, then they can incur very different levels of costs. Care homes can cost between around £400 and £900 per week (2007 figures) depending on where the home is and on the level of care needed by the resident.[93] The amount that people have to pay towards their own care is dependent on their level of income and/or capital, the type of care they need and whether or not they are considered to be the responsibility of the NHS (in which case the whole of the care is free).[94]

[91] Zaidi and Burchardt (2005)
[92] People may also be eligible for the DLA mobility component of up to £46.75 per week, (if they were already claiming before the age of 65) depending on their disability
[93] PSSRU (2008)
[94] For more information on care charging see: www.ageconcern.org.uk/AgeConcern/fs20.asp and www.ageconcern.org.uk/AgeConcern/fs10.asp

The gender and household structure of pensioners can affect levels of expenditure on health

As well as age, the likelihood of reporting a disability and incurring disability related costs is also correlated with household structure and gender. Older women who live alone are more likely than any other household unit to report health problems.

- After the age of 75, almost 50% of older women living alone report health problems that limit their daily activities, whereas around 35% of women living with one or more other people report health problems.[95]
- Only around 30% of lone men over the age of 75 report health problems.
- Within couples over the age of 75, around 45% of women and around 30% of men report a health problem.
- Men living alone are only around 5% more likely than men in couples to report health problems, even after the age of 75.[96]

Maintaining health and preventing disability has associated costs

Pensioners could prevent or postpone disability and increase longevity by living a healthy lifestyle which includes a nutritious diet and regular exercise and by engaging in social participation.[97] Nutrition may be especially important as pensioners whose diets do not contain enough micronutrients are more likely to experience health problems.[98]

The cost of a nutritious diet and social participation are included in the Minimum Income Standard[99] discussed in chapter 1 and are calculated as being around £30 to £40 per week for a single pensioner to maintain a nutritious diet and around £25 per week for a single pensioner to engage in social and cultural participation and, though the costs for medium and high income pensioners to engage socially and culturally may be much higher.

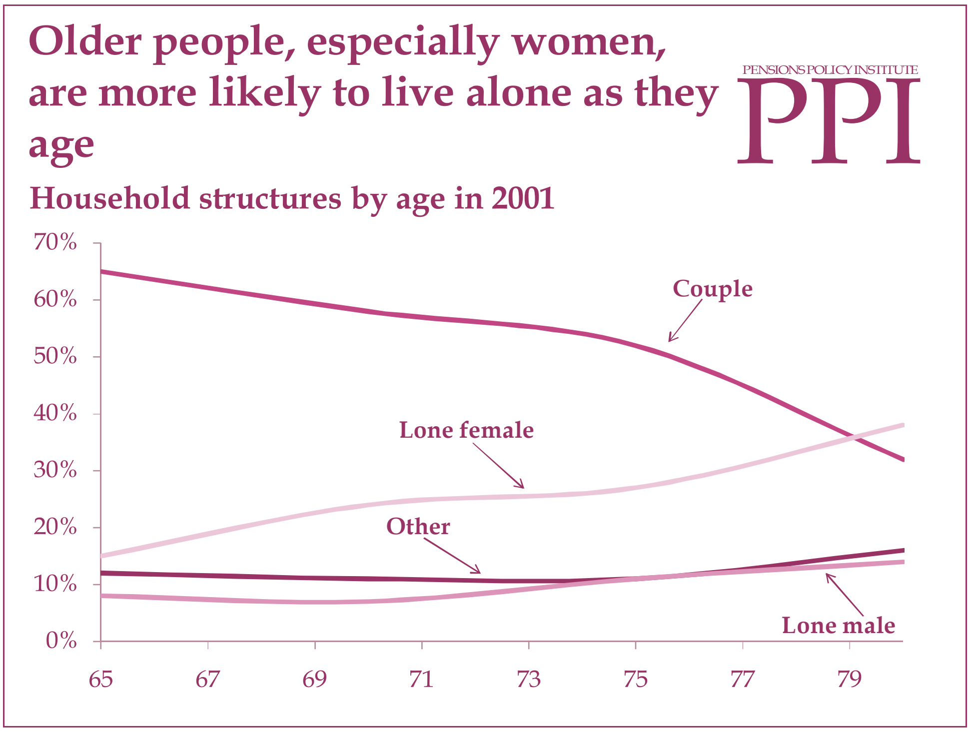
Single occupancy households and women tend to engage in more health related expenditure than other households

The structure of household units can change during retirement as partners die, new partnerships are formed and people move in with and away from family members (Chart 5). The changes which have the greatest correlation with need are those which cause a household unit to change from multiple to single occupancy, especially for women. Households containing a single older woman over the age of 75 are 15 to 20% more likely to report a health problem than single older male households and pensioner couple households.

[95] Kellard *et. al.* (2006)
[96] Kellard *et. al.* (2006)
[97] Age Concern (2005) p. 14
[98] Age Concern (2005)
[99] JRF (2008)

The higher reporting of disability by single women could be partly due to the fact that women in general are more likely to acquire a health related problem at any time,[100] but may also be due to single pensioners requiring more outside assistance with health related needs,[101] and therefore being more likely to report a health related problem in order to obtain assistance from the State.

Chart 5[102]



As people age the likelihood that they will live alone increases, especially for women, and this trend has become more prevalent over time. It is possible that pensioners may continue to be more likely to live alone in the future. Pensioners who live alone are more likely to have a low income than pensioners that live in couples or with other people. Around 65% of pensioners who live alone are in the bottom two quintiles of income and only 5% of pensioners living alone are in the top quintile. For all other household groups the distribution across income quintiles is more even.[103]

[100] Kellard *et. al*. (2006)
[101] Kellard et. al. (2006)
[102] Data from Kellard *et. al* (2006) p. iii
[103] DWP (2008a) figures are before housing costs

Conclusion

Single pensioners living alone, especially women, are more likely to be on a low income and are also more likely to report health problems than pensioners living with other people. Individual pensioners with disabilities could face an increase in income need of around £45 - £260 per week, and pensioner couples with disabilities could face an increase in need of around £30 – £150 per week, yet pensioners with health problems are more likely to be in a low income group than pensioners without health problems.[104] As pensioners age and develop health problems they could require a minimum income level of around £30 - £260 above the poverty line or minimum income measure in order to fund the extra costs associated with disability entirely from their own financial resources.

People tend to spend a smaller proportion of their income as they age because they are less likely to spend on goods and services related to social participation such as leisure goods and services, motoring, tobacco and alcoholic drink. It might be the case that some of the income need generated by the onset of disability can be met by the extra funds generated by the decreases in spending on social participation. However, it is unclear whether pensioners are using the extra funds to save for future health related costs or bequest, in which case they may not necessarily be considered available funds for assisting with current health related costs. It is also possible that pensioners with health problems may require more income in order to remain socially included and that the decrease in spending represents a re-prioritisation of funds and not a genuine desire to decrease social participation.

[104] JRF (2006)

Chapter three: What sources of income are available to people after State Pension Age?

After State Pension Age (SPA), people are likely to receive their income from a variety of sources. Sources of income in older age can vary greatly between individuals and household units. This chapter investigates the main sources of income that pensioners receive and analyses the implications that different types of income sources have for the level of income pensioners receive. It examines how income sources change as people age and how sources vary across different household units.

The main sources (Table 6) that people currently receive income from after SPA are:
- State pension
- Means-tested benefits
- Disability and mobility related benefits
- Financial assets such as savings and investments
- Occupational pensions
- Personal pensions
- Earnings

This chapter describes each source in turn and then goes on to look at other sources of capital or income people use in retirement.

Table 6:[105] Pensioners income sources and percentage of pensioners in receipt of income from each source

Income source	Percentages of pensioners in receipt of income from this source	Average (mean) amount for pensioner in receipt, per week		Median amount for pensioner in receipt, per week	
		Single	Couple	Single	Couple
State pension	95%	£104	£149	£99	£154
Means-tested benefits	32%	£64	£62	£59	£47
Disability and mobility related benefits	23%	£52	£65	£43	£61
Investments	72%	£33	£70	£4	£11
Occupational pension	59%	£104	£206	£67	£144
Personal pension	13%	£82	£103	£32	£42
Private pension	66%	£106	£205	£67	£139
Earnings	16%	£257	£432	£198	£309

[105] DWP (2008b) figures from 2006/07

State pension

The Basic State Pension is the first tier of state pension provision in the UK. It operates on the contributory principle so that an individual's final pension entitlement depends on the number of years in which they made, or were credited as making, National Insurance contributions during their working life. Individuals can qualify for up to £90.70 a week from the Basic State Pension (in 2008/09), but can receive more if they defer taking their pension till after State Pension Age (SPA), or less if they have not paid or been credited with paying sufficient National Insurance Contributions (NICs).

The Second State Pension (S2P) is the second tier of the state pension provision in the UK. It was introduced in 2002 as a replacement for the previous scheme, SERPS. With S2P, an individual's final pension entitlement is more closely related to their level of earnings during their working life than under the Basic State Pension. In total, around 95% of pensioners are in receipt of income from the state pension (including S2P).[106] The average amount of income received from the state pension in 2006/07 was around £100 for single pensioners and around £150 for pensioner couples.[107]

Pension Credit and other means-tested benefits

Pension Credit is a means tested benefit that some people over the age of 60 on low incomes qualify for. The Pension Credit is designed to ensure that people aged 60 and over have a minimum guaranteed income of £124.05 a week for a single person and £189.35 a week for a couple (in 2008).[108] People on pension credit may also be eligible for Savings Credit of up to £19.71 per week (£26.13 per week for a couple).[109] As well as Pension Credit, pensioners on low incomes are also eligible for other means tested benefits including Housing Benefit, Council Tax Benefit and Social Fund Grants. Around 30% of pensioners are in receipt of income from a means-tested benefit including Pension Credit.[110] The average amount of means-tested benefit income received by pensioner couples and individuals is around £60.[111]

Disability and mobility related benefits

Pensioners with disabilities or limits to their mobility may be eligible for Attendance Allowance or, for those disabled and claiming before the age of 65, Disability Living Allowance. These benefits are not means tested and can pay up to £67 per week (in 2008/09). Pensioners with disabilities may also be eligible for other non means-tested disability benefits including Industrial Injuries Disablement Benefit, Constant Attendance

[106] DWP (2008b)
[107] DWP (2008b)
[108] These amounts can be higher for some carers, severely disabled people, and homeowners with certain housing costs.
[109] PPI (2008b)
[110] DWP (2008b)
[111] DWP (2008b) figures from 2006/07

Allowance and other direct payments, grants or pensions for pensioners with disabilities including disablement pensions for veterans.[112] Around 20% of pensioners are in receipt of income from a disability benefit and the average amount received is around £50.[113]

Savings and Investments

Income from savings or investments is the second most common source of income for people after SPA, with around 70% of pensioners receiving income from savings or investments.[114] The average amount received from investment income by pensioners is around £30 per week, though the most commonly received amounts are much lower at around £10 per week.[115] Table 7 shows the proportions of pensioners who receive income from different savings and investment sources.

Table 7:[116] Proportion of pensioners in receipt of income from investment or saving sources

Type of saving or investment	Pensioner couple	Single male pensioner	Single female pensioner
Bank/Building Society account	55%	41%	40%
ISA	48%	29%	29%
Premium Bonds	36%	22%	21%
Stocks & Shares	27%	16%	15%
Post Office Card Account	10%	12%	14%
Personal Equity Plans[117]	11%	7%	6%

Occupational pensions

An occupational pension is a type of pension scheme which has been organised by an individual's employer. The employer usually contributes to these schemes, and more often than not an employee contribution is required. Most schemes are arranged through a single employer, although there are a few industry-wide arrangements. Such schemes can be Defined Benefit (DB), where the final pension is based on earnings and length of service; Defined Contribution (DC) – where the employer contributes a specified amount, usually expressed as a percentage of salary, or; a Hybrid pension scheme, which combines DC and DB features within the same pension. Around 60% of pensioners receive some income

112 For a full list see: www.direct.gov.uk/en/MoneyTaxAndBenefits/BenefitsTaxCreditsAndOtherSupport/Disabledpeople/index.htm
113 DWP (2008b)
114 DWP (2008b)
115 DWP (2008b)
116 Data from DWP (2008c)
117 PEPs were abolished in 1999 and replaced by ISAs, in 2008 all PEPs were converted into stock and share ISAs see: www.hmrc.gov.uk/isa/rule-change-april08.htm

from an occupational pension and the average amount that they receive is around £100 per week.[118]

Personal pensions

People can take out a DC pension without going through their employer, these pensions are called personal pensions. Personal pensions can also be taken out through an employer known as a Group Personal Pension. People sometimes have personal pensions alongside one or more occupational pensions. Around 13% of pensioners receive some income from an annuity bought with a personal pension and the average amount they receive is around £80 per week.[119] A stakeholder pension is a type of personal pension.

Annuities

DC Pension Schemes do not pay out income in retirement in the same way that DB pension schemes do. When people with a DC pension retire, they are generally required to purchase an annuity. An annuity is an insurance product that pays an income from the date of purchase until the date of death. An annuity insures an individual against the financial risk that he or she lives longer than expected so requires an income for longer than expected. The actual level of pension that an individual will receive from an annuity depends on the accumulated fund and the annuity rates applicable at retirement. The pension level that an individual will receive from an annuity also depends on their risk profile; if they are in poor health, obese, or a smoker they may receive a higher rate from an annuity as they will be expected to have a shorter life expectancy than a healthy pensioner.

There are a large range of annuity types that people can buy. The most commonly selected are level annuities, which pay the same amount every month for the life of the annuitant. People can also purchase index linked annuities, most of which escalate in line with the Retail Price Index. These annuities pay less in the beginning than level annuities, but protect pensioners against future increases in prices. People can also purchase joint life annuities where a certain proportion of the annuity (for instance, 50%) continues to pay out to the surviving spouse of the annuitant after their death.

