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ASPECTS OF THE ECONOMICS OF AN AGEING POPULATION

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NOTE: References in the text of the Report are as follows:

(Q) refers to a question in oral evidence.
(p) refers to a page of written evidence.

FOURTH REPORT

5 NOVEMBER 2003

By the Select Committee on Economic Affairs

ORDERED TO REPORT

ASPECTS OF THE ECONOMICS OF AN AGEING POPULATION

SUMMARY

The population of the United Kingdom is ageing. In 2001, for the first time in the United Kingdom, there were more people aged over 60 than under 16. By 2051, an estimated one in four people will be aged over 65. Much debate on the ageing population has focused on the challenges it presents. We believe that, just as society has adjusted to accommodate the demographic changes that have been experienced so far, so too will it adjust to accommodate the challenges of the future.

Inevitably, given our remit[1], our inquiry focused on economic aspects, although we recognise and appreciate social and cultural factors such as attitudes towards older people and their needs and preferences.

Having explained the scope and focus of our inquiry in chapter 1, in chapters 2 and 3 we briefly set out the demographic and macroeconomic context. We identify the causes of population ageing, and note that its economic impact is likely to be greater in other developed economies than in the United Kingdom.

Chapters 4 to 6 cover employment, in relation to participation (chapter 4); productivity (chapter 5); and age discrimination (chapter 6). We emphasise the importance of increasing the labour force participation of older workers. We note that average age-specific participation rates mask much lower rates in some regions and among some ethnic minorities and women. We also discuss the relative importance of supply-side and demand-side factors in the economic activity of older people.

Supply-side and demand-side factors are further assessed in chapters 5 and 6, which discuss how older people's capacity for work, and employer perceptions of that capacity, affect employment opportunities for older workers. We recommend job and workplace redesign and the promotion of skill acquisition in order to enhance older people's work capacity, and we note the dearth of reliable evidence on the relationship between age and individual productivity. We advocate comprehensive legislative and cultural initiatives to ensure the elimination of age discrimination in both the public and private sectors.

Chapter 7 considers some of the consumption issues that arise in relation to older people. We draw attention to cases of market failure in the design, provision and marketing of goods and services, and to restrictions on access to providers of goods and services.

Chapters 8, 9 and 10 deal with retirement income. Chapter 8 draws attention to the changing social structure and the particular problems faced by women, who constitute the majority of pensioners, and ethnic minorities in making adequate pension provision. We conclude that the contributory system should be replaced by a pension paid on the basis of citizenship entitlement.

Chapter 9 assesses the opportunities available for making private provision for retirement, and the context in which such provision is made. We note the factors involved in decisions relating to making private provision, and conclude that, despite inadequate voluntary private pension saving, further compulsion in addition to that which is already in place under the national insurance system is not inevitable.

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[1] "to consider economic affairs"

Chapter 10 deals with the excessive complexity of the public pension system and the implications of that complexity. We note the effects of means testing, which include high marginal tax rates and reduced incentives to save. Finally we assess whether, and in what respects, the United Kingdom faces a pensions crisis, and we recommend the establishment of an independent authority to provide more stability and certainty in the design and implementation of appropriate pensions policies.

CHAPTER 1: SCOPE OF THE INQUIRY

1.1. One of the greatest achievements of the past 150 years has been the increase in average length of life. In the middle of the nineteenth century, average life expectancy at birth in England was just 42 years, by 1911 it was over 50 years, and today it is over 75 years for men and 80 years for women.[2] Not only do we live much longer lives than our forebears, but we also live healthier lives, and today the majority of people aged over 65 are healthy, fit and active.

1.2. This remarkable improvement in the life chances of British citizens is one of the most obvious benefits of the economic growth and scientific progress of the past two centuries. Our society has adjusted readily and enthusiastically to the new opportunities and challenges offered by longer and healthier lives, and it seems reasonable to believe that we will continue to adjust successfully to future increases in life expectancy which will occur in the 21st century.

1.3. Our society has also adjusted to a fall in average family size, as women have chosen to have fewer children. Women born in the mid-1930s had, on average 2.45 children, but those born in the mid-1950s had on average 2.03 children, and for women born in the mid-1970s it is expected that average family size will fall to around 1.74 children.[3]

1.4. This fall over time in fertility, together with the simultaneous improvement in mortality, has reduced the relative size of the child population, and increased the relative size of the pensioner population. This upward shift in the age structure of society is what is meant by the term "ageing population". The ageing of the population has enormous economic implications; indeed, it has the potential to have an impact on all sectors of the economy and all aspects of economic activity.

1.5. We recognised at the outset that it would be essential to focus our inquiry, and a strategic decision was taken not to examine the issues of long-term care and health, which have recently been the subject of investigation by the Royal Commission on Long-Term Care and the Wanless Report.[4] We decided to concentrate on the issues of employment and income, in particular in relation to length of working life and the position of women, and to focus on the fundamental principles involved. In our consideration of income in retirement we have chosen not to examine in detail the operation of the current pension system, which is an issue that has recently been reported on by the House of Commons Work and Pensions Committee.[5] Instead we have directed our attention to the general principles and structure of the UK pension regime.

1.6. The inquiry was formally launched in December 2002 with the issue of the call for evidence reproduced in Appendix 4. We received written evidence from a wide range of sources, which are listed in Appendix 3. The written evidence was complemented by oral evidence received at 21 public hearings between February and October 2003. The oral and written evidence is published in volume II. We are extremely grateful to all those who provided us with evidence.

1.7. Our Specialist Adviser was Professor Paul Johnson, AcSS, Professor of Economic History at the London School of Economics and Political Science. He contributed to all aspects of the inquiry and the final report. We are especially grateful for his assistance in eliciting and evaluating our evidence.

