PENSIONS POLICY INSTITUTE

PPI

Case studies for Scottish Widows Executive Summary

Summary of conclusions

Scottish Widows has commissioned the Pensions Policy Institute to produce a series of case studies illustrating the potential outcomes of the state pension reforms in the White Paper ***Security in retirement: towards a new pension system*** on different illustrative individuals.

A median-earning man could receive £74 a week (in 2006/7 earnings terms) from a Personal Account at state pension age (68), if he stays opted in from age 22 until retiring three years before state pension age at age 65. This would be on top of a state pension of around £137 a week.

- Working longer, until the new state pension age of 68, could increase his weekly Personal Account income from £74 to £98.
- Opting out of Personal Accounts until age 28 could reduce his weekly Personal Account income from £74 to £66.
- Increasing his contributions to 5.8% of salary, the latest Scottish Widows Average Savings Ratio, could increase his weekly Personal Account income from £74 to £96.

A median-earning woman could receive £51 a week from a Personal Account at state pension age (68), if she stays opted in from age 22 to her retirement at age 65. This is less than the £74 the median-earning man could receive because of her lower earnings and higher life expectancy. This would be on top of a state pension of around £136 a week.

- Taking career breaks for childcare and eldercare and working part-time for 5 years could reduce her weekly Personal Account income from £51 to £30. Her weekly state pension could be reduced from £136 to £128.
- If, in addition to the career breaks and part-time work, she was a low earner, her weekly Personal Account income could be reduced to £22.
- If, in addition to the career breaks and part-time work, she retired at age 60, but still earned median earnings, then her weekly Personal Account income could be reduced to £18.

A lifetime self-employed person would not receive employer contributions to Personal Accounts and would not be entitled to State Second Pension. If he earned at median earnings and contributed the equivalent of the employee contribution to Personal Accounts from age 22 until retiring at age 65, then he could receive £46 from a Personal Account and £76 from Basic State Pension, at state pension age (68). He could be eligible for Pension Credit unless his business is worth £37,000 or more.

- Opting-in twenty years later could reduce his weekly Personal Account income from £46 to £24.
- Doubling his contributions could double his weekly Personal Account income from £46 to around £93.
- If he worked until age 70, while still contributing to a Personal Account, then he could receive £68 a week from his Personal Account at age 70. If he deferred his Basic State Pension to age 70, then it could be increased from £76 to around £92.

For all of the individuals, income would decrease in retirement, relative to average earnings. This is because, although Basic State Pension would be indexed to average earnings, income from State Second Pension would increase with prices in retirement. Further, a level annuity is assumed to be chosen for Personal Accounts so that payments are fixed in cash terms during retirement.

For example, the median-earning man's weekly income from his Personal Account could reduce from £74 to £48 between the ages of 68 and 78, and his weekly state pension could reduce from £137 to £126 over the same period.

Outcomes from state pensions and Personal Accounts will depend on many factors, including work histories and age. All of the individuals illustrated are aged 22 when the reforms are assumed to be introduced in 2012 and many have relatively full work histories. Income from state pensions and Personal Accounts is likely to be lower for people with broken work histories. Today's older people are likely to receive less from Personal Accounts because there are fewer years in which they can contribute.