People are not required to purchase their annuity from the pension provider that holds their fund, and can search for the provider who offers the best rates for an individual's particular needs.[120] This is called the Open Market Option. The type of annuity that an individual purchases

[118] DWP (2008b)
[119] DWP (2008b)
[120] The FSA provides an annuity rate comparison tool www.moneymadeclear.fsa.gov.uk/tools/compare_products.html

will have implications for how their income will change throughout retirement.[121]

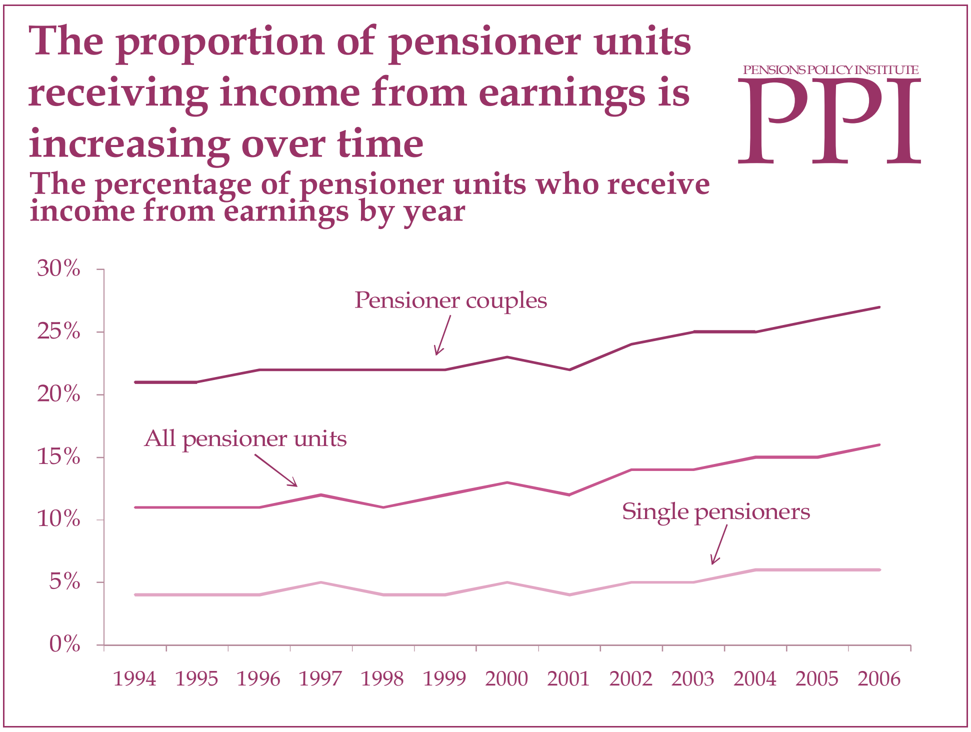
Income Drawdown
Income withdrawal or 'drawdown' allows an individual to draw an income from their pension fund whilst leaving the remaining fund invested. The minimum and maximum amounts available for withdrawal are set by Government. People are allowed to drawdown income from their pension fund until the age of 75, when they are required to secure their pension, usually by buying an annuity.[122]

Earnings
It has become more common over the last decade for people to work after SPA. In 1994-95, 11% of pensioners received some income from earnings and in 2006-07, 16% of pensioners received some income from earnings (Chart 6) (though some of these people will have received income from the earnings of a partner whose age was below SPA).[123] The increasing trend for people to work after SPA may continue as longevity and health outcomes increase, however working after SPA is also associated with paying off outstanding mortgages and debts, a desire to maintain or improve living standards, and low incidence of receiving income from occupational pensions.[124]

The length of time spent working after the ages of 60 (Women) and 65 (Men) may also be affected by the planned rises in SPA included in the Pensions Act 2007. After 2010 the SPA will start to rise for women so that in 2020 women and men will both have an SPA of 65. Post 2020 the SPA will continue to rise incrementally for both men and women until 2046 when it will be 68 for both men and women.

[121] There are many different other types of annuities available to people. For further information, see www.moneymadeclear.fsa.gov.uk/products/retirement/types/lifetime_annuities.html
[122] People with religious objections to purchasing annuity products may be able to continue using drawdown after the age of 75 in an Alternatively Secured Pension (ASP). For more information on ASPs see Financial Services Authority or HMRC websites
[123] DWP (2008b)
[124] DWP (2003)

Chart 6[125]



Pensioners often have capital and assets which can be used as sources of income or support

The majority of the above income sources (Table 6) are traditionally designed to provide income in retirement or support for people who have a low income or disabilities. The next section of this chapter discusses some of the other sources of capital, income and support which pensioners use, specifically:

- Housing,
- Assets,
- Inheritance, and
- Support/income from friends and family.

Housing

Property can help to fund retirement in three ways:[126]

- Owning your own home could reduce day-to-day living costs in retirement.
- Equity released by homeowners could be used to provide extra income.
- Property could be used as part of an investment portfolio generating income in retirement.

In 2007, around 73% of the 6 million pensioners in the UK were owner-occupiers.[127] However not all pensioners who own their homes have paid

[125] DWP (2007), DWP (2008b) Table 3.10
[126] PPI (2004)

off their mortgage (around 10% of owner-occupiers)[128] and some pensioners may not be able to release a sufficient amount of equity from their home to make a significant contribution to their income in retirement.[129] This has become especially true in 2008/09 as house prices have started to fall.[130] In 2008, 33% of working-age people expected their property to be one of the main contributors to their income in retirement,[131] however, it is likely that because of the complications involved in equity release and a possible continued fall in house prices that people may not receive the level of income from their property in retirement that they anticipated in their working life.[132]

Tax-free lump sums

People with private and occupational pensions are currently allowed to take a quarter of their fund, tax-free, as a lump sum after the age of 50, though this age will rise to 55 after 2010. About a quarter of people elect not to take their lump sum, with three quarters of people taking some or all of their lump sum at the point of retirement.[133] Around half of people who take a lump sum put it into savings for the future, and around 20% invest it.[134] Around a third of people use their lump sum for home improvements and many use it to pay off their mortgage (around 20%), pay off loans and credit card debt (around 20%) or go on holiday (around 20%).[135] Lump sums, therefore, are a potential source of flexible income in retirement as they can be used on large purchases, to pay off debts, or be re-invested as a way of providing a future source of income in later retirement.

Inheritance

As people age they are more likely to receive an inheritance of some form and currently the majority of inheritances are received between the ages of 30 and 69.[136] However the trend over time has been for more people to receive inheritances overall, so each age group is more likely to receive an inheritance than any older age group. In 2004, 53% of people over 60 had received an inheritance of some kind and 22% of people over 60 had received an inheritance worth at least £10,000 (in 2004 prices).[137] 11% of inheritances are in the form of property.[138] This means that some pensioners may be able to use income or assets from inheritance to help fund their retirement.

---

[127] House of Commons, 20 January 2009, Hansard, Column 1406W
[128] DWP (2008a)table 6.5
[129] PPI (2004)
[130] Nationwide house price index January (2009)
[131] Alliance Trust (2008) www.alliancetrust.co.uk/press_releases/0083.htm
[132] For a further discussion of how property is used in retirement see: PPI (2004) *Property or Pensions?*
[133] Prudential. YouGov. (2008)
[134] Prudential. YouGov. (2008)
[135] Prudential. YouGov. (2008)
[136] Rowlingson, McKay (2005)
[137] Rowlingson, McKay (2005)
[138] Rowlingson, McKay (2005)

The chances of inheriting are higher for people in traditionally higher income groups. Senior professionals are 70% likely to receive some inheritance during their lifetime, whereas clerical workers are 57% likely and casual workers/unemployed people are around 30% likely.[139]

Family and community support

It is difficult to calculate the monetary value of the support which pensioners receive from their families, though most pensioners who receive support from their families find it easier to meet their practical needs in retirement than pensioners without family support.[140] The support that pensioners receive from family tends to be provided in the form of services such as home repairs, shopping and transport.[141] Each of these services could require expenditure by pensioners to meet the need on their own without family help.

Pensioners reported that the above types of support tended only to be provided by family and not friends or community, though friends and community often provide support in other ways.[142] This has implications for the income and expenditure needs of pensioners who do not have family available or willing to provide them support.

Support provided to pensioners by their communities tends to take different forms than that which is provided by families. The community resources which pensioners find the most valuable are: accessible shops, health services, public transport, social activities, volunteering opportunities, advice services and libraries.[143] Pensioners who live in rural areas are the ones who are least likely to find some or all of these resources in their community and may have to pay (or pay more) to access services than pensioners living in more urban areas.

Pensioners with savings and assets could use these to help fund retirement

Around 70% of pensioners own their own homes[144] and around 70% also have some income from savings or investments[145] (average receipt from investments is £51 per week for all pensioner households).[146] This means that a significant proportion of pensioners have access to some income from housing, savings or investments. The ability that assets and savings/investment income have to help pensioners in retirement may be dependent on the worth of the assets and how they are used in retirement.

139 Rowlingson, McKay (2005)
140 JRF (2007b)
141 JRF (2007b)
142 JRF (2007b)
143 JRF (2007a)
144 House of Commons, 20 January 2009, Hansard, Column 1406W
145 DWP (2008b)
146 DWP (2008b), half of all pensioners receive £7 or less per week from investment income.

Many people intend to rely on their property to provide them with income in retirement;[147] however owning property does not necessarily insure pensioners against having a low income in retirement.

- 16% of pensioners who own their own home (including those with outstanding mortgages) fall into a low income group.[148]
- 28% of pensioners who rent social housing fall into a low income group.[149]
- 38% of pensioners who rent privately fall into a low income group.[150]

20% of pensioners with no savings at all are in a low income group.[151] Whereas, 15% of pensioners with a small amount of savings/assets (less than £1,500), around 10% of pensioners with savings over £1,500 and around 5% of pensioners with savings and assets of over £20,000[152] are in a low income group. This breakdown implies that having even a small amount of savings is associated with a much lower risk of being in a low income group in retirement. This association may be as a result of savers and non-savers having different financial histories and patterns of behaviour.

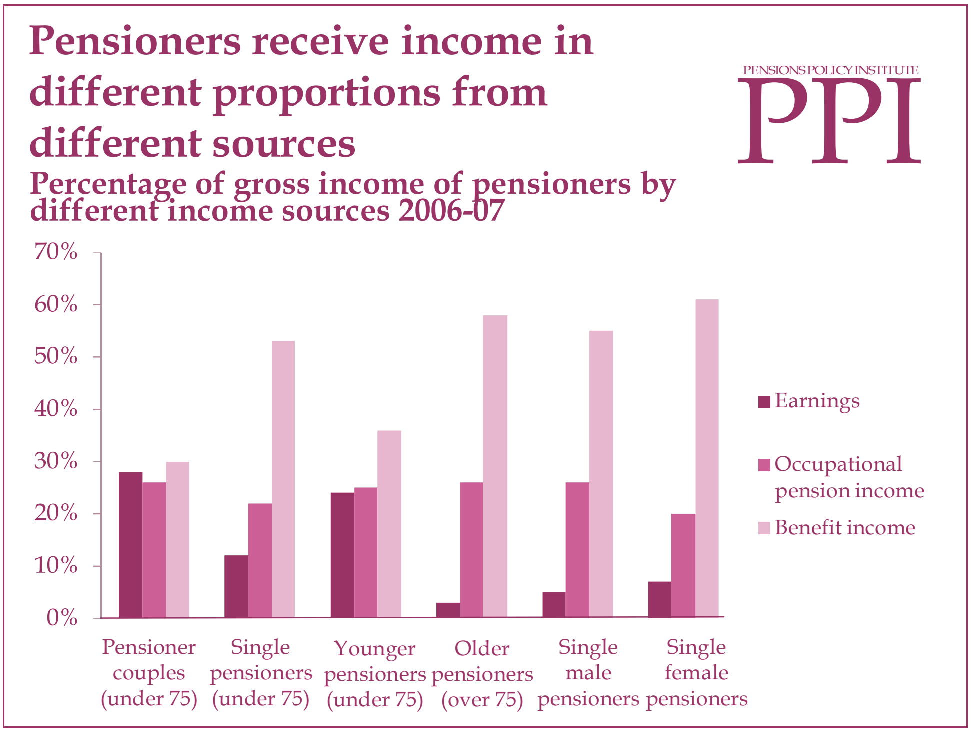
It is likely that having savings and assets in retirement, in addition to income, will make meeting needs and expectations easier, however it is not clear whether it is the income from the assets and savings itself which prevents people from falling into a low income group, or whether those with an adequate income are simply more likely to have assets and savings.

Income sources differ between pensioners of different ethnicities, genders and household types

Most pensioners receive some income from most of the sources listed above, however pensioners living in different household groups, and of different genders, ethnicities and ages tend to receive income in slightly varying proportions from particular sources (Chart 7). This has implications for the level of income that pensioners receive in retirement as different income sources will have various levels of income associated with them. For example, pensioners who receive the majority of their income from earnings or occupational pensions are likely to be receiving a higher overall level of income than pensioners whose main source of income is state benefits or state pension. The next section of this chapter examines the ways that income sources differ between different household units, age groups, genders and ethnicities.

[147] Alliance Trust (2008) www.alliancetrust.co.uk/press_releases/0083.htm
[148] DWP (2008a) Low income group defined here as below 60% median income for the UK, Before Housing Costs
[149] DWP (2008a)
[150] DWP (2008a)
[151] Alliance Trust (2008)
[152] Alliance Trust (2008)

Chart 7[153]



Pensioner couples receive more income from earnings and occupational pensions than single pensioners

Pensioner couples[154] receive a larger proportion of their income from earnings (28%) and occupational pensions (26%) than single pensioners (12%, 22%).[155] However, single pensioners receive state benefits (53%) in a larger proportion than pensioner couples (30%).[156] This breakdown is not surprising, as single pensioners are more likely to be on a low income than pensioner couples.[157] In respect of other main income sources, pensioner couples and single pensioners receive income in similar proportions.