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[2] Government Actuary's Department, *National Population Projections, 2000-based* (TSO, 2002), p 22

[3] GAD, *National Population Projections, 2000-based*, p 18

[4] Royal Commission on Long-Term Care, *With Respect to Old Age* (1999) (CM-4192-I); Derek Wanless, *Securing Our Future Health: Taking a Long-Term View* (2002)

[5] Work and Pensions Committee, 3rd Report (2002-03): *The Future of UK Pensions*, (HC 92-I)

CHAPTER 2: DEMOGRAPHIC CONTEXT

Introduction

2.1. The ageing of the population is not a new phenomenon. At the beginning of the 20th century barely one in 20 Britons was aged over 65, compared to more than three out of every 20 today. Although population ageing is likely to be slightly faster over the next 50 years, with five out of 20 people aged over 65 by 2051, we should recognise that this represents the continuation of a long-run trend rather than an abrupt break with the past. Our society and economy have adjusted readily to both the opportunities and the challenges offered by the ageing of the population over the past century, and there is little reason to believe that adjustment will be less readily achieved in the future.

2.2. This chapter outlines the basic demographic data that defines the pattern of past and future ageing of the United Kingdom population. Comparisons are drawn with ageing in other developed economies, and consideration is given to the reliability of the underlying demographic estimates.

The causes of population ageing

2.3. The ageing of the population is a process common to almost all developed and most developing countries. An increase in the average age of the population is driven by two separate forces:

- a reduction in age-specific mortality (longer lives)
- a reduction in the fertility rate (fewer births)

2.4. In the United Kingdom, life expectancy has risen dramatically over the past 160 years, driven in turn by better sanitation, medical developments, lower infant mortality, and, over the past three generations, by increased longevity.[6] The increase over the past eight decades in average life expectancy for a person aged 65 is illustrated in Table 1. Similar increases in life expectancy have been experienced in other developed countries.[7]

Table 1: Life expectancy at age 65[8]

	Men	Women
1928	11.5	13.3
1960	12.1	15.3
2002	16.0	19.0

2.5. Fertility rates in the United Kingdom have been falling for the past 40 years, and are now at an all time low. Demographers estimate that a total fertility rate of 2.08 births per woman of child-bearing age is required to maintain the population in the long run at its current size. The fertility rate in the United Kingdom has been below replacement level since the early 1970s, and long-run projections assume that it will level off at 1.74.[9] If this fertility rate is maintained, and if there is no net immigration, in the long run the population of the United Kingdom will decline. However, fertility has been falling faster in many other countries; the total fertility rate across all European countries averages only 1.4.[10]

2.6. The outcome of these mortality and fertility trends is a population in the United Kingdom that has aged significantly over the past 40 years, and that is projected to age further over the next half-century. The 2001 census showed that for the first time there were more people in the United Kingdom aged over 60 than under 16.[11] However, many other developed economies have experienced and will continue to experience a more rapid rate of population ageing.

[6] International Longevity Centre , volume II, p 449

[7] Department for Work and Pension, volume II, p 1

[8] Ibid

[9] GAD, *National Population Projections, 2000-based*, p 18

[10] PAPRI, volume II, p 464

[11] International Longevity Centre , volume II, p 449

2.7. Data reported in Box 1 set the past and projected future course of ageing in the United Kingdom in a comparative context. In 1960, the United Kingdom had the highest proportion of people over 65 among the G7 group of leading industrial economies, but by 2000 Italy, Japan, Germany and France all had a larger share of persons over 65 than the United Kingdom. Over the next 50 years, ageing in the United Kingdom is expected to be slower than in any other major European Union country, and slower also than in Australia, Canada and Japan. Thus, in so far as population ageing may have any direct impact – positive or negative – on economic activity or performance, this impact is likely to be less pronounced in the United Kingdom than in most other developed economies.

Box 1

Past and future trends in population ageing

A number of different indicators can be used to trace the pattern of population ageing. One simple indicator is the proportion of the population aged over 65. Table 2 shows that, by this measure, the United Kingdom has aged more slowly than most other major industrial nations. In 1960, the United Kingdom had the oldest age structure among the G7 countries, but by 2000 it had relinquished this position to Italy, and had been overtaken by Japan, France and Germany. However, this measure takes no account of changes in the relative size of other age groups.

Table 2: Population age structure in G7 countries, 1960-2000[12]

	Population 65 or older(%)	
	1960	2000
Italy	9.0	17.7
Japan	5.7	17.3
Germany	10.8	17.2
France	11.6	16.1
United Kingdom	**11.7**	**15.6**
US	9.2	12.6
Canada	7.6	12.5

A more informative, and widely used, indicator is the old-age dependency ratio, which represents the population aged 65+ as a percentage of those aged 16-64. Table 3 shows that, by this measure, the United Kingdom is expected to age more slowly over the next 50 years than other major economies, with the exception of the USA.

Table 3: Old-age dependency ratios in G7 countries, 2000-2050[13]

