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**PRESS RELEASE**
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# "Paying for state pensions would be more difficult in an Independent Scotland, but not necessarily unaffordable" says Pensions Policy Institute

An Independent Scotland, keeping the same State Pension Age and state pension policy as the rest of the UK, could find it more difficult than the UK as a whole to afford state pension expenditure according to evidence submitted to the Scottish Parliament Finance Committee and published today by the Pensions Policy Institute.

The Pensions Act 2014 implements a new single-tier state pension from April 2016 that will replace the current Basic State Pension and the State Second Pension. The Act also contains a process for determining future increases to the State Pension Age.

The PPI evidence highlights significant differences in estimates of life expectancy within the UK. While for England, 2032 is the trigger year in which the SPA would need to increase to 68 to meet the criteria set out in the 2014 Pensions Act, the first year in which this would happen in Scotland is 2045.

However, despite lower life expectancy levels overall for Scotland, the population is ageing more quickly in Scotland than the rest of the UK, and increasing faster relative to the number of working age people.

This could make paying for state pensions more difficult in future in an Independent Scotland, with higher state pension expenditure being funded by a relatively smaller working age population.

The Scottish Government has also proposed a number of further state pension measures for Scotland, including a delay in increases to the State Pension Age compared to the rest of the UK, a potentially more generous single-tier pension than in the rest of the UK and retaining Savings Credit (which would be abolished for people reaching State Pension Age in the rest of the UK from April 2016 onwards). All of these would further increase state pension costs in Scotland.

Chris Curry, Director of the PPI, said "The increased state pension spending implied by the plans of the Scottish Government is not necessarily unaffordable. However, the Scottish Government would need to either raise higher revenues (for example through taxation), reduce spending in other areas (for example where demographic pressures are less), or have higher Government debt levels."

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**A summary of conclusions from the briefing follows on the next page.**

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The report can be downloaded from www.pensionspolicyinstitute.org.uk

**Notes for editors**

1. The Pensions Policy Institute (PPI) is an educational research charity, which provides non-political, independent comment and analysis on policy on pensions and retirement income provision in the UK. Its aim is to improve the information and understanding about pensions policy and retirement income provision through research and analysis, discussion and publication. The PPI does not make policy recommendations or lobby for any particular policy solutions. Further information on the PPI is available on our website www.pensionspolicyinstitute.org.uk.

2. The evidence will also be discussed later today (Wednesday 18 June) at a seminar organised by the David Hume Institute and the Institute of Chartered Accountants of Scotland (ICAS), considering '*The Implications of Scottish Independence for State Pensions in Scotland*.' The seminar will be held at the Royal Society of Edinburgh, on Wednesday (18 June) beginning at 6pm.

3. Following the main presentation, Chris Curry will be joined for a panel discussion by David Gordon, member of the Institute and Faculty of Actuaries' Scottish Board's Independence Working Party and a Consulting Actuary with Towers Watson, and David Davison, Director and owner of Spence & Partners. David Davison is also a member of the ICAS Pensions Committee.

4. The seminar will be chaired by Jeremy Peat, Visiting Professor University of Strathclyde International Public Policy Institute and former Director of the David Hume Institute.

5. Registration for the event can be made via the ICAS website: http://icas.org.uk/Events/ImplicationsofScottishIndependenceontheStatePension/

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# *The Implications of Scottish Independence for State Pensions in Scotland*

## Summary

On 18 September 2014 Scotland will hold a referendum as to whether Scotland should become independent from the rest of the UK. If there is a "Yes" vote and Scotland does become independent, there will be far reaching consequences. This Briefing examines the implications for Government spending on State Pensions, and the implications for pensioners in Scotland.

The Pensions Policy Institute (PPI) promotes the study of pensions and other provision for retirement and old age. The PPI is unique in the study of pensions, as it is independent (no political bias or vested interest); focused and expert in the field; and takes a long-term perspective across all elements of the pension system. The PPI exists to contribute facts, analysis and commentary to help all commentators and decision-makers to take informed policy decisions on pensions and retirement provision. The PPI does not make policy recommendations or lobby for any particular policy.

The Pensions Act 2014 implements a new single-tier state pension from April 2016 that will replace the current Basic State Pension (BSP) and the State Second Pension (S2P). It also makes proposals for future increases to the State Pension Age.

There are significant differences in estimates of life expectancy within the UK. While for England, 2032 is the trigger year in which the SPA would need to increase to 68 to avoid more than 33% of adult life being spent in retirement, the first year in which this would happen in Scotland is 2045.

There are also variations in life expectancies within each country**.** While the average life expectancy in Scotland may be lower than in other parts of the UK, there are parts of Scotland with better life expectancies than parts of the rest of the UK.

Despite lower life expectancy levels overall for Scotland, the population is ageing more quickly in Scotland than the rest of the UK. The old age dependency ratio is expected to increase more quickly in Scotland than in the UK as a whole.