Older pensioners receive less income from earnings and more income from state benefits

Older pensioners receive a much smaller proportion of their income from earnings than younger pensioners. Pensioner households where the head is over 75 receive just 3% of their income from earnings, whereas pensioner households where the head is under 75 receive 24% of their income from earnings.[158] This difference in proportions of income received from earnings could be attributed mostly to the fact that older pensioners are far less likely to be in work than younger pensioners. 13%

[153] DWP (2008b)
[154] Pensioner couples where the head of the household is under 75 in 2006/2007, DWP (2008b)
[155] DWP (2008b)
[156] DWP (2008b)
[157] DWP (2008b)
[158] DWP (2008b)

of men and 25% of women continue to work some time during the first five years after retirement age.[159] By age 70, only 8% of men and 3% of women are still working.[160]

Older pensioners receive slightly more of their income from occupational pensions (26%) than younger pensioners (25% for pensioners under 75 and 24% for pensioners within 5 years of SPA).[161] Conversely, younger pensioners receive slightly more of their income from personal pensions (4%) than older pensioners do (3%).[162]

The third way in which income sources differ between pensioners of different ages is in state benefit receipt. Older pensioners are far more likely to receive income from state benefits. Pensioner households where the head is over the age of 75 receive 58% of their income from state benefits, whereas pensioner households with the head under age 75 receive 36% of their income from state benefits.[163]

Female pensioners receive more income from state benefits and less income from occupational pensions than male pensioners

- Single female pensioners receive slightly more of their income from earnings (7%) than single male pensioners (5%), however single male pensioners have higher incomes overall than single female pensioners. The percentage difference between men and women receiving earnings after SPA may change once SPA becomes equalised between men and women (around 2020).
- Male pensioners receive more of their income from occupational pensions than female pensioners (26% (M), 20% (F)) and receiving income from occupational pensions is often associated with higher income than receiving income from some other sources such as state benefits.
- Single female pensioners receive more of their income from state benefits (61%) than single male pensioners (55%).[164]

White pensioners receive more income from occupational pensions than pensioners from ethnic minority groups

Income sources differ quite widely across pensioner groups of different ethnicities (Table 8). The greatest variation is in occupational pensions, where 60% of White pensioners, 43% of Chinese/Other, 38% of Black/Black British pensioners and 30% of Asian/Asian British pensioners receive some income from occupational pensions.[165] Members of ethnic minority groups are less likely to have saved in an occupational

[159] However women currently reach retirement age five years earlier than men, which may go some way to explaining why they are more likely to work after SPA
[160] DWP (2003)
[161] DWP (2008b)
[162] DWP (2008b)
[163] DWP (2008b)
[164] DWP (2008b)
[165] DWP (2008b)

or personal pension as they are more likely to be self employed and more likely to have spent time unemployed or in low paid, insecure work.[166]

Table 8:[167] The proportion in receipt of income sources by ethnic group

Income source	Asian/ Asian British Pensioners	Black/ Black British Pensioners	Chinese/ Other Pensioners	White Pensioners
State pension	80%	90%	84%	97%
Means tested benefits	47%	50%	37%	32%
Disability benefits	22%	22%	20%	23%
Occupational pension	30%	38%	43%	60%
Personal pension	4%	4%	6%	12%
Investment income	46%	39%	57%	73%
Earnings	12%	18%	16%	15%

Older pensioners receive less income from earnings and are more likely to be on a low income

The sources that pensioners receive their income from vary with age and older pensioners are more likely to be on a low income than younger pensioners (Chart 8). This variation in income sources may be partly due to the following factors.[168]

- **Earnings:** younger pensioners are more likely to be in work than older pensioners; 12% of pensioners under the age of 75 and 2% of pensioners over the age of 75 receive some income from earnings.[169] Therefore, older pensioners are likely to have less income than younger pensioners because they are less likely to receive income from earnings.
- **Eligibility for benefits:** As pensioners age they are more likely to gain a disability and become eligible for disability benefits. Pensioners are also more likely to qualify for income and age related benefits as they age and income from sources, such as earnings and pensions income, decreases.

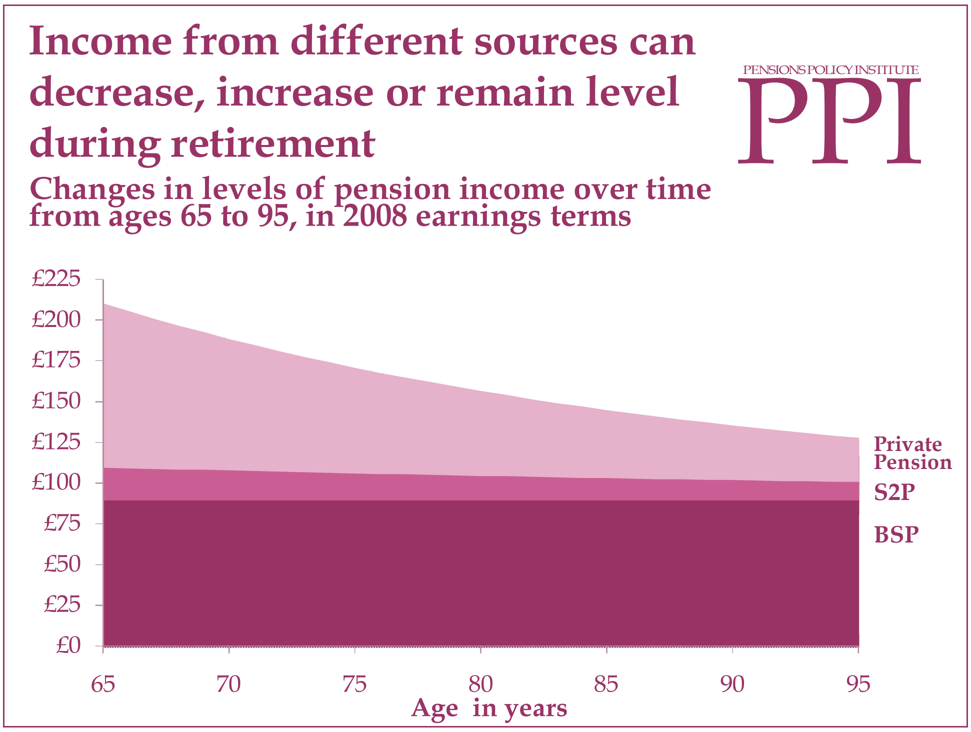
[166] EHRC, PPI (2008), Kennelly (2005)
[167] DWP (2008b) p. 73
[168] DWP (2008b)
[169] DWP (2008b) data on single pensioners in 2006/07

Chart 8[170]

The levels of income from some sources will change during retirement
The sources that pensioners receive their income from will affect how those levels of income change during their retirement. Income from different sources can increase, decrease or stay at the same level in earnings terms during retirement, depending on the way in which yearly adjustments are calculated. Chart 9 shows the way that income from BSP, S2P and an annuity from a private pension could change for someone retiring after 2012, in earnings terms, as they age.

[170] DWP (2008b) p. 25

Chart 9[171]



- Chart 9 shows the income of someone retiring after BSP has been linked to earnings (which will happen from 2012 or by the end of 2015 at the latest) in 2008 earnings terms. In Chart 9, the BSP income stream stays at the same level in earnings terms throughout retirement.
- The income from S2P[172] declines in earnings terms during retirement as it is indexed to prices (RPI) which generally increase at a slower rate than earnings.
- Income from a private pension could decline more quickly in earnings terms than S2P and BSP, for instance, if it is from a level annuity. Chart 9 shows the income in earning terms from a level annuity which pays a rate of £100 per week.[173]
- However, people may also purchase annuities that are linked to prices which decline more slowly in earnings terms, as seen in the S2P income stream.
- Income from DB pensions are also generally linked to prices, though there may be a limit placed on the annual increase allowed.

[171] PPI Modelling
[172] Chart 9 shows a starting S2P entitlement of £20 per month, the average 06/07 entitlement for a man, not including income from contracted-out pensions. See PPI (2008a) *Pensions Facts*
[173] A level annuity will pay the same amount to the annuitant every year until their death.

Initial levels of retirement income have changed over time for pensioners

Each generation of pensioners is likely to have a higher income than previous, older generations. This may be due to many factors, including those below:[174]

- **Availability of pension saving products:** younger pensioners are likely to have more income than older pensioners because of the availability of different savings products when they were young. For example, there was more availability of occupational pensions for those born in the 1930s than those born in the 1910s which has implications for the incomes of these age groups when they retire.[175] The current trend is for each new 'cohort' of pensioners to have a higher income than those older than them. However with the decline in DB pensions, the trend may become for pensioners to have less or the same income as previous generations.
- **The length of time spent in retirement:** pension income from occupational pensions and annuities is generally linked to earnings at the point of retirement but then tends to rise in line with the Retail Price Index (RPI) rather than earnings, though this depends on the type of pension or annuity a pensioner receives. Earnings generally rise slightly faster than RPI, though this is not always the case. Therefore, as pensioners age their incomes are likely to become relatively smaller than the incomes of younger pensioners.[176]
- **Changes in the structure of the household unit:** As pensioners age they are more likely to live alone, due to partners dying or family moving away (Chart 5, chapter 2). Pensioners who live alone are more likely to be on a low income. This could be due to many factors such as loss of income and assets or loss of free support and care which must now be paid for, though it may also be a factor of age.

Pensioner households may have trouble meeting needs or attaining desired levels of expenditure

The fact that older pensioners are more likely to be on a low income indicates that pensioners may have trouble meeting their needs or desired levels of expenditure as they age, though pensioners on a very low income may have many of their primary needs provided for by state benefits and state support through health and social care services.

It is also possible that the average pensioner could find it difficult to meet both of the spending increases in early and later retirement (Chart 3, chapter 2) identified as a reaction to both income needs and people's expectations for their retirement. Pensioner's income tends to decline during retirement and pensioner households may not have the resources to meet the later spending increase around the age of 90, identified as a

[174] DWP (2008b) see page 20: the 'age' effect; the 'cohort' effect; the length of time since retirement
[175] DWP (2008b)
[176] DWP (2008b)

reaction to increases in the need for health and mobility related spending, increases in spending on housing, food, fuel and power while maintaining some spending on leisure related goods and services. However, pensioners with assets such as housing or savings may be able to use these to fund increases in needs in later retirement.

Conclusions

There are many different income sources which can be used to fund retirement, and different sources tend to have different levels of income associated with them. On considering each source in isolation as well as in comparison with other sources, the following variations have been highlighted:

- Pensioners who receive the majority of their income from earnings or occupational pensions are likely to be receiving a higher income than pensioners in general.
- Pensioners who receive the majority of their income from state benefits are likely to be on a lower income than pensioners in general
- The majority (over 50%) of pensioners can expect to receive some inheritance during their lives, which, for those who receive substantial amounts could be used to help fund retirement.
- Support provided by family and community could reduce living expenses for some pensioners.
- Pensioners with savings/assets of at least £1,500 are much less likely to fall into a low income group than pensioners with no savings/assets.

This chapter also examined the ways that income sources differed across different household units, age groups, genders and ethnicities:

- Pensioner couples receive a larger proportion of their income from earnings and occupational pensions than single pensioners.
- Single pensioners, older and female pensioners receive a larger proportion of their income from state benefits than pensioner couples, male pensioners, and younger pensioners.
- Younger pensioners and female pensioners are more likely to receive income from earnings than older pensioners and male pensioners.
- Older pensioners are likely to receive slightly more income from occupational pensions than younger pensioners.
- Ethnic minority pensioners are less likely to receive income from occupational pensions than white pensioners, but are more likely to receive income from earnings.

Income sources change over time for all pensioner household units partly as a result of changes in:

- Earnings – younger pensioners are more likely to receive income from earnings than older pensioners.
- Eligibility for benefits – older pensioners are more likely to be in receipt of certain state benefits, especially disability related benefits.

Levels of income have changed for pensioners over time as a result of:

- The changing availability of pension products – younger pensions often have had greater access to savings and pension products than older pensioners.
- The length of time older pensioners have spent in retirement – often pension income rises more slowly than earnings.
- Changes in household structure - older pensioners, especially women, are more likely to live alone. Living alone in older age is associated with lower income.

Chapter four: Do pensioners in Britain have sufficient income to meet their needs?

It is difficult to make predictions about the future adequacy of pensioner's incomes, but we can look at a number of hypothetical cases to illustrate what the circumstances of typical households retiring in 2008 may look like. This chapter uses four hypothetical individual pensioners and four hypothetical pensioner couples to examine how different baskets of assets and income might be able to fund different need sets in retirement.

Each hypothetical individual and couple (Tables 9 and 10) is assumed to start out at retirement with a different set of assets and income, representing the spectrum of experiences from those who rely solely on state pension and state benefits in retirement to people with large baskets of assets including property, pensions, savings and investment income. Table 11 shows the quintile of pensioner income distribution that each individual and couple fall into. The hypothetical individuals and couples are intended to illustrate some of the possible variations within the range of assets and income baskets that people may have. They are not intended to be representative of the average pensioner.