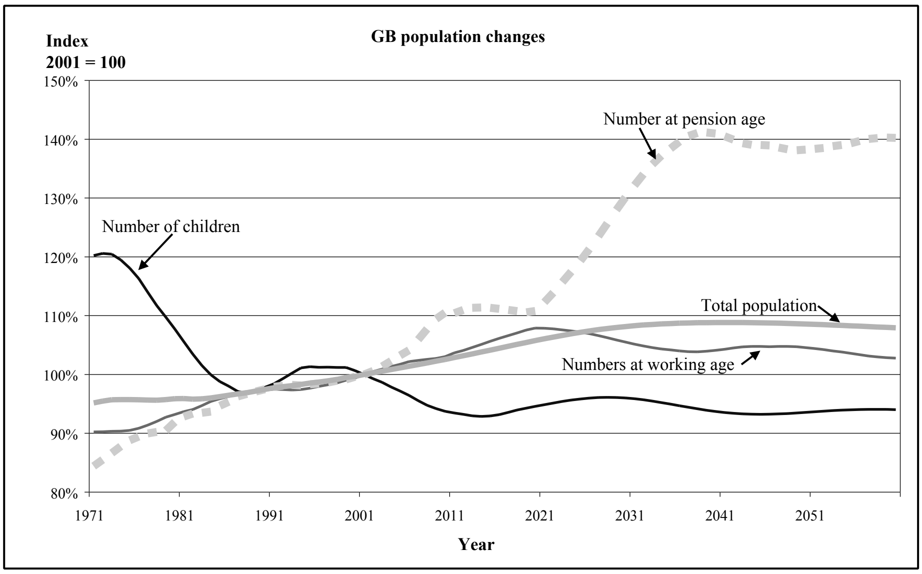
	2000	2025	2050
Italy	26.7	40.6	68.1
Japan	25.2	49.0	71.3
Germany	24.1	39.0	54.7
France	24.5	36.2	46.7
United Kingdom	**24.4**	**32.8**	**39.2**
Weighted average of EU member states	24.5	37.1	54.7
United States	18.6	29.3	34.9
Canada	18.5	32.6	40.9

It should be noted, however, that the old-age dependency ratio does not accurately represent trends in economic dependency, for two reasons. First, it excludes the child (0-15) population, which is also economically dependent. Since low fertility rates are leading to a decline in the proportion of children in the population which coincides with the increase in the size of the older population, the total dependency ratio (the population aged 0-15 and 65+ as a percentage of those aged 16-64) is projected to remain stable at about 37.5 over the period 2001-2025, before rising to 40.9 by 2040. Secondly, age ratios of this type take no account of actual economic activity. Many people aged 15-64 are not economically active because of education, caring responsibilities, disability or early retirement. Conversely, some persons above retirement age continue to be active in the labour market.

[12] Trades Union Congress, volume II, p. 112.. Data taken from OECD sources

[13] DWP, volume II, p 2. Data taken from UN and GAD sources

Table 4: Population changes in Great Britain, 1971-2051[14]



Composition of the ageing population

2.8. Population ageing alters the relative proportions of the child, working age and pensioner age groups, and also affects the age distribution within these groups. Thus the general process of population ageing will have an impact on people of all ages, and not just on older people. Within the working-age population, for example, between 2000 and 2025 the number of people aged 30-39 is projected to decline from 9.5 to 8.7 million, while the number aged 50-59 is projected to increase from 7.3 to 8.6 million. [15]

2.9. It should be recognised that changes in mortality and fertility have a long-run impact on the overall age structure of the population. A short-run increase in fertility, such as happened with the post-war “baby-boom” in the late 1940s, will affect the age structure of the total population over the succeeding century as each birth cohort ages. Because of the very long time period required for a population to reach a stable equilibrium following any change in fertility or mortality, a “snapshot” view of the population at a single point (such as that provided by the census) needs to be set in the context of longer-run trends.

2.10. One notable trend is past and projected ageing within the pensioner population. In 1971, persons aged 65+ comprised 13.2 per cent of the total UK population, and persons aged 80+ comprised 2.3 per cent of this total. By 2000, the 65+ population had grown to 15.6 per cent of the total, but the 80+ population had almost doubled its proportionate share to 4.0 per cent. Over the 50 years to 2050, the Government Actuary’s Department projects that the 65+ age group will have expanded to 24.4 per cent of the total UK population, but that the 80+ age group will have more than doubled to reach 9.1 per cent of this total.[16]

2.11. Because of the better survival chances at older ages of women relative to men (see table 1 above), the sex ratio changes with age. The 2001 UK census shows that, while the ratio of women to men in their late 60s is 1.07, this rises to 1.29 in their 70s, 1.91 for people in their 80s, and 3.46 for those in their 90s. As the Women’s Budget Group has noted, ageing in the United Kingdom, as elsewhere, is a “progressively gendered experience”.[17]

[14] Actuarial Profession , volume II, p 339

[15] GAD, *National Population Projections, 2000-based*, p 56

[16] GAD, *National Population Projections, 2000-based*, p 2

[17] Women’s Budget Group/Fawcett Society, volume II, p 131

2.12. These age-specific sex ratios have important implications for the living arrangements of older people. Nearly three quarters of men aged 65+ are married, and nearly half of men aged 85+ are married. By comparison, only 42 per cent of women aged 65+, and 10 per cent of women aged 85+ are married. In consequence, women aged 65+ are almost twice as likely to be living alone as are men of the same age.[18]

2.13. Most minority ethnic groups currently display an age profile which is younger than that of the white population, but these groups are likely to experience particularly rapid ageing in coming decades. In the late 1990s, 6 per cent of the black and minority ethnic population of the United Kingdom was aged 60+, compared with 21 per cent of the white population.[19]

2.14. The timing of immigration is a major determinant of the age composition of different minority ethnic groups. The large-scale immigration of young adults from the Caribbean in the early 1960s has led to the black Caribbean group being the first to experience significant numbers reaching retirement age. High rates of immigration from the Indian sub-continent in the early 1970s will in turn lead to significant increases in the number of Indian, Pakistani and Bangladeshi elders over the next two decades.[20]

The future impact of immigration on population ageing

2.15. The difference between the age profiles of the white population and of the various black and minority ethnic populations indicates that past immigration has had some effect on the overall age structure of the United Kingdom. In an increasingly integrated global economy, immigration into the United Kingdom appears to be viewed as an attractive option by many aspirant migrants. Net migration to the United Kingdom of non-British citizens has risen by over 100,000 persons per year since the early 1990s, with the greatest proportionate increase being persons coming from other countries in the European Economic Area.[21] Since most immigrants are young adults, future immigration will tend to increase the size of the working-age population, and thus could reduce the rate at which the old-age dependency ratio rises. The Confederation of British Industry (CBI) is of the clear opinion that immigration of workers at both the low-skill and high-skill ends of the labour market helps ease the current skill shortage, has no perceptible impact on the wages of the indigenous workforce, and helps to sustain economic growth (Q599).