A higher old age dependency ratio can indicate that a certain level of expenditure is less affordable, as there is potentially a smaller National Insurance and income tax base available to fund the expenditure.

An independent Scotland, keeping the same State Pension Age and state pension policy as the rest of the UK, may therefore find it more difficult than the UK as a whole to afford state pension expenditure.

This does not mean that it would be unaffordable. Rather the Scottish Government would need to either raise higher revenues (for example through taxation), reduce spending in other areas (for example where demographic pressures are less), or have higher Government debt levels.

State pension spending in the UK is projected to increase in the coming decades, allowing for the reforms in the Pensions Act 2014, which introduces a new single-tier state pension for individuals reaching SPA from April 2016 onwards.

Annual pensioner benefit expenditure per head of the working age population is currently higher in Scotland than it is in the UK, and is expected to increase further in the future. In 2014, pension benefit expenditure per working age individual is estimated to be £2,260 across the UK population, but £2,290 for Scotland (2014 earnings terms). The gap is set to increase between Scotland and the rest of the UK up until around 2045, after which the gap will reduce as differences between the dependency ratios narrows. In 2055, pension benefit expenditure per working age individual is estimated to be £3,230 across the UK population, and £3,330 for Scotland (2014 earnings terms).

The current Scottish Government:

- has stated that in an independent Scotland they would reserve judgement as to when the SPA in Scotland would increase from 66 to 67.
- proposed that it would retain the single-tier state pension as introduced by the Pensions Act 2014, set at a level of at least £160 per year (matching the figure for the rest of the UK if it is higher than £160 per week),
- committed to increase the level of the pension each year in line with the triple lock (that is, the higher of average earnings growth, CPI inflation or 2.5%).
- would allow those expecting a pension based on their spouses contributions to still do so for people reaching state pension age in the 15 years after implementation.
- would retain the Savings Credit element of Pension Credit.

Each of these policy proposals would impact on the level of expenditure on pensioner benefits in Scotland if they were to be introduced.

The overall impact of the Scottish Government policy proposals on annual pensioner benefit expenditure would be to further increase expenditure per working age individual in Scotland. By 2055, compared to pension benefit expenditure per working age individual estimated at £3,230 across the UK population, pension benefit expenditure per working age individual in Scotland is estimated to be £3,400 allowing for the Scottish Government policy proposals (2014 earnings terms).

After allowing for expected changes in earnings, and focussing on the difference between Scotland under the Scottish Government proposals and the UK as a whole, the difference peaks at £330 per individual of working age in 2032, where

Scotland would still have a lower SPA than the rest of the UK. £180 of this is due to the policy changes, with the remainder due to underlying demographic differences.

Although the proposals put forward by the Scottish Government would increase expenditure on pensioner benefits, if implemented they could also lead to higher state pension incomes for pensioners in Scotland compared to the rest of the UK, depending on the final level of the single-tier pension on introduction in 2016 and the rate at which it is increased.

A median earning man aged 44 in 2014 and reaching State Pension Age (67) in 2037, who is automatically enrolled into a workplace pension at the minimum contribution level from October 2012, could have income from state and private pensions over £1 a week higher under the Scottish Government proposals than in the current UK system (in 2014 earnings terms).

The difference in outcomes could be greater for lower income individuals. For example, a low earning woman with career breaks, aged 44 in 2014 and reaching SPA at 67 in 2037, who is automatically enrolled in a workplace pension at the minimum contribution level when she is in work, could have an income from state and private pensions £14 a week higher under the Scottish Government proposals than in the current UK system (in 2014 earnings terms).

The majority of this increase in income is due to the availability of Savings Credit, as this particular individual has a low level of private pension income as a result of having relatively low earnings and spending time caring rather than in paid employment.

However, the relative generosity of Savings Credit means that the median earning man could be entitled to Savings Credit less than 5 years after reaching State Pension Age. This would increase his state and private pension income further under the Scottish Government proposals, compared to in the current UK system.

Although Savings Credit leads to a higher income in retirement, it can also reduce the relative value of remaining automatically enrolled in a workplace pension scheme. If the median earning man opted-out of his workplace pension as a result of being able to claim Savings Credit in retirement, his income from state and private pensions would be significantly lower (although his disposable income when working would be higher). However, he would receive £15 a week (2014 earnings terms) of Savings Credit per week under the Scottish Government proposals.

The old age dependency ratio, and therefore estimates of pensioner benefit expenditure per individual of working age, is sensitive to a number of assumptions, such as life expectancy, birth rates and in particular migration assumptions. In the ONS high migration population scenario the assumed increase in the number of people in working age in Scotland means that from 2040 onwards expenditure per individual of working age is lower in Scotland, even with the Scottish Government policy proposals, than in the UK under current UK Government policy.

This written evidence has been submitted and published by:
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