Table 9:[177] Hypothetical individuals experiencing life course scenarios, weekly income in 2008 at SPA 60 (F), 65 (M)

Individual	Total state pension (SP)[178] income and state benefit income at SPA	Private and occupational pension income at SPA	Other income	Tenancy – weekly rent or house value in 2008
Keisha: a 60 year-old low-earning woman	£123 (SP) £5 (PC)[179] £70 (HB)[180] £15 (CTB)[181]	No income from this source	£1pw from savings £10,000 inheritance at age 70	£70pw Rent
Amit: a 65 year-old median-earning man	£187 (SP)	£72 level annuity (from DC pension)	£6pw from savings	Owner occupier worth £200,000
Grace: a 60 year-old high-earning woman	£230 (SP)	£304 index linked (from DB pension)	£20pw from savings	Owner occupier worth £250,000
William: a 65 year old man on disability benefits	£96 (SP) £31 (PC)[182] £70 (HB) £15 (CTB) £44.85 (AA)[183]	No income from this source	No other income	£70pw Rent

[177] Figures in table (except Attendance Allowance) rounded to nearest pound, for further details on each individual see Appendix 3
[178] Including Graduated Retirement Benefit, SERPS and S2P income
[179] Pension Credit: Guarantee Credit – £4.75, not eligible for Savings Credit until age 65
[180] Housing Benefit
[181] Council Tax Benefit
[182] Pension Credit: Guarantee Credit – £27.67, Savings Credit - £3.06
[183] Attendance Allowance

Table 10:[184] Hypothetical couples experiencing life course scenarios, income in 2008 at SPA 60 (F), 65 (M)

Individual	Total state pension (SP)[185] income and state benefit income at SPA	Private and occupational pension income at SPA	Other income	Tenancy – weekly rent or house value in 2008
The Chens – a median earning man and a high earning woman	£417 (SP)	£375 level annuity and index-linked DB pension	£26pw from savings	Owner occupiers worth £250,000
The Greens - a median earning man and a low earning woman	£310 (SP)	£63 level annuity (from DC pension)	£7pw from savings	Owner occupiers worth £200,000
The Smiths – a couple on disability benefits	£201 (SP) £21 (PC)[186] £70 (HB)[187] £14 (CTB)[188] £89.70 (AA)[189]	No income from this source	No other income	£75pw Rent
The Khans – man on disability benefits and a low earning woman	£220 (SP) £19 (PC)[190] £68 (HB) £13 (CTB) £44.85 (AA)	No income from this source	No other income	£75pw Rent

Table 11:[191] Pensioner income distribution of hypothetical individuals and couples at SPA in 2008

Pensioner individual/couple	Total income at SPA (AHC)	Pensioner income distribution (AHC)
Keisha	£129	20% to 40% quintile
Amit	£264	80% to 100% quintile
Grace	£554	80% to 100% quintile
William	£172	60% to 80% quintile
The Chens	£819	80% to 100% quintile
The Greens	£380	60% to 80% quintile
The Smiths	£308	20% to 40% quintile
The Khans	£277	20% to 40% quintile

184 For further details on each couple see Appendix 3
185 Including income from Graduated Retirement Benefit, SERPS and S2P
186 Pension Credit: £21.23 Savings Credit
187 Housing Benefit
188 Council Tax Benefit
189 Attendance Allowance
190 Pension Credit: £18.97 Savings Credit
191 Pensioner's income: PPI Modelling, Income distribution: DWP (2008b) table 4.1, figures 2008 uprated

In order to enable analysis of how different baskets of assets and income could be used to fund different need sets, each couple and individual is assumed to live through several different life course scenarios (Table 12) which are intended to illustrate some of the experiences that pensioners may have. Life course scenarios include experiences such as: working after SPA, losing a partner, the onset of a disability, high and low life expectancy and receiving an inheritance.

Table 12:[192] Life courses experienced by hypothetical individuals

Life course scenarios	
Baseline scenario	Individual dies at age 82 (M), 85 (F) (median life expectancy)
Longer working	Individual dies at age 82 (M), 85 (F) (median life expectancy) and works after SPA part time for 5 years
Severe disability	Individual dies at age 92 (M), 95 (F) (high life expectancy), acquires a low severity disability at age 75 (M), 75 (F),[193] acquires a high severity disability at age 87 (M), 90 (F)[194]
Shorter life	Individual dies at age 70 (M), 70 (F) (low life expectancy), acquires a low severity disability at retirement 65 (M), 60 (F)

Each individual's income during their life course scenario is compared to the different measures of minimum and desired income in retirement set out in Chapter 1, including the desired replacement rates suggested by the Pensions Commission (Table 13).

Table 13:[195] Desired replacement rates for hypothetical individuals

Individual	**Income in working life per week**	**Percentile of earnings**[196]	**Replacement rate**	**Replacement income per week**
Keisha	£293	30th	70%	£205
Amit	£377	50th	70%	£264
Grace	£735	90th	60%	£441
William	£147	20th	80%	£118[197]

Further information about the individuals, couples, scenarios and the assumptions used in modelling is given in Appendix 3.

[192] Median, high and low life expectancy calculated from the ONS interim Life Tables based on UK data from 2005 – 2007 based on a future life expectancy from current age: 60 for females, 65 for males. Estimated time of average spell of post SPA retirement estimated from data regarding length of work after retirement, DWP (2003), p. 15
[193] Based on data from Kellard *et. al.* (2006). 55% of people age 75 have a moderate or severe disability
[194] Based on data from Kellard *et. al.* (2006). Around 50% of people age 87 -90 have a severe disability
[195] Pensions Commission (2004)
[196] Labour Force Survey 2007 data
[197] This replacement rate is below the poverty line and would therefore not be considered adequate to provide a basic acceptable standard of living, Pensions Commission (2004)

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 individuals with a certain basket of assets and income faced a certain set of experiences in retirement?*) The life course scenarios and income levels examined in this paper are intended as illustrative rather than as forecasts. The analysis seeks to illustrate the potential impact of a *range* of possible life course scenarios and is not intended to imply that any of the life course scenarios or income levels is more likely to occur for individual pensioners than any other. Many more factors than are allowed for here would need to be incorporated into this type of analysis to produce a forecast.

For each scenario, the analysis illustrates the levels of income which might be available to the hypothetical individuals and couples during their retirement, and compares this to different measures of needs and expectations. The scenarios consider the relative poverty and Minimum Income Standard lines after housing costs (rent/mortgage and council tax) have been taken out.

This paper does not show each couple and individual experiencing all four of the life course scenarios. Each scenario that is discussed focuses on the individual or couple that best illustrates the potential impacts which particular experiences may have on pensioner's income.

Do individual pensioners have enough income to meet their needs as they change during retirement?

The baseline scenarios (Charts 10 - 12) show the outcomes using the baseline assumptions for each of the individuals.

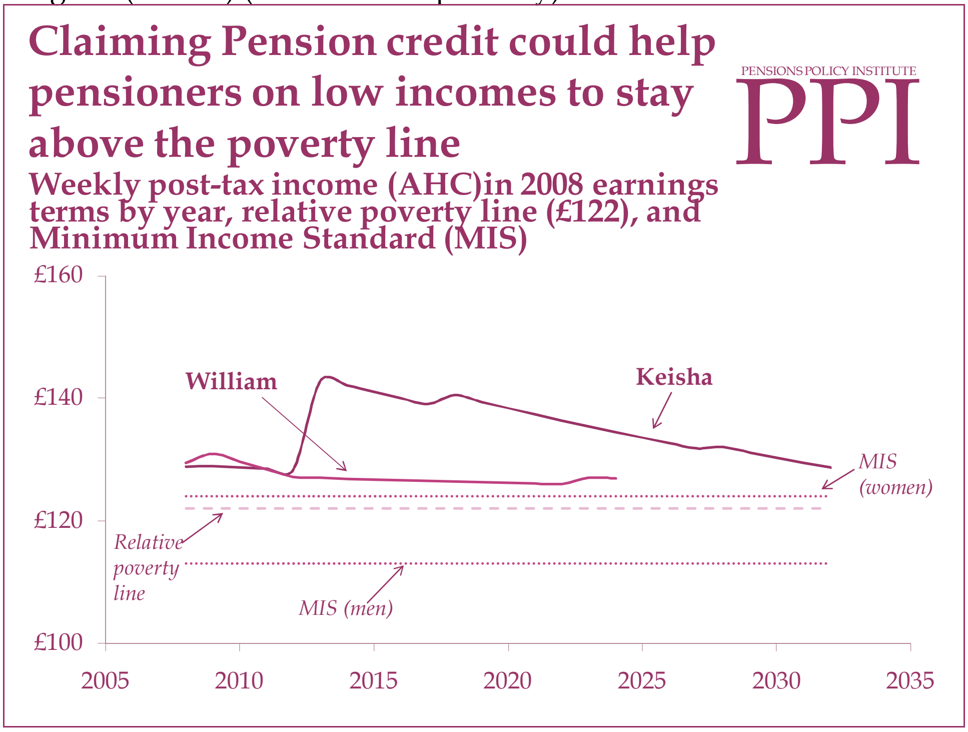
William is assumed to have a low severity disability at SPA. To account for the impact that disability has on his living standards, William's income is shown after subtracting the costs of disability.[198]

It is assumed that Keisha, Amit and Grace all retire at SPA, and that all of the individuals take their state, private and occupational pensions as soon as they reach SPA.

When comparing incomes against needs and expectations, Keisha and William's income is compared to the relative poverty line and the Minimum Income Standard lines as their incomes are low. Amit and Grace's incomes, which are higher, are compared to a spending cycle based on preferences as well as need.

[198] See appendix 2 for full calculations of the costs of disability

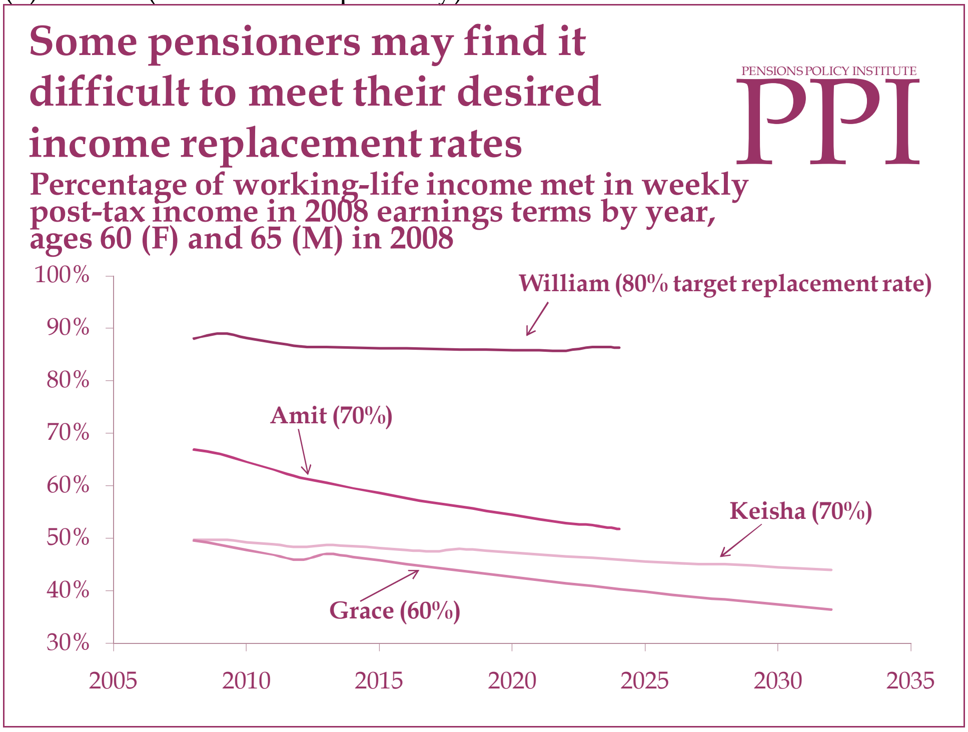
Chart 10:[199] Baseline Scenario: William dies at age 82 (in 2025), Keisha dies at age 85 (in 2033) (median life expectancy)



- William and Keisha (Chart 10) remain above the Government poverty line and the Minimum Income Standard lines for single adults (Chapter 1, Table 1) for all of their retirement. They are both in receipt of Pension Credit during their retirement. If they did not receive Pension Credit then William's income would be below the poverty line for all of his retirement and Keisha's would fall below the poverty line from her third year of retirement at age 62.
- Keisha's income declines more rapidly than William's in earnings terms as Keisha receives more income from SERPS and S2P which are linked to prices (RPI), whereas the majority of William's income comes from Basic State Pension.
- Keisha is not eligible for the Savings Credit element of Pension Credit until she is age 65. When she starts to receive Savings Credit, her income increases by around £15 a week.

199 PPI Modelling

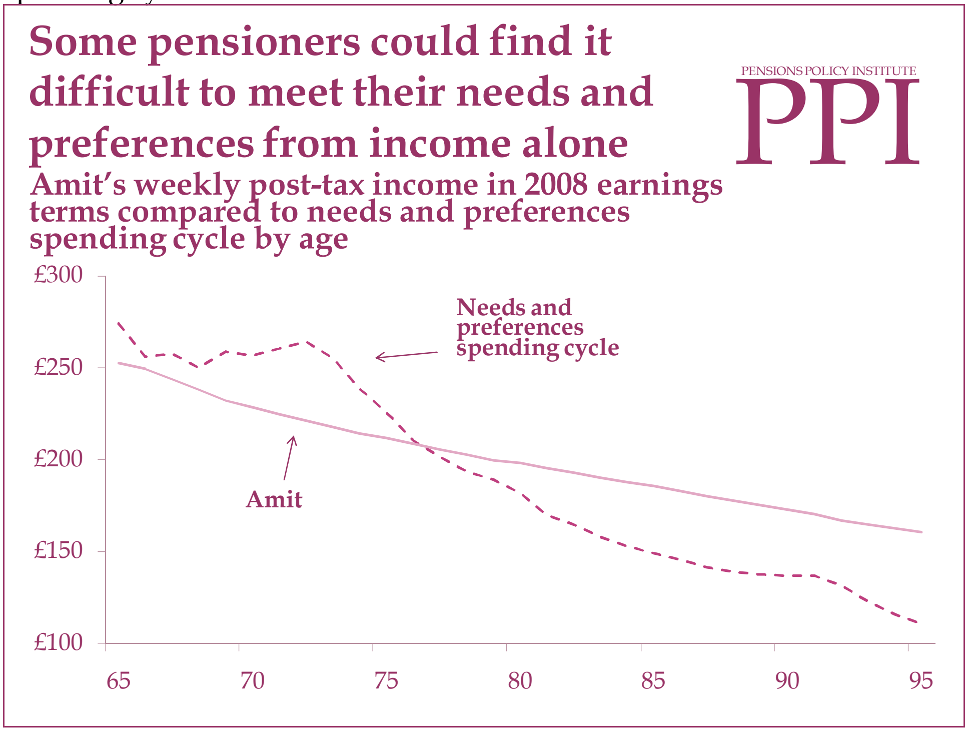
Chart 11:[200] Baseline Scenario: individuals die at age 82 (M) in 2025 and 85 (F) in 2033 (median life expectancy)



- Neither Grace, Amit or Keisha meet the replacement rates identified by the Pensions Commission (Table 13)[201] as the level of income needed to maintain a desired standard of living in retirement (Chart 11). William does exceed a replacement rate of 80% of his working-age income but as 80% of his working life income would be below the poverty line it would not be considered as a high enough level of income to provide an adequate standard of living.
- In order for Grace and Amit to reach their replacement rates for some or all of their retirement they would both need to use some of their capital and/or release equity from their homes, however this option would not be available to Keisha and William who have small or no savings and who do not own their homes.
- At age 70 Keisha inherits £10,000. In this scenario it is assumed that she draws down a weekly income from her inheritance of around £10 per week. She could use her inheritance to help meet her replacement rate of £205 per week, however this would deplete her inheritance after about two years and she may wish to save the capital for use in emergencies or for the later years of her retirement.
- The desired replacement rate calculations assume that a flat rate of income is needed by pensioners to meet their expectations throughout retirement, but desired income may change during retirement (Chart 12).