2.16. Professor David Blake (Director of the Pensions Institute, Birkbeck College, University of London) provided us with an analysis of the potential impact of future immigration on the worker-pensioner ratio. He demonstrated (QQ 190-191) that estimates of the number of immigrants required to stabilise the ratio of the economy-wide wage bill to the economy-wide pensions bill are highly sensitive to assumptions about future growth rates of real wages and pensions, but that an annual level of net immigration of around half a million people might be necessary once the baby-boom generation enters retirement from around 2010. This may be compared with average net immigration of under 100,000 per annum from the mid 1980s to the mid 1990s, of just under 200,000 persons in both 2000-01 and 2001-02, and projections of 135,000 per annum for the future.[22]

2.17. **We conclude that, although net immigration will tend, in the short run, to increase the relative proportion of younger persons within the population, it is neither appropriate nor feasible to attempt to counter the trend towards a more aged society in the United Kingdom through a manipulation of immigration policy.**

The reliability of population projections

2.18. Assessment of the future scale and pace of population ageing in the United Kingdom depends critically on assumptions made about trends in fertility, mortality and immigration. The Government Actuary's Department uses different assumptions to produce a range of projections around a central estimate. For fertility, high and low variant projections assume that the fertility rate will rise to 1.94 or fall to 1.54 by 2012. Any such changes in fertility would have the effect of either reducing or increasing the rate of ageing of the United Kingdom population, but they cannot alter the number of older persons alive at mid-century, since all such persons have already been born. The absolute size of this older population, therefore, depends solely on future mortality trends. Estimates of life expectancy produced by the Government Actuary's Department assume that mortality improvements beyond age

[18] WBG/Fawcett Society, volume II, p 131

[19] Policy Research Institute on Ageing and Ethnicity, volume II, p 197

[20] Commission for Racial Equality, volume II, p 193

[21] GAD, *National Population Projections, 2000-based*, p 33

[22] GAD, *National Population Projections, 2000-based*, p 31

65, which have been significant over the course of the 20th century (see table 1 above) will tail off by the middle of the 21st century. The "principal" estimates (as used, for example, in the 2002 Green Paper on pensions, *Simplicity, security and choice*) assume that life expectancy at 65 for men will rise by 2.3 years over the period 2002 to 2025, but by only 0.7 years between 2025 and 2050. The corresponding figures for women show a rise of 2.1 years from 2002 to 2025, and 0.6 years from 2025 to 2050.[23]

2.19. The Government Actuary's Department explained that mortality rates are currently improving fastest at older ages up to the mid-80s, especially for men. This is believed to be a consequence, to some degree, of past trends in smoking behaviour, and it is unlikely that future improvements can be sustained at these high levels indefinitely. For this reason it is assumed that improvements in mortality rates will tail off from about 2025. However, variant projections are produced by the Government Actuary's Department on assumptions of both higher and lower life expectancies at birth than the principal projection, and both the projection methodology and the projections themselves are periodically reviewed.[24]

2.20. Witnesses from the Actuarial Profession noted that there is a wide difference of opinion, not only among actuaries but also among demographers, about the likely future development of mortality rates (Q939). Baroness Greengross noted that there is dispute among academic analysts as to whether there is a genetic limit to the length of human life (Q100). It is possible, for example, that a breakthrough in the treatment of one of the main degenerative diseases could have a marked effect on mortality rates. Such a breakthrough could significantly improve mortality rates at older ages, and thus could raise life expectancy at age 65.

2.21. Given the pace of scientific advance in human genetics, we think that significant improvements in mortality rates at older ages are likely to be achieved within the next two decades. Baroness Greengross pointed out that projections of the size of the older population made as recently as 1991 have had to be revised in the light of recent data on the rising life expectancy of older people.[25] We thus view the Government Actuary's assumptions about future trends in life expectancy at age 65 as conservative and unduly pessimistic.

2.22. We recognise that a degree of uncertainty necessarily surrounds population projections, and we believe that due acknowledgement should be made of this uncertainty in any use the Government make of these projections in, for example, forecasting future pension costs.

2.23. We note that an example of good practice in presenting variant projections of future outcomes exists in the inflation projections made by the Bank of England. The central projection is now reported, as a matter of course, in conjunction with high and low variant projections, and the "funnel of doubt" around the principal projection is displayed graphically in a fan chart.

2.24. **We recommend that the Government should, when publishing long-range population projections, or pension or other expenditure projections which incorporate population projections, always report the "funnel of doubt" created by the variance between high and low assumptions about mortality and other key demographic variables.**

[23] GAD, *National Population Projections, 2000-based*, pp 40-50

[24] GAD, volume II, p 443

[25] Baroness Greengross, volume II, p 27

CHAPTER 3: MACROECONOMIC CONTEXT

Introduction

3.1. Population ageing can directly affect macroeconomic performance through both the labour and capital markets. It can also indirectly affect macroeconomic performance via its impact on public expenditure. The extent of potential interaction between demographic structure and the economy is vast, and this chapter does not attempt to examine all possible influences of demography on the macro economy. Attention is here confined to the specific question of whether the ageing of the UK population will have a significant negative impact on the long-term growth potential of the economy via its effect on macroeconomic aggregates, particularly on labour supply and on the rates of saving and capital accumulation. The microeconomic impact of ageing on individual worker productivity is discussed separately in chapter 5, and the potential impact of ageing on public pension expenditure is considered in chapter 10.