[200] PPI Modelling
[201] Pensions Commission (2004)

Chart 12:[202] Baseline Scenario compared to needs and preferences spending cycle for Amit



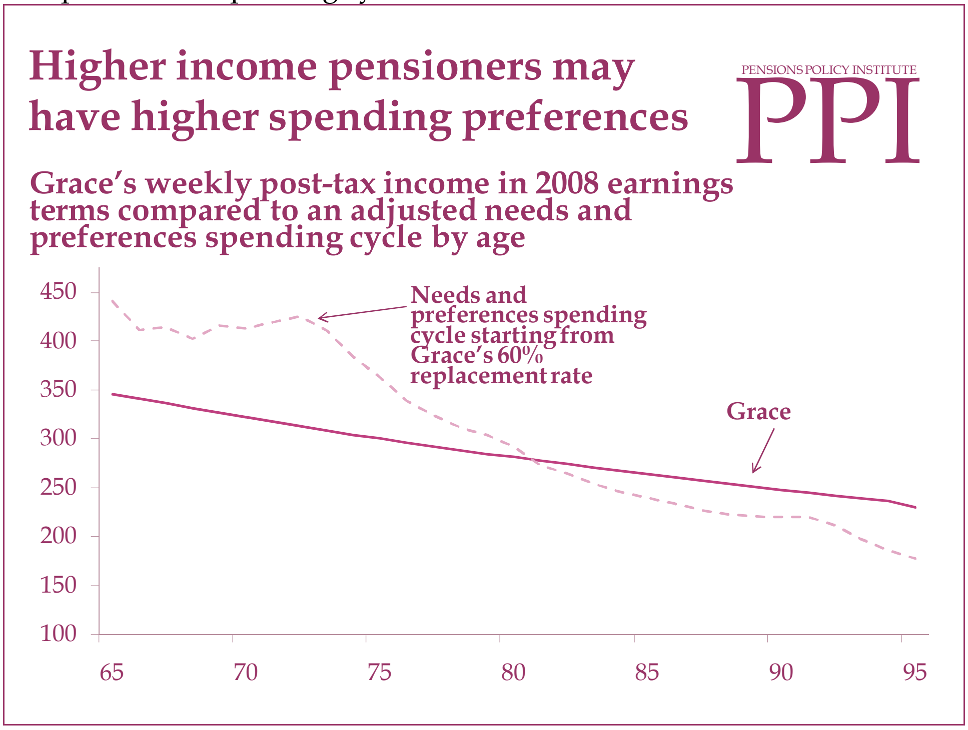
- The needs and preferences spending cycle line[203] (Chart 12) indicates that there could be periods of higher and lower spending in retirement as a result of spending preferences, such as a preference to spend more on recreation and leisure in early retirement, or the need to spend more on housing, fuel, food and power in later retirement as mobility diminishes and health needs become more prominent. The amounts spent each week differ from pensioner to pensioner, and would depend on their income in working life, their particular spending preferences and their specific needs in retirement. However the pattern of the spending cycle in Chart 12 may be an indication of how expenditure could change during retirement.
- Amit's income line does not follow the same trend as the pattern in the needs and preferences spending cycle. His income gradually decreases in earnings terms in every year during retirement, whereas the spending cycle sees spending increase in some years.
- Amit may find it difficult to meet initial spending highs from his income alone though he could meet them by using income from his savings. Amit could find meeting later spending increases in his 80s and 90s easier from his income alone. However, this spending cycle represents an average for pensioners and Amit's needs may be for

[202] PPI Modelling (Income), Life Trust, cebr (2008) (needs and preferences spending cycle). As Grace and Amit are different ages in 2008, the Chart shows income from age 65 rebased to 2008 earnings terms.
[203] (Chapter 2, Chart 3), Life Trust, cebr (2008). In this and subsequent charts the needs and preferences spending cycle has been re-calculated in 2008 earnings terms, to allow comparison with incomes.

higher spending than depicted in this chart if, for instance, he acquires disabilities as he ages.

- In particular, if Amit acquired a severe disability in later life, and needed intensive home care or to enter a home, his spending needs may increase significantly compared to those shown for the 'average' pensioner in Chart 12.
- As a higher income pensioner, Grace may prefer to have a higher initial level of spending than the 'average' pensioner. If her own individualised needs and preferences spending cycle followed the same pattern as that of the average pensioner, but started at her target replacement income level of 60% of pre-retirement earnings, Grace may find it difficult to meet her initial spending preferences (Chart 13). It should be noted that Grace has income above the needs and preferences spending cycle for the 'average' single pensioner throughout her retirement.

Chart 13:[204] Baseline Scenario compared to an alternative illustrative needs and preferences spending cycle for Grace.

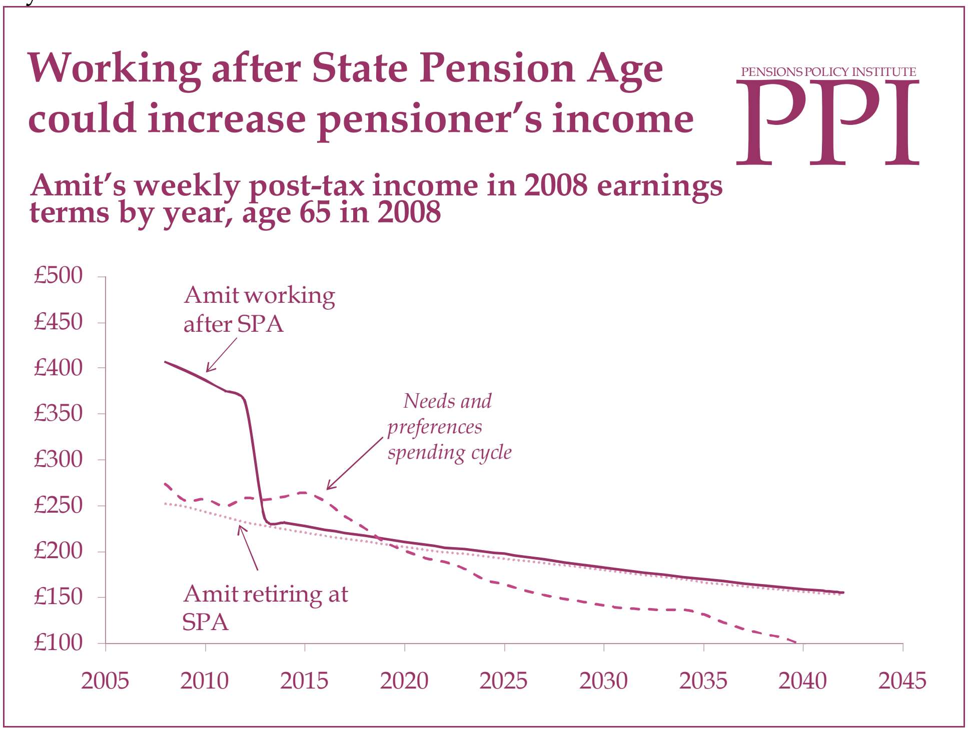


[204] PPI Modelling (Income), Life Trust, cebr (2008) (needs and preferences spending cycle) adjusted to start at 60% of Grace's pre-retirement earnings. This is an illustrative cycle, as preferences and needs are likely to vary between different income groups.

How does working after State Pension Age affect income in retirement? In the Longer Working Scenario (Chart 14) it is assumed that Amit works part time after SPA for 5 years.[205] Amit is assumed to take his State and private pension at SPA to supplement the earnings from his part time work.

If he deferred his pension he may increase his pension income in later retirement, but would then forgo receiving income from his pension during the years of deferment.

Chart 14:[206] Longer Working Scenario: Amit works part time after SPA for 5 years



- The boost in income that comes from working an extra 5 years part time (Chart 14) means that Amit could find meeting initial spending highs identified in the needs and preferences spending cycle (Chapter 2, Chart 3) easier in early retirement than if he had retired from work at SPA. If he spends his earnings right away (as is assumed in this modelling) then it will not necessarily mean that his income in later retirement will be higher than if he had not worked, however the extra income generated from working longer could be saved and used to meet increases in needs in later retirement.

[205] Estimated time of average spell of post SPA retirement estimated from data regarding length of work after retirement, DWP (2003), p. 15

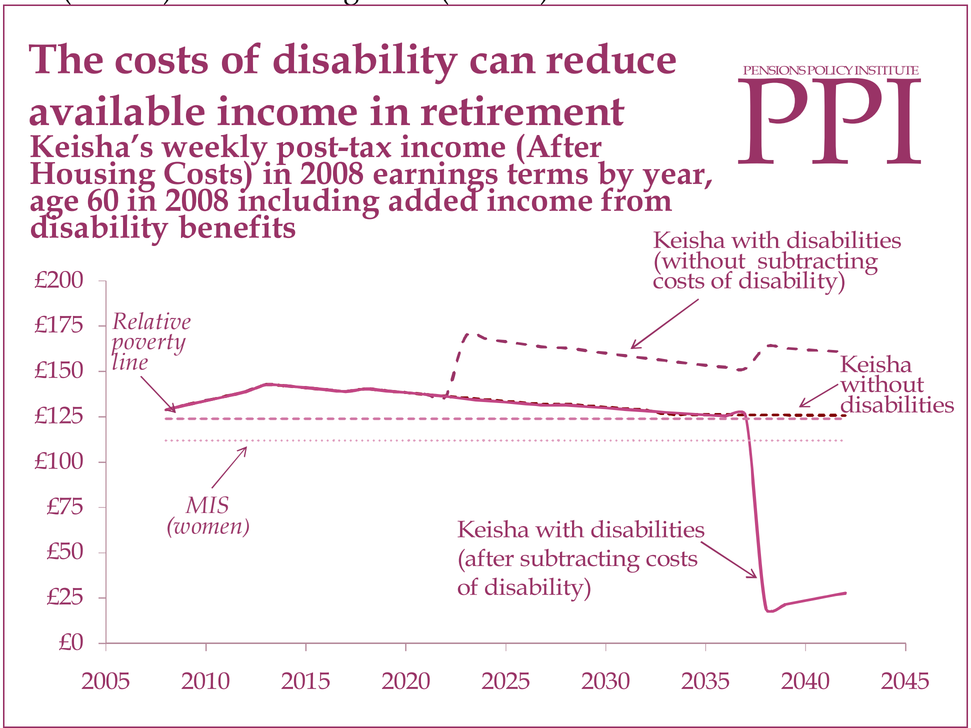
[206] PPI Modelling (Amit's income), Life Trust, cebr (2008) (needs and preferences spending cycle). Chart data depicted in cash terms, allowing for yearly increases in inflation of 2.5%

How do episodes of disability affect income in retirement?
In the Severe Disability Scenario (Chart 15) it is assumed that Keisha acquires a low severity disability age 75[207] and acquires a high severity disability at age 90 in 2038.[208]

As a result of this disability, Keisha receives the lower rate of Attendance Allowance of £44.85 per week (2008/09 rate) when she has a low severity disability and receives the higher rate of £67.00 per week when she has a high severity disability.

These additions are reflected in the income shown in Chart 15, which also shows Keisha's income after subtracting the costs of disability.[209] Keisha is assumed to die at age 95 in 2043.[210]

Chart 15:[211] High Severity Disability Scenario: Keisha acquires a low severity disability at age 75[212] (in 2023), a high severity disability at age 90[213] (in 2038) and dies at age 95[214] (in 2043).



[207] Based on data from Kellard *et. al.* (2006). 55% of people age 75 have a low, moderate or severe disability
[208] Based on data from Kellard *et. al.* (2006). Around 50% of people age 87 -90 have a severe disability
[209] See appendix 2 for full calculations of the costs of disability
[210] Long life expectancy
[211] PPI modelling
[212] Based on data from Kellard *et. al.* (2006). 55% of people age 75 have a low, moderate or severe disability
[213] Based on data from Kellard *et. al.* (2006). Around 50% of people age 87 -90 have a severe disability
[214] Long life expectancy

- The costs associated with a high severity disability are calculated as being 131% of the mean income of pensioners,[215] making the cost of severe disability equal to around £260 per week in 2008.[216] However, the highest available rate of Attendance Allowance is £67.00 per week in 2008/09.
- When Keisha acquires a high severity disability at age 90 (in 2038) her actual income rises to around £160 per week (in 2008 earnings terms) as a result of receipt of disability benefits, but after subtracting the costs associated with a high severity disability Keisha's available income falls to around £20 per week (Chart 15), which is below the relative poverty and Minimum Income Standard lines.
- As Keisha would not be able to meet the costs associated with having a high severity disability and still maintain an adequate standard of living she may need to depend on family, or receive state support in the form of Local Authority or NHS care as a result of her disability.[217]
- This scenario indicates that that if pensioners qualify for Attendance Allowance they may be able to meet the costs of a low severity disability without an adverse effect on their available income, but that pensioners may find it difficult to meet the costs associated with high severity disability unless they have a high income and/or extra savings and assets.