Ageing and aggregate labour productivity

3.2. Population ageing will reduce the rate of growth (and ultimately the absolute size) of the working-age population. If age-specific labour force participation rates remain at their current levels (an issue discussed further in chapter 4 below), the ratio of inactive to employed people will rise. Labour productivity will therefore have to increase to maintain the level of Gross Domestic Product (GDP) per person.[26]

3.3. Because the United Kingdom experienced "baby booms" in the late 1940s and in the 1960s, the impact of ageing on aggregate labour supply is "lumpy" rather than linear; as the large baby-boom cohorts move from middle age to retirement, they are likely to have a big impact on the relative size of worker and pensioner populations. The Treasury estimates that employment growth will contribute 0.25 per cent per annum to growth of GDP in the decade 2011-20, but will account for -0.25 per cent of GDP growth in 2021-30, followed by zero impact over the two decades 2031-50.[27]

3.4. This physical impact on GDP growth of changes in the number of workers needs to be set in the context of expected future increases in labour productivity. Analysis of the impact on the UK economy of demographic ageing by the Bank of England makes the assumption that labour productivity will grow in the long run by a constant 1.75 per cent per annum, with 30-44 year olds consistently exhibiting 40 per cent greater productivity than younger and older workers (although, as noted in chapter 5 below, empirical evidence on the relationship between age and productivity is inconclusive). This productivity growth dominates the stagnation in the size of the future workforce, producing a more than doubling of "effective" labour supply in the period 2001-51.[28] An additional (and cautious) assumption of a growth in capital stock by 10 per cent per decade results in a projection that income per capita will more than double in real terms over the next half-century.

3.5. Estimates of this sort are subject to a degree of error. It was noted by Professor Richard Disney (Professor of Economics, University of Nottingham) that labour economists do not know how ageing will affect productivity (Q802); this issue is discussed further in chapter 5 below. However, projections of long-run productivity growth are based on assumptions that future improvements in the quality of human and physical capital will be broadly distributed throughout the economy, and will produce economic returns consistent with long-run historical experience. Even if assumptions about the *level* of age-specific productivity prove to be incorrect, such errors will have only a small impact on future income as long as similar rates of productivity *growth* are achieved by workers of all ages.

3.6. Population ageing over the next 50 years is likely to have a small negative impact on the growth of income per capita, primarily by reducing the size of the workforce relative to that of the inactive population. Any action that can be taken to increase age-specific participation rates would diminish this negative economic impact (we discuss such possibilities in chapters 4, 5 and 6 below). However, the expectation of continued labour productivity growth in the long run, together with continued capital accumulation, is likely to ensure that real income per capita grows, most probably doubling its 2002 level by the middle of the 21st century. For those entering the labour force today and retiring in the middle of the century, GDP at present growth rates will be 2 to 2.5 times what it is now.

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[26] DWP, volume II, p 3

[27] HM Treasury, *Long-term public finance report: an analysis of fiscal sustainability*, November 2002, cited by DWP, volume II, p 3

[28] Garry Young, *The implications of an ageing population for the UK economy*, Bank of England Working Paper 159, July 2002, p 13

3.7. **We conclude that population ageing does not pose a threat to the continued prosperity and growth of the United Kingdom economy; in this sense, therefore, there is no looming "crisis" of population ageing in the United Kingdom.**

3.8. **This does not mean that the future growth of the economy is in any sense guaranteed; that depends on how we manage our economic resources. A failure, for example, to sustain historic rates of technological progress and productivity growth might drastically reduce future growth rates below those projected here. We conclude, however, that such risks exist independently of any demographic pressures on the economy.**

Ageing, inflation, saving and capital accumulation

3.9. As well as affecting the size of the working population, ageing will also increase the proportion of the population that is retired, if current age-specific participation rates are maintained. This could have important economic effects on inflation, saving and capital accumulation. Evidence on these issues was presented by Professor Philip Booth (Professor of Insurance and Risk Management, City University Business School), who had previously undertaken a study of the economic impact of demographic changes for the Foresight Ageing Population Panel of the Department of Trade and Industry in 2000. Note was also taken of the Bank of England's assessment of these issues.

3.10. In theory an increase in the proportion of the population of non-working age will increase demand for goods and services relative to the ability of the working population to supply such goods and services, thus leading to inflationary pressures. However, such pressures for a relative increase in the supply of consumption goods are likely to be met by a reduction in the demand for capital goods, together with a liquidation of overseas assets accumulated by retirees during their working life. Professor Booth concludes that "there may be changes in the equilibrium level of interest rates and exchange rates necessary to contain inflation and such changes may mean that the management of monetary policy is more complex. However, there is no reason to believe that there will be an increase in inflation."[29]

3.11. An increase in the relative size of the retired population could affect rates of saving, interest, and capital accumulation. The Bank of England has noted that this represents a key area of uncertainty for two separate reasons: it is unclear how the savings behaviour of older people in the future will develop; and domestic savings may not be the primary determinant of domestic investment in a competitive international capital market.[30]

3.12. Uncertainty about future savings behaviour is likely to be minimised if individuals feel that they can save with confidence. In general, conditions of low and stable inflation will produce a consistent relationship between real and nominal interest rates, which will be conducive to savings. The Government's commitment to a low and stable rate of inflation, as monitored by the Monetary Policy Committee of the Bank of England, can thus be seen as providing an appropriate economic context for population ageing.