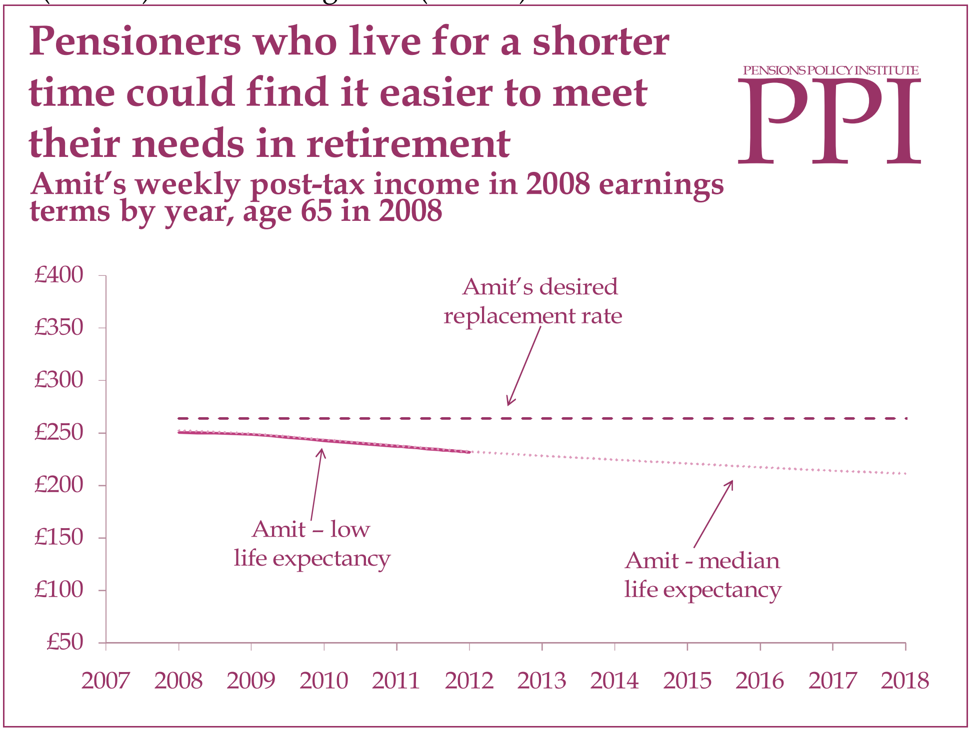
The High Severity Disability Scenario indicates that acquiring a low severity disability may not affect people's available income if they qualify for Attendance Allowance as the costs associated with a low severity disability (around £45 per week in 2008/09)[218] are similar to the lower rate of Attendance Allowance (£44.85 per week in 2008). However the costs of disability used in this paper are intended to represent the average experience and the actual costs associated with a low severity disability may be higher or lower than £45 per week. Therefore, acquiring a low severity disability may affect the income available to pensioners in a different way than seen in this scenario.

How does living for less than median life expectancy affect income in retirement?

In the Shorter Life Scenario (Chart 16) it is assumed Amit has a low severity disability at SPA, age 65 (in 2008), and Amit's income is shown after subtracting the costs of this disability.[219] It is assumed that Amit dies at age 70 (in 2013) (low life expectancy).

[215] Zaidi and Burchardt (2005)
[216] Mean income of pensioners in 2008 is £199.13, DWP (2008b)
[217] Individuals with savings, housing or other assets may be required to use these to fund care that they receive from the State or Local Authority.
[218] Costs of disability calculated using Zaidi and Burchardt (2005) p. 103. For full calculations see Appendix 2
[219] See appendix 2 for full calculations of the costs of disability

Chart 16:[220] Shorter Life Scenario: Amit has a low severity disability at age 65 (in 2008) and dies at age 70[221] (in 2013)



- If Amit only lives for five years after retiring (Chart 16) his income does not have the chance to decrease as dramatically in earnings terms as it would if he lived for longer.
- Amit would require around an extra £5,000 in total income to meet his replacement rate of £264 during his five years in retirement, which he could cover with his savings.
- Whether Amit would use his savings and equity to meet his replacement rate or his needs as they change during retirement could depend on his family circumstances, styles of financial behaviour and his own perception of how long he is going to live.
- In reality, Amit may wish to spend less on leisure related activities than the average pensioner of his age as a result of his low severity disability.

[220] PPI Modelling
[221] Low life expectancy

Do pensioner couples have enough income to meet their needs as they change during retirement?

The next section of this chapter examines how pensioner couples with different baskets of assets and income may be able to fund different need sets in retirement. It is worthwhile to look at pensioner couples as well as individual pensioners as couples are likely to have income from different or more varied sources than single pensioners and are likely to have some different experiences in retirement which affect income needs and expenditure such as widowhood or having a disabled partner.

The hypothetical couples that are used as case studies in this chapter are all mixed-sex married couples. It is important to note that unmarried couples, same-sex couples and civil partners are likely to have some variation in income levels and needs sets from married, mixed-sex pensioner couples. Unmarried pensioner couples (same-sex or mixed-sex) may not have the same entitlement to receive income or benefits from their partner's state and private pension as married pensioners. Unmarried partners may also encounter problems with inheritance (if their partner dies intestate), capital gains tax, and assessment for care home charges (where married partners often have their homes disregarded in assessments of their ability to pay for their own care).[222]

The Civil Partnership Act 2004,[223] entitled same-sex civil partners to the same state pension benefits as married mixed-sex couples and required occupational and private pension providers to backdate entitlement for the civil partners of scheme members from 1988.[224] However same-sex couples are still likely to face income differences from married mixed-sex pensioner couples as partners will often not benefit from private and occupational pension accrual that occurred before 1988. It is also likely that some same-sex pensioner couples in the UK have not formed civil partnerships,[225] and will continue to encounter many of the income and entitlement restrictions of unmarried partners.

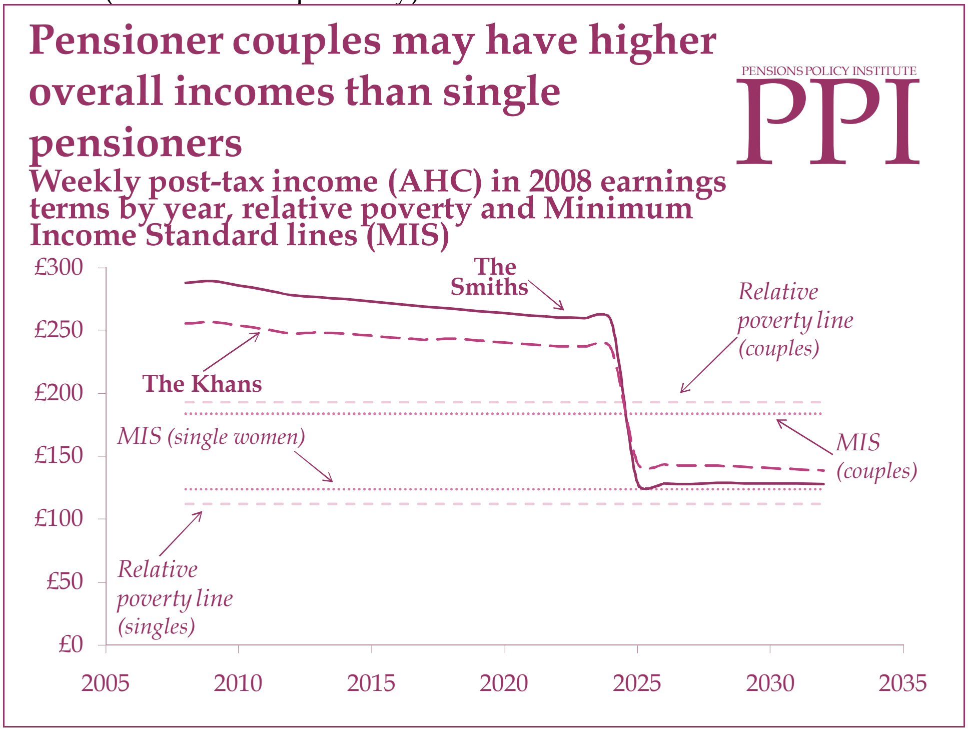
How does losing a partner affect pensioners' income in retirement?

In the Baseline Scenario for couples (Charts 17 and 18) it is assumed that the Chens and the Greens have no incidences of disability. However, Mr and Mrs Smith and Mr Khan have a low severity disability at SPA, and for these couples income is shown after subtracting the costs of disability.[226]

All of the couples retire at SPA and take their State, private and occupational pensions.

[222] Age Concern (2002)
[223] www.opsi.gov.uk/acts/acts2004/ukpga_20040033_en_1
[224] For more information on civil partner entitlements see UNISON (2007)
[225] 26,787 civil partnerships were formed between the introduction of the Civil Partnership Act 2004 and the end of 2007. In 2007, 8,728 civil partnerships were formed. The rates have fallen since the introduction of the Act and halved in 2007 from 2006. ONS (2008b) www.statistics.gov.uk/cci/nugget.asp?id=1685
[226] See appendix 2 for full calculations of the costs of disability

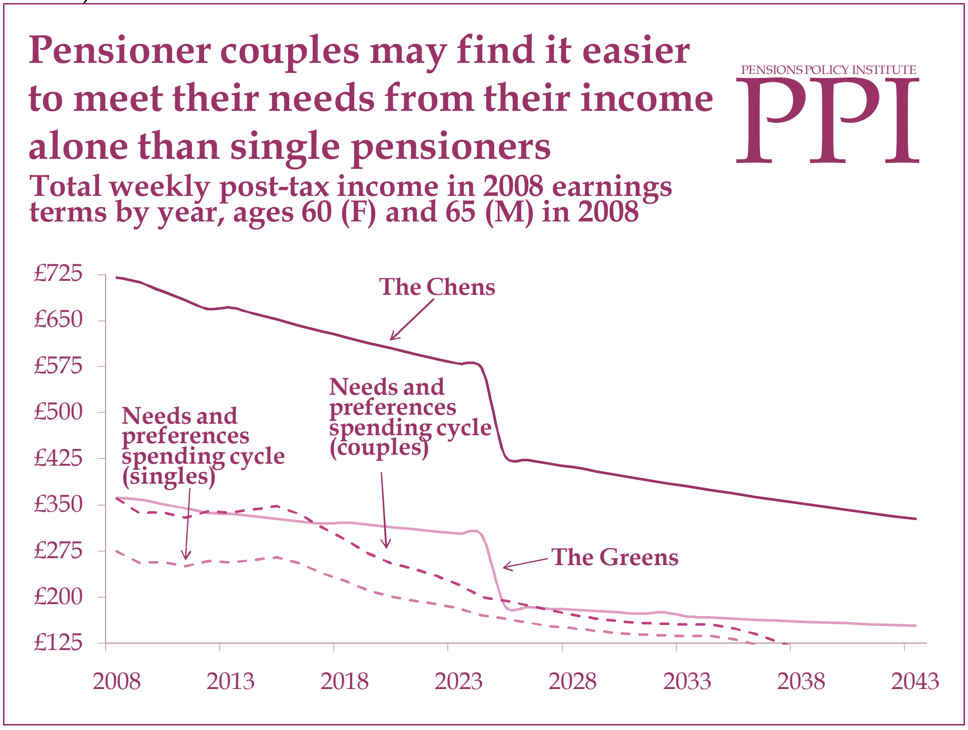
Chart 17:[227] Baseline Scenario: Couples die at age 82 (M) in 2025 and 85 (F) in 2033 (median life expectancy)



- The Smiths and the Khans remain high above the poverty line and the Minimum Income Standard (MIS) line while both partners are alive (Chart 17).
- When Mr Smith and Mr Khan die, both Mrs Smith and Mrs Khan's income falls to just above the relative poverty line for single pensioners and the MIS for single women pensioners. Mrs Smith and Mrs Khan are between £10 - £30 a week more well off after their husbands deaths than they would have been if they were single because they both receive benefits from their husbands' state pension.
- Mrs Smith's income after her husband's death is lower than Mrs Khans, partly because she does not qualify for the Guarantee Credit element of the means-tested benefit, Pension Credit, due to having around £10,000 in savings (in 2008 earnings terms).
- If Mrs Smith did not receive Pension Credit after her husband's death, she would fall below both the poverty and MIS lines.

[227] PPI Modelling

Chart 18:[228] Baseline Scenario (with extended lives for Mrs Chen and Mrs Green)



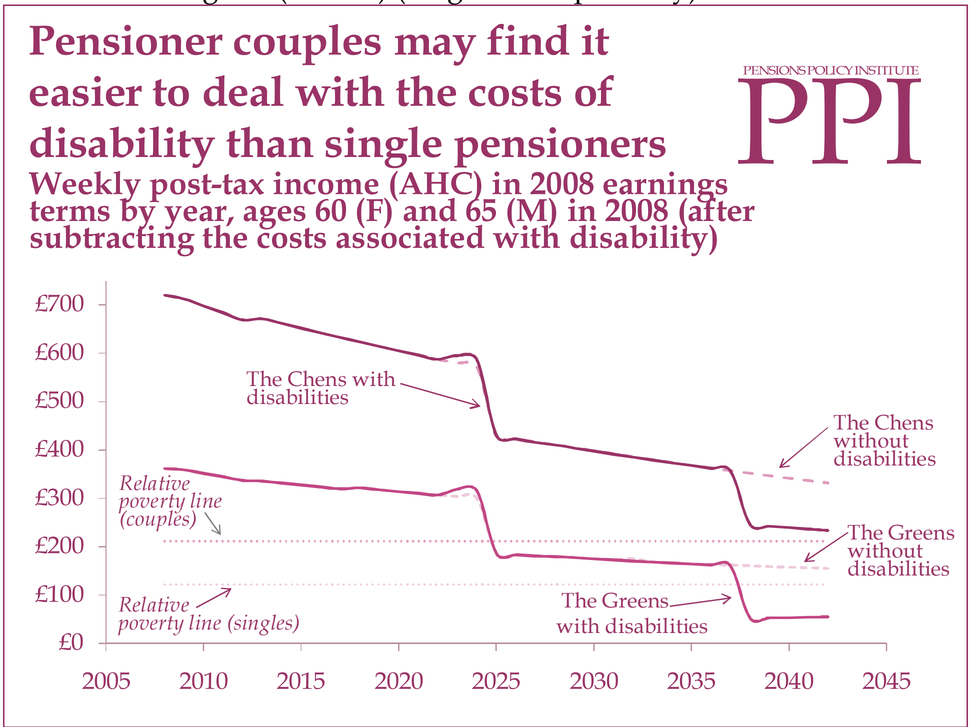
- The Chens and the Greens have higher combined incomes than they had as single pensioners and are both able to afford the spending pattern set out in the needs and preferences spending cycle for the 'average' pensioner household at almost every age (Chart 18). In reality the Chens and the Greens may prefer to spend a different amount than the 'average' pensioner household used in the spending cycle.
- Even after Mr Chen's death, Mrs Chen's income is around £300 a week higher (in cash terms) than it would have been if she were single, as a result of receiving benefits from Mr. Chen's pension, a level annuity.
- Mrs Green benefits less than Mrs Chen from her husband's pension after his death, even though Mr Chen and Mr Green both have the same level annuity (from a DC pension). This is because Mrs Green would have been entitled to around £200 per week in means tested benefits (including Housing and Council tax Benefit) if she had been single. In cash terms, Mrs Green is around £100 a week better off after Mr Green's death than she would have been if she was single (Chart 10).