3.13. Standard economic theory posits that individuals will pursue a pattern of "life-cycle savings" in which they accumulate assets during their working years, and decumulate them during retirement. Population ageing over the next 50 years will increase the number of individuals living in the decumulation phase of life, while the number living in the accumulation phase will remain constant or decline slightly. This could lead to more individuals wishing to sell assets than buy (a decline in the net savings rate), which would tend to reduce asset values and increase interest rates (though it should be noted that household saving in the United Kingdom in 2000 accounted for just 3.5 percentage points of GDP, out of an aggregate savings total of 16 per cent of GDP).[31]

3.14. On the other hand, actual outcomes may be very different. Over the last quarter of the 20th century, measured savings rates recorded in household surveys tended to rise with age, with households aged 75+ exhibiting higher saving rates than younger households, including those of prime working age who are likely to be in the middle of their accumulation phase.[32]

3.15. These recorded savings rates appear to overstate the true level of net savings, because they do not include the effective decumulation of pension assets by retired households. Analysis by Professor David Miles, which makes an adjustment for this mis-measurement, indicates that demographic change could reduce the United Kingdom aggregate national savings rate by 8 percentage points by

[29] Professor Booth, volume II, p 276

[30] Young, *The implications of an ageing population for the UK economy*, p 35

[31] Ibid, p 16

[32] Ibid, p 17

2030.[33] The Bank of England notes that a change in aggregate savings of this amount would, by reducing capital accumulation, slow down the rate of growth of output.[34]

3.16. Any such decline in domestic savings would put upwards pressure on the rate of return on domestic capital, and so would tend to attract capital from abroad, though this effect would be diminished to the extent that other industrial countries face greater demographically induced reductions in their domestic savings rates.

3.17. On balance the Bank of England concludes that there remains considerable uncertainty about the impact of ageing on saving, interest rates and capital accumulation, but on the balance of probability the net effect is likely to be small. Both Professor Booth and the Bank of England concur that ageing is most unlikely to cause a collapse in asset values as more people begin to decumulate.[35] They note that the long-run volatility of United Kingdom equity and bond yields in the past has not been correlated with underlying demographic trends, and there is little reason to suppose it will be in the future.

3.18. **We conclude that population ageing may affect savings, interest rates and capital accumulation, but its effect is likely to be small relative to the large range of other economic and political factors which determine the course of these economic aggregates.**[36]

[33] David Miles, 'Modelling the impact of demographic change upon the economy', *Economic Journal*, vol 109 (1999), pp. 1-36

[34] Young, *The implications of an ageing population for the UK economy*, p 35

[35] Booth, volume II, p 271; Garry Young, 'Ageing and the UK economy', *Bank of England Quarterly Bulletin*, Autumn 2002, p 290

[36] Similar conclusions have been drawn for the United States: J.M Poterba, 'Demographic structure and asset returns', MIT *mimeo*, 2000

CHAPTER 4: AGEING AND WORK I: PARTICIPATION

Introduction

4.1. This chapter examines the impact of population ageing on participation in both paid and unpaid work. Participation in the formal labour market declines quite sharply after age 55, and the majority of men have exited the labour market before the state pension age of 65. Some exit from the labour market is a result of individual choice, but some of it may be imposed by personal factors such as ill health, or by the actions of employers. We examine the patterns of early exit from the labour force for various sub-groups of the population, and consider the extent to which these patterns may be driven by supply-side or demand-side factors.

Participation rates below pension age

4.2. Participation in paid employment in the United Kingdom declined sharply for men over the age of 50 between the 1960s and the mid 1990s, since when participation rates have increased. Since 1997, the employment rate for men aged between 50 and the state pension age has risen from over 67 per cent to 70 per cent. Participation rates for older women have also increased over this period, from 61 per cent to 66 per cent, but this has been driven by a rise in general employment rates for successive cohorts of women who entered the labour market from the 1960s onwards. [37] Thus male and female age-specific participation rates are converging (Q143).

4.3. In 1999, the average age of withdrawal from the labour force in the United Kingdom was 62.6 years for men and 60.4 years for women. By state pension age (65 years for men and 60 years for women) around two thirds of men and half of women have left the labour market. In total, a third of people aged between 50 and state pension age are outside the labour market – almost 3 million people.[38]

4.4. The pattern of participation at older ages in the United Kingdom is similar to that in other European Union countries. Italy, for instance, has an average age of withdrawal for both men and women which is several years below that of the United Kingdom, whereas in Sweden the average age of withdrawal is one year higher than in the United Kingdom for men, and two years higher for women.[39] Box 2 reports data on trends in labour force participation by age in the United Kingdom, and locates the UK experience in international context.

[37] DWP, *Simplicity, security and choice* (2002), p 98

[38] DWP, volume II, p 2

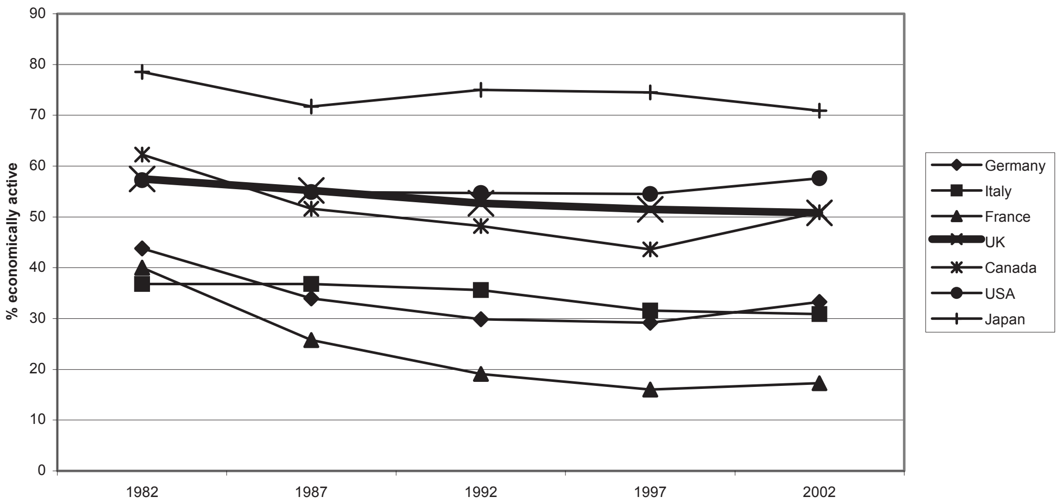
[39] Ibid

Box 2

Trends in labour force participation by age

Labour force participation among older men has declined in most industrialised countries since the early 1980s, although the past five years have witnessed a general reversal of this trend. The figure below shows this trend for men aged 60-64. [40]