[228] PPI Modelling

How does disability affect the income of pensioner couples in retirement?

In the Severe Disability Scenario (Chart 19) it is assumed that Mrs Green and Mrs Chen acquire a low severity disability at age 75 and a high severity disability at age 90. Chart 19 shows the Couple's weekly income after subtracting the costs of disability.[229] Mr Green and Mr Chen die at age 82 (median life expectancy) and that Mrs Green and Mrs Chen die at age 95 (long life expectancy.

Chart 19:[230] Severe Disability Scenario: Men die at age 82 (in 2025) and women die at age 95 (in 2043) (longer life expectancy)



- When Mrs Green and Mrs Chen acquire a low severity disability at age 75 (in 2023) (Chart 19), the Couples' weekly income is reduced by less than it would have been if they had been single pensioners. This is because the costs associated with disability are lower for pensioner couples than for single pensioners (Chapter 2, Table 5) owing to pensioner couples being able to provide care for each other and to share disability and mobility related equipment.
- By the time Mrs Green acquires a severe disability at age 90 (in 2038), Mr Green has died. Mrs Green is not able to afford the costs of disability from her own income without falling below the poverty line, and may need to depend on family or the State for support.
- Mrs Chen, who receives an income from her own DB pension as well as from her husband's pension (a level annuity) is able to afford the

[229] See appendix 2 for full calculations of the costs of disability
[230] PPI Modelling

costs of high severity disability and still have an available income of around £250 per week. If she had been a single pensioner, then the costs of high severity disability would have caused her available income to drop to around £140 per week.

- If Mr Chen and Mr Khan provide care for their wives when they are disabled, they may qualify for Carers Allowance and receive an extra £50.22 per week in income.

Conclusions

- Most of the pensioners modelled see a drop in their income in later retirement as their pension income fails to keep its value in real (earnings) terms.
- None of the individuals modelled, even those on median to high earnings, are able to meet a replacement rate calculated to replicate working-life living standards in retirement[231] solely from their pension income though they may be able to meet their replacement rates for some or all of their retirement by using their savings and/or releasing equity from their homes.
- Pensioners who earned at median to high levels during their working life and have complete (private or occupational) pension saving records, could find it easier to meet many, but not all, of their needs in retirement from income alone. However even higher income pensioners may not be able to meet all of their spending preferences solely from income if they aim to have a standard of living similar to that they had in their working life.
- Pensioners may find it easier to maintain similar consumption levels in retirement to those they experienced in working life if they have a combination of assets and savings to use in retirement as well as income from State and private pensions.
- Pensioners may find it easier to meet changes in needs and expenditure preferences if they conserve their income during some of the years of their retirement and spend more than their average yearly income during others. They may also wish to supplement their pension income with income from assets and savings during times where greater expenditure may be needed to meet changes in needs or preferences.
- Working part or full-time after State Pension Age can increase pensioner income which can be used to boost expenditure during the years in which is it is earned, or can be saved and used later in retirement to meet changes in needs and spending preferences. Working part time after SPA can be a way to ease the transition into receiving a lower income in retirement.
- Acquiring a disability in retirement could reduce available income depending on the severity level of the disability and the level of state benefits which pensioners receive as a result of their disability. Acquiring a high severity disability in retirement could incur a very

[231] Pensions Commission replacement rate, (Table 13), Pensions Commission (2004)

high level of costs which pensioners may not be able to afford on their own. Pensioners with one or more disabilities may need to depend on family, or receive state support in the form of Local Authority or NHS care, depending on the level of costs incurred by their disability.

- Pensioners in couples are likely to have a higher level of available income than single pensioners. Living expenses, including housing, and the costs of disability are likely to be lower per person in pensioner couples than for single pensioners. Pensioners in couples also have the possibility of benefiting from a partner’s higher pension entitlement.
- Pensioners who have lost a partner are likely to have a higher income than pensioners who were never partnered but have the same income and earnings history, due to receiving entitlement from their partner’s state pension and possibly their private or occupational pensions.

Appendix 1:

Budget standards

The first budget standard was drawn up in 1901 by Benjamin Seebohm Rowntree during his 1899 survey of York, *'Poverty, a Study of Town Life'*.[232] Rowntree's survey took information about the rent that families paid and the minimum they would need to spend on clothes in order to maintain health, perform their work and maintain social respectability. Rowntree calculated the minimum amount of food, fuel and other household sundries which a family would need. Using all of these calculations Rowntree drew up a 'Basket of Goods' which represented the minimum food and goods a household unit required to maintain mere physical efficiency. The cost of this basket of goods was the first minimum budget standard for Britain, and Rowntree considered households with incomes below this number to be below the poverty line.

Since Rowntree's study there have been several other studies which attempted to calculate the minimum income which household units require to be considered above the poverty line,[233] however more recent studies have taken into account the need for social and cultural participation in calculating budget standards.

Budget standards are tailored to different household units, e.g.: single adults, couples with children, single pensioners etc. The customary method of designing budget standards is through consultation with people representative of the group that the standard is being created for, so that the consumption preferences and capabilities of particular groups can be accounted for. People are asked to form a consensus regarding which goods and services are necessary for them to maintain a minimum acceptable standard of living. Then the 'basket' of goods and services are priced and the total is given as the budget standard for that individual or household.

It should not be concluded that any given minimum income standard will suit all people. Different people may have different needs because of living in rural or urban areas, areas where goods cost more or less, having a disability or other specialised needs.[234]

Notes on the Minimum Income Standard for Britain

The study determined that an acceptable standard of living for pensioners is one in which people have the resources required to:

- Eat a nutritious diet;[235]
- Participate socially;[236]

[232] Rowntree (1901)
[233] See www.york.ac.uk/res/fbu/publications.htm for a list of budget standards from 1993
[234] JRF (2008) p. 4
[235] Age Concern (2005)
[236] JRF (2008)

- Accumulate further skills and participate in learning;[237]
- Maintain relationships with friends and family and afford *'the mutual obligations and costs associated with interaction and communication'*;[238]
- Take a one week self-catered holiday in the UK every year; and
- Have the occasional meal out.[239]

It is important to note that the above Minimum Income Standards assume that:[240]

- No household members are disabled;
- No household members have special health or dietary needs;
- Household members have their minimum transport needs met by public transportation;
- Personal computer and internet access is not essential for pensioner households; and that,
- Money to purchase cigarettes is not essential.

The Minimum Income Standards allow for:

- Households to have a landline and mobile phones (on a pay-as-you go basis) as these might be necessary for emergencies;
- Funds for prescription costs, dental and optical care - the Minimum Income Standard assumes that the NHS will cover general medical costs;
- Some provision for hiring taxis as these may be needed for emergency trips to hospital, trips home from the weekly shop or for travelling late at night; and,
- All budgets included a one-week holiday in the UK every year and amounts for celebrating Christmas, or an equivalent festival, and money to purchase birthday presents for friends and family.

The *'Minimum Income Standard for Britain'* study does not break down budget needs between people of different ethnicities, though there are differences in lifestyle between some ethnic groups which might translate into different income needs, for example because of different dietary requirements. However, the research group participants were ethnically diverse and therefore the Minimum Income Standard should in some way represent a general standard that could be suitable for most if not all individuals.[241] The research groups included people of all different income levels, and the Minimum Income Standard is intended to apply to all people in Britain and not just those used to living on a low income.[242]

[237] Age Concern (2008)
[238] Age Concern (2005) p. 40
[239] JRF (2008)
[240] JRF 2008
[241] JRF (2008) p. 16.
[242] JRF (2008)

Appendix 2:

The Costs of Disability

The costs of disability discussed in this paper (Chapter 2, Table 5 and Chapter 4) were calculated using percentages of mean income as costs of disability as detailed in previous research:[243]

Table A1:[244]

	Individual pensioner	Pensioner Couple with 1 disabled	Pensioner couple with both disabled
Weekly Income 2002	£124	£278	£281
Low severity disability	23% - £29	6% - £18	7% - £19
Medium severity disability	69% - £86	20% - £55	20% - £56
High severity disability	131% - £162	37% - £104	37% - £105

The 2008 costs used in this paper were derived by uprating the mean income of pensioners, and applying the percentages in Table A1:[245]

Table A2:[246]

	Individual pensioner	Pensioner Couple with 1 disabled	Pensioner couple with both disabled
Weekly Income 2008	199.13	419.8	419.8
Low severity disability	£46.57	£25.19	£28.39
Medium severity disability	£137.40	£83.96	£83.96
High severity disability	£260.86	£155.33	£155.33

[243] Zaidi and Burchardt's Comparing Incomes When Needs Differ: Equivalisation for the Extra Costs of Disability in the UK. (2005) p. 103.
[244] Zaidi & Burchardt (2005)
[245] 2008/09 RPI, DWP (2008b), Table A2
[246] 2008/09 RPI, DWP (2007)

The severity levels used were based on the Office of Population Censuses and Surveys (OPCS) severity scores of disability.[247] The scores used in these costs of disability are outlined in Table A3

Table A3:[248]

Disability level used in this paper	**OPCS Score**	**Examples of possible associated difficulties**
Low severity disability	3	• Difficulties with sight or comprehension
Medium severity disability	9	• Difficulties with mobility, comprehension and memory
High severity disability	17	• Difficulties with feeding self • Requires 24 hour care

[247] For more information on OPCS severity scores see Martin, Meltzer and Elliot (1988), pp. 13 - 15
[248] Zaidi & Burchardt (2005) p. 32

Appendix 3:

This appendix describes modelling assumptions used in this report. The modelling uses the PPI's Individual Model that was developed with a grant from the Nuffield Foundation.

Individual modelling

The modelling of the pension pot sizes of hypothetical individuals uses the PPI Individual Model.[249] Detailed assumptions have been made about the individuals' working and saving behaviours and these are described in the boxes below. Throughout, the modelling assumes:

- Future annual price inflation of 2.5%.
- Future annual earnings growth of 2% in excess of prices.
- Expected investment returns of 3.5% in excess of prices, before charges, corresponding to a mixed equity/bond fund.[250]
- Annual management charges of 0.5% of assets under management.

Hypothetical individuals and couples used in this report

This report uses four hypothetical individuals (Boxes A1 – A4) and four hypothetical couples (Boxes A5 – A8) to examine the way that different sets of assets and income could be used to fund different need sets in retirement. The basket of assets and income which each of the hypothetical individuals and couples have at SPA are intended to represent some of the possible variations within the range of assets and income baskets that people may have. They are not intended to be representative of the average pensioner. Their working life earnings are within the 20th, 30th, 50th and 90th percentiles of earnings.[251]

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

[250] This corresponds to assumed equity returns of 7.5% a year, assumed bond returns of 4.5% a year, and a portfolio of 55% equities and 45% bonds

[251] Labour Force Survey 2007 data

Box A1: Keisha: a 60 year-old low-earning woman

Keisha is a low-earning woman, aged 60 in 2008.

- Keisha starts working full-time from the age of 18 in 1966.
- Between the ages of 22 and 32 Keisha takes time out of work to care for her children during which time she qualifies for two years of Home Responsibilities Protection (HRP).[252]
- Keisha returns to work full time for thirteen years till she is 45, then she takes two years out of work to care for her mother (and qualifies for two more years of HRP) Keisha returns to work at 47 and works for another thirteen years.
- During her 30 years of full-time work Keisha earns at low age-specific earnings for women.

At SPA (60 in 2008):

- Keisha's BSP entitlement is £77.74
- Keisha's SERPS/S2P entitlement is £45.71
- Keisha has £1,000[253] of non-pension savings from which she receives an income of £0.96[254] a week.
- Keisha rents a council flat with a rent of £70 per week.[255]
- At age 70 Keisha receives £10,000 in inheritance

Box A2: Amit: a 65 year-old median-earning man

Amit is a median-earning man, aged 65 in 2008.

- Amit starts working full-time from age 21 in 1964.
- Amit works until he is 65 in 2008.
- During his 44 years of full-time work Amit earns at median age-specific earnings for a man.
- Between the ages of 30 and 65, Amit and his employer contribute to a DC occupational pension scheme 5% and 3% of salary respectively.

At SPA (65 in 2008):

- Amit's income from his occupational pension is £71.55 per week which does not increase with RPI (level annuity).
- Amit takes a lump sum of £18,388 at age 65.
- Amit's BSP entitlement is £90.70
- Amit's SERPS/S2P entitlement is £91.92 and Amit receives £4.34 per week from the Graduated Pension Scheme
- Amit has £6,000[256] of non- pension savings from which he receives an income of £5.77[257] per week
- Amit is an owner-occupier. His house is worth £200,000 in 2008.[258]

[252] HRP was introduced in 1978, 2 years before Keisha stopped providing care
[253] 25th percentile of savings for pensioners (rounded) calculated by PPI based on data from FRS (06/07) in DWP (2008a)
[254] Weekly income of 5% annual drawdown
[255] Council house rent info: www.communities.gov.uk/housing/housingresearch /housingstatistics/housingstatisticsby/rentslettings/
[256] 50th percentile of savings for pensioners (rounded) calculated by PPI based on data from FRS (06/07) in DWP (2008a)
[257] Weekly income of 5% annual drawdown

Box A3: Grace: a 60 year-old high-earning woman

Grace is a high-earning woman, aged 60 in 2008.

- Grace starts working full-time from age 25 in 1973.
- Grace works until she is 60 in 2008.
- During her 35 years of full-time work Grace earns at high earnings for a woman.
- Between the ages of 25 and 60 Grace contributes to an occupational pension scheme with a 1/80th accrual rate.

At SPA (60 in 2008):

- Grace's income from her occupational pension is £303.61 per week.[259]
- Grace's BSP entitlement is £88.37.
- Grace's SERPS/S2P entitlement is £139.29 and Grace receives £2.47 per week from the Graduated Pension Scheme.
- Grace has £21,000[260] of non-pension savings from which she receives an income of £20.19[261] per week.
- Grace is an owner-occupier whose house is valued at £250,000 in 2008.[262]

Box A4: William: a 65 year old man on disability benefits

William is a man on benefits for disability, aged 65 in 2008.

- William only works 8 years during his working-aged life, as a result of a disability.
- William spends the majority of his working-aged life on state benefits for incapacity.
- During his working-aged life William receives Incapacity Benefit of £84.50 with an age addition of £17.75 and Disability Living Allowance at the middle rate of £44.85.[263]
- William qualifies for National Insurance Credits as a result of his disability.

At SPA (65 in 2008):

- William ceases to receive Incapacity Benefit of £84.50 + £17.75.
- William receives Attendance Allowance at the lower rate of £44.85 (this replaces his DLA).
- William's BSP entitlement is £90.70.
- William's S2P entitlement is £4.38.
- William rents a council house in retirement at £70 per week.[264]

---

[258] House prices: www.communities.gov.uk/publications/corporate/statistics/hpi102008 CLG House price Index October 2008 - 'The mix-adjusted average house price in the UK stood at £203,539 in October 2008 (not seasonally adjusted).'
[259] Calculation made on the basis of Grace receiving entitlement 35 years of reckonable service that can count towards her DB civil service pension.
[260] 75th percentile of savings for pensioners (rounded) calculated by PPI based on data from FRS (06/07) in DWP (2008a)
[261] Weekly income of 5% annual drawdown
[262] House prices: www.communities.gov.uk/publications/corporate/statistics/hpi102008 CLG House price Index October 2008 - 'The mix-adjusted average house price in the UK stood at £203,539 in October 2008 (not seasonally adjusted).'
[263] William does not receive income support as he is above the applicable rate of £86.35 for a single adult with a disability

Box A5: The Chens - a median earning man and a high earning woman

- Mr Chen shares the earnings and pension history of Amit above.
- Mrs Chen shares the earnings and pension history of Grace above.
- Mr and Mrs Chen live together as owner occupiers of a house worth £250,000.[265]

Box A6: The Greens – a median earning man and a low earning woman

- Mr Green shares the earnings and pension history of Amit above.
- Mrs Green shares the earnings and pension history of Keisha above.
- Mrs Green elects to pay reduced Married Woman's NI contributions during her working life.
- Mr and Mrs Green live together as owner occupiers of a house worth £200,000.[266]

Box A7: The Smiths - a couple on disability benefits

- Mr and Mrs Smith both share the earnings and pension history of William above except substituting 60 for 65 for Mrs Smith's SPA.
- Mr and Mrs Smith live together in a council house with a rent of £75 per week.[267]

Box A8: The Khans – a man on disability benefits and a low earning woman

- Mr Khan shares the earnings and pension history of William above.
- Mrs Khan shares the earnings and pension history of Keisha above.
- Mr and Mrs Khan live together in a council house with a rent of £75 per week.[268]

264 Council house rent info: www.communities.gov.uk/housing/housingresearch /housingstatistics/housingstatisticsby/rentslettings/

265 House prices: www.communities.gov.uk/publications/corporate/statistics/hpi102008 CLG House price Index October 2008 - 'The mix-adjusted average house price in the UK stood at £203,539 in October 2008 (not seasonally adjusted).'

266 House prices: www.communities.gov.uk/publications/corporate/statistics/hpi102008 CLG House price Index October 2008 - 'The mix-adjusted average house price in the UK stood at £203,539 in October 2008 (not seasonally adjusted).'

267 Council house rent info: www.communities.gov.uk/housing/housingresearch /housingstatistics/housingstatisticsby/rentslettings/

268 Council house rent info: www.communities.gov.uk/housing/housingresearch /housingstatistics/housingstatisticsby/rentslettings/

Box A9: Life Course Scenarios

Baseline Scenario:
- Individual dies at age 82 (M), 85 (F) (median life expectancy)[269]

Longer Working Scenario:
- Individual dies at age 82 (M), 85 (F) (median life expectancy)
- works after SPA part time for 5 years[270]

Severe Disability Scenario:
- Individual dies at age 92 (M), 95 (F) (high life expectancy)
- Individual acquires a low severity disability at age 75 (M), 75 (F)[271]
- Individual acquires a severe disability at age 87 (M), 90 (F)[272]

Shorter Life Scenario:
- Individual dies at age 70 (M), 70 (F) (low life expectancy)
- Individual acquires a low severity disability at retirement 65 (M), 60 (F)

Box A10: Couple Life Course Scenarios

Couple Scenario 1:
- Individual scenario 1 + Individual scenario 1

Couple Scenario 2:
- Individual scenario 1 (M) + Individual scenario 3 (F)

Couple Scenario 3:
- Individual scenario 2 (F) + Individual scenario 4 (M)

In all scenarios it is assumed that:
- Basic State Pension payments increase in line with earnings after 2012 as outlined in the Pensions Act 2007.
- The hypothetical individuals and couples draw down 5% annually from their savings.
- The hypothetical individuals and couples take their 25% tax-free lump sum from their pension savings at SPA and use the income on an immediate purchase (such as mortgage payments, house improvements or give it away).[273]
- The hypothetical individuals and couples who own their own homes have fully paid off mortgages. They do not use their homes to release

[269] Median, high and low life expectancy calculated from the ONS interim Life Tables based on UK data from 2005 – 2007 based on a future life expectancy from current age: 60 for females, 65 for males.
[270] Estimated time of average spell of post SPA retirement estimated from data regarding length of work after retirement, DWP (2003), p. 15
[271] Based on data from Kellard *et. al.* (2006). 55% of people age 75 have a moderate or severe disability
[272] Based on data from Kellard *et. al.* (2006). Around 50% of people age 87 -90 have a severe disability
[273] The majority of people (76%) take their lump sum at SPA and of those who take their lump sum, many spend the money soon after taking it (80%) or give it away to friends or relatives (17%) Prudential. YouGov. (2008)

equity during their retirement (though in reality they may be required to release equity or sell their homes to fund residential care).

- The hypothetical individuals and couples claim all the benefits that they are entitled to, including Pension Credit, Housing Benefit, Council Tax Benefit and Attendance Allowance.[274]
- None of the individuals are entitled to receive the Severe Disability Premium of Pension Credit when they are disabled because they either receive care from their partner or from a relative.[275]

[274] Many pensioners do not claim all of the benefits that they are entitled to and have lower incomes as a result, Age Concern (2008)

[275] Pensioners who receive Attendance Allowance may be entitled to a Severe Disability Premium (of £50.35 in 2008/09) if they receive Attendance Allowance, live alone, or live with someone who is also receiving Attendance Allowance or is registered blind, and no one is receiving Carers Allowance for providing care to them, http://www.ageconcern.org.uk/AgeConcern/Documents/FS48Pension_Credit(1).pdf

Acknowledgements and Contact Details

The authors are grateful for input from many people in support of this paper, in particular:

Dean Blower
Niki Cleal
Chris Curry
Fay Goddard
Donald Hirsch
Helen McCarthy
Michael Pomery
Sally West
Asghar Zaidi

Editing decisions remained with the authors who take responsibility for any remaining errors or omissions.

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, grants and benefits-in-kind from a range of organisations, as well as being commissioned for research projects. To learn more about the PPI, see: www.pensionspolicyinstitute.org.uk

Contact:
Niki Cleal, Director
Telephone: 020 7848 3744
Email: info@pensionspolicyinstitute.org.uk

Pensions Policy Institute
King's College
26 Drury Lane
3rd Floor, Room 311
London WC2B 5RL

The PPI is grateful for the continuing support of its Platinum members:

AEGON Scottish Equitable
Barclays Global Investors
Hewitt
Prudential
The Pensions Regulator
Threadneedle Investments

A full list of supporting members is on the PPI's website.

References

Age Concern. (2002). *Issues facing Older Lesbians, Gay Men and Bisexuals.* Age Concern. www.spectrum-lgbt.org/downloads/OlderLGBT/AgeConcern_Issues_facing_older_LGB.pdf

Age Concern. (2005). *Minimum Income for Healthy Living: Pensioners*. Age Concern.

Age Concern. (2006). *Just Above the Bread Line. Living on a Low Income in Later Life*. Age Concern.

Age Concern. (2008). *Flagship or Flagging? The impact of pension credit five years on*. Age Concern.

Alliance Trust (2008). *Press Release: Faith in property as a pension has plummeted this year.* Alliance Trust www.alliancetrust.co.uk/press_releases/0083.htm

Department for Transport (DfT). National Statistics (ONS). (2006) *National Travel Survey 2005.* (DfT). (ONS).

Department for Work and Pensions (DWP). (2003). *Working after State Pension Age: Quantitative Analysis.* (DWP) HMSO.

Department for Work and Pensions (DWP). (2005). *Review of existing research on the extra costs of disability.* (DWP) HMSO.

Department for Work and Pensions (DWP). (2006a). *Which pensioners don't spend their income and why?* (DWP) HMSO.

Department for Work and Pensions (DWP). (2007). *The Pensioners' Income Series 2005-06.* (DWP) HMSO.

Department for Work and Pensions (DWP). (2008a). *Households Below Average Income. An analysis of the income distribution 1994/95 – 2006/07.* (DWP) HMSO

Department for Work and Pensions (DWP). (2008b). *The Pensioners' Income Series 2006-07.* (DWP) HMSO.

Department for Work and Pensions (DWP). (2008c). *Family Resources Survey. United Kingdom. 2006-07.* (DWP) HMSO.

Equality and Human Rights Commission (EHRC). Pensions Policy Institute. (PPI). (2008). *The under-pensioned: disabled people and people from ethnic minorities.* EHRC. PPI.

Gordon, D. Adelman, L. Ashworth, K. Bradshaw, J. Levitas, R. Middleton, S. Pantazis, C. Patsios, D. Payne, S. Townsend, P. and Williams, J. (2000). *Poverty and Social Exclusion in Britain.* York. Joseph Rowntree Foundation.

The Institute for Fiscal Studies (IFS). (2008). *Living in the 21st Century: Pensioners in England. The 2006 English Longitudinal Study of Ageing (Wave 3).* IFS.

Joseph Rowntree Foundation (JRF). (2000). *Poverty and social exclusion in Britain*. JRF.

Joseph Rowntree Foundation (JRF). (2006). *The Material Resources and Well-being of Pensioners*. JRF.

Joseph Rowntree Foundation (JRF). (2007a). *Measuring Resources in Later Life: a review of the data*. JRF.

Joseph Rowntree Foundation (JRF). (2007b). *Understanding Resources in Later Life: Views and Experiences of Pensioners*. JRF.

Joseph Rowntree Foundation (JRF). (2008). *A Minimum Income Standard for Britain: what people think*. JRF.

Kellard, K. Beckhelling, J, Phung, V. Middleton, S. Perren, K Hancock, R. (2006). *Needs and Resources in Later Life.* Centre for Research in Social Policy, Loughborough University. Department of Health and Human Services, University of Essex.

Kennelly, C. Age Concern. (2005). *Cultural and Generational Attitudes of Black and Minority Ethnic Communities to Pensions and Preferences for Financial Support in Later Life: a Review of the Literature.* Policy Unit. Age Concern.

Life Trust, centre for economics and business research (cebr). (2008). *Life Trust Cost of Retirement Report.* 2008. Life Trust.

Martin, J. Meltzer, H. Elliot, D. (1998). *The Prevalence of Disability among Adults.* London. HMSO
The Office for National Statistics (ONS). (2008a). *Family Spending: A report on the 2007 Expenditure and Food Survey.* ISBN 978-0-230-21989-2. Palgrave Macmillan.

The Office for National Statistics (ONS). (2008b). *Society: Civil Partnerships. Numbers almost halved in 2007.* ONS. www.statistics.gov.uk/cci/nugget.asp?id=1685

Pensions Commission. (2004). *Pensions: Challenges and Choices The First Report of the Pensions Commission*. Pensions Commission. TSO.

Pensions Policy Institute. (PPI). (2003). *The Under-Pensioned.* PPI.

Pensions Policy Institute. (PPI). (2004). *Property or Pensions?* PPI.

Pensions Policy Institute. (PPI). (2008a). *Pensions Facts.* PPI.

Pensions Policy Institute. (PPI). (2008b). *The Pensions Primer.* PPI.

Personal Social Services Research Unit. (PSSRU). (2008). *Unit Costs of Health and Social Care.* PSSRU. University of Kent.

Prudential. YouGov. (2008) *Press Release: Three quarters of pensioners with company and private pension schemes taking lump sums averaging £24,000.* Prudential.
www.pru.co.uk/content/acrobat/presscenter/11062008_lumpsums.pdf

Rowlingson, K. McKay, S. (2005). *Attitudes to inheritance in Britain*. July 2005/Findings/Informing Change. Joseph Rowntree Foundation.

Rowntree, S. (1901). *Poverty: a Study of Town Life.* Macmillan, London.

Standard Life. (2009). Press Release. *Retirement is dead: long live retirement.* Standard Life.
ukgroup.standardlife.com/content/news/new_articles/2009/retirement_is_dead.xml

UNISON (2007) *Pensions Briefing: Civil Partnership and Pensions.* UNISON

Zaidi, A. Burchardt, T. (2005). *Comparing Incomes When Needs Differ: Equivalisation for the Extra Costs of Disability in the UK.* Review of Income and Wealth. Series 51, Number 1, March 2005. SAGE.

Published by
PENSIONS POLICY INSTITUTE

www.pensionspolicyinstitute.org.uk
ISBN 978-1-906284-08-4