Participation rate for males 60-64
Selected OECD countries, 1982-2002



More striking than the trend over time is the difference in the level of participation. There is virtually no tradition of early withdrawal from the labour force by men in Japan. In the USA, Canada and the United Kingdom more than half of men aged 60-64 remain economically active. In most EU countries, however, early retirement is the norm, with barely a third of men aged 60-64 continuing in employment in Germany and Italy, and fewer than one in five in France.

A more comprehensive indicator of economic activity across all age groups, rather than just a single age range, is provided by the average age of withdrawal from the labour force. This measure reveals the average age at which employment income has to be replaced by pension or other non-wage income. Again the UK age of withdrawal lies above the norm for EU countries, close to that for North America, and below that for Japan.

Average age of withdrawal from the labour force in selected OECD countries in 1999[41]

Country	Men	Women
Italy	58.8	57.9
Germany	60.3	60.1
Netherlands	60.4	59.8
Canada	62.4	60.8
United Kingdom	62.6	60.4
USA	64.6	63.4
Japan	68.5	64.7

4.5. There is broad support for increasing rates of employment among older workers, for example by the Trades Union Congress (TUC) (Q326), the Confederation of British Industry (CBI) (p 220), the Engineering Employers' Federation (EEF) (Q571) and Age Concern (p 95). It is viewed as being consistent with trends in life expectancy and age-specific health status; the current and anticipated

[40] OECD, *Labour Force Statistics 1982-2002* (Paris, 2003)

[41] DWP, volume II, p 2

demand from employers for more older workers to balance an anticipated decline in the size of the younger adult workforce; and the desires of many people in their 50s and 60s to remain attached to the labour market, though not necessarily on a full-time basis or in their primary occupation.

4.6. We note with approval that the Government share this desire to increase employment among older workers, which they regard as "essential if we are to address the pensions challenge."[42] Higher participation rates at older ages, and thus longer average working lives, help to address the pensions challenge for individuals by increasing the value of their life-time earnings, and thus increasing the personal resources they have to support themselves in old age. Higher participation rates at older ages also help to address the macroeconomic aspect of the pensions challenge, by increasing the ratio of workers to non-workers in the economy.

4.7. The potential contribution that an increase in participation rates could make to the way in which population ageing will affect our economy and society was emphasised by Mr John Grieve Smith and Mr Phil Mullan. They noted that labour force participation rates are more variable and volatile than the age structure of a population, and are much more amenable to policy intervention than is the age structure. As an example, they pointed out that between 1979 and 2000 the number of people over state pension age rose by 1.3 million, but that the increase in the "working-age" population who were not in work – the unemployed, the otherwise inactive, and those on Government training schemes – was 2.2 million. Thus over this period labour market changes substantially outweighed demographic forces in their upward effect on the economic dependency ratio between workers and pensioners.[43]

4.8. John Grieve Smith and Phil Mullan suggested that an increase in participation rates in the United Kingdom is perfectly feasible in the light of experience in other EU countries. They noted that if over the next 30 years the United Kingdom raised its age- and sex-specific participation rates to the current levels in Sweden or Denmark, this would generate an extra 2 million workers, and would serve to keep the ratio of workers to total population in the United Kingdom stable at its 1999 level. It might also be noted that if those EU countries with particularly low participation rates, such as Italy, were to raise their rates to the current UK level, this would make a substantial contribution to the financing of old age support in these countries.

4.9. The CBI made a similar point by reference to the United Kingdom's recent labour market history. It suggested that raising the participation rate for the 50-65 age group from its current level to the United Kingdom average for all people of working age of 79 per cent is a realistic objective, given the fact that the employment rate for men aged 50-65 was 84 per cent as recently as 1979, whereas today it stands at 70 per cent.[44]

4.10. Given the Government's explicit commitment to extend opportunities for older workers, and the widespread support for this ambition, it is surprising that enhanced employment opportunities for older workers do not appear to be fully reflected in some official forecasts of economic activity rates. Mr Grieve Smith and Mr Mullan noted that projections of age-specific activity rates in 2030, as used by the Government Actuary's Department in the 1999 Quinquennial Review of the National Insurance Fund posit a fall in rates for men aged 55-59 from 74.6 per cent in 1999 to 71.1 per cent, and from 53.8 per cent for men aged 60-64 to 49.2 per cent. For women aged 55-59, the projected activity rate rises from 1999 to 2030, but only marginally from 53.1 per cent to 54.5 per cent, which seems surprisingly small given the cohort effects on female participation rates noted in paragraph 4.2 above.

4.11. The Government Actuary's Department agreed that the 1999 Quinquennial Review did not include any sensitivity analysis considering the effect on the main projection of assuming alternative age- and sex-specific economic activity rates.[45] We welcome the fact that the 2000 Quinquennial Review includes alternative calculations based on higher activity rates for older workers.[46] This work includes a full sensitivity analysis, which we hope becomes the norm.

4.12. **We conclude that official projections of future age-specific labour force participation rates are inconsistent with the Government's stated objectives and policy intentions of increasing the employment rates of older people.**

4.13. We recognise that such projections are calculated on the basis of there being no change in policy. However, when significant new Government policy objectives are introduced, we believe that

[42] DWP, *Simplicity, security and choice* (2002), p 93

[43] John Grieve Smith and Phil Mullan, volume II, p 38

[44] Confederation of British Industry, volume II, p 219

[45] GAD, volume II, p 446

[46] GAD, *Quinquennial Review of the National Insurance Fund 2000* (2003), p 61 (Cm 6008)

it is important that official labour force projections take account of the possible effects of those objectives.

4.14. **We therefore recommend that the Government pay full attention to the need for their labour force projections and policy objectives to be consistent and compatible with each other, bearing in mind that each interacts with the other.**

Participation rates above state pension age

4.15. The Government's ambition to raise labour force participation rates for people aged between 50 and state pension age is matched by a desire to facilitate greater choice and employment opportunity for workers above state pension age. The 2002 pensions Green Paper included proposals to bring forward the date at which more generous rewards are offered to people who choose to defer the receipt of their state pension beyond the normal state pension age, and to allow members of occupational pension schemes to continue working for the sponsoring employer while drawing their occupational pension.[47]

4.16. However, the Government have rejected the idea of raising participation rates beyond age 65 by means of an increase in the state pension age. They have argued that such a move would disproportionately affect lower-income people who rely more on state benefits in retirement, and who, on average, have lower life-expectancy than the population average (Q49). Furthermore, most people have already left the labour market before they reach state pension age, and Mr Peter Tompkins (PricewaterhouseCoopers) noted that an increase in the state pension age to 67 might therefore do little other than increase the number of low-paid older persons who are dependent on non-pension means-tested benefits (Q259).

4.17. Opinion among other witnesses on the idea of raising the state pension age was divided. We agree with Professor Blake, who noted that "it seems very odd, as we live longer and in greater health, that we have this fixed retirement age of 65 for men, soon to be 65 for women" (Q195). He suggested that it would be appropriate to raise the state pension age in response to these improved mortality rates, but to do so with a considerable delay of 20 to 30 years in order to allow individuals to adjust their expectations and their work and savings plans (Q196). The CBI, on the other hand, felt that there is no pressing need to raise the state pension age, and that effort should be directed instead towards increasing participation rates for people in the 50-65 age range.[48] Baroness Greengross suggested that the state pension age should be kept under review in the light of active, fitter and longer life (Q104). Ms Jeannie Drake (Commissioner, Equal Opportunities Commissioner) pointed out that an increase in the state pension age might well lead to many older people re-presenting themselves to the state for means-tested benefits rather than pensions, because of the difficulties they face in securing employment (Q502).

4.18. Ms Alison O'Connell (Director, Pensions Policy Institute) suggested that the Government's appeal to social class differences in mortality rates as a justification for maintaining the current state pension age was unconvincing. She noted that the three-year gap in life expectancy between people in the manual and non-manual groups was less than the five-year gap between men and women, or the seven-year gap between smokers and non-smokers, yet there is no suggestion that state pension age should vary to take account of these inequalities (Q903).

4.19. It is clear that opinions differ about the desirability of driving up participation rates beyond age 65 through an increase in the state pension age. The Government's approach of increasing choice for current workers who wish to work beyond 65 is appropriate for today. However, the Government's decision to reject the case now for a phased increase in the state pension age may not be appropriate for the future. Even on the basis of the Government Actuary's conservative estimate that mortality improvements will tail off by mid-century (paragraph 2.18 above), it is expected that average life expectancy at age 65 will rise by an additional 3 years for men and an additional 2.7 years for women. By 2050, life expectancy at 65 is projected to be 19 years for men and 21.7 years for women, compared with 11.5 years for men and 13.3 years for women in 1928 when the state pension age was set at 65.

4.20. We believe that it would be prudent to link this expected extension in length of life with new expectations that individuals should normally work beyond age 65. Although state pension age does not directly affect employment beyond 65, as people do not have to stop work to collect the pension, nevertheless, as Ms O'Connell pointed out, "it has a huge totemic significance … a signal from the

47 DWP, *Simplicity, security and choice*, pp 101, 105

48 CBI, volume II, p 219

Government that [state pension age] is to be raised in the future is a very powerful message to say that people are now expected to work longer" (Q901).

4.21. **We recommend that the Government should formally review the state pension age every five years in the light of trends in life expectancy beyond age 65, and in the light of their own desire to increase participation rates at older ages. Our own judgment is that the state pension age should be raised.**

Diversity in patterns of participation: regional effects

4.22. Average age-specific participation rates conceal considerable diversity in employment among sub-groups of the population.

4.23. Evidence on the regional diversity of labour market participation among people aged 50 and above was provided by Christina Beatty and Stephen Fothergill (Centre for Regional Economic and Social Research, Sheffield Hallam University). Their research shows that the average United Kingdom employment rate among 50-64 year old men is 70 per cent, but that this varies between a high of 78 per cent in the South East to a low of 55 per cent in the North East. For women the average United Kingdom participation rate of 55 per cent varies ranges from 62 per cent in the South East to 45 per cent in Wales.

4.24. The share of this same 50-64 age group who are out of employment and claiming sickness benefit varies inversely with the employment rate. In large parts of southern and eastern England, the proportion of older men and women claiming sickness-related benefit is under 10 per cent. On the other hand, in most of northern industrial England, in Wales and in much of central Scotland, the proportion is typically 20-30 per cent. The highest claimant rate in May 2002 was in Merthyr Tydfil (South Wales), where 51 per cent of men aged 50-64 were out of employment and claiming sickness-related benefits.[49]

4.25. This evidence suggests that low rates of labour force participation among older workers are not inevitable, but are strongly influenced by local labour market conditions. In many parts of the South-East there is practically full employment among people aged 50-64 who wish to work. This suggests that the Government's ambition of raising the overall participation rate for the 50-64 age group is unlikely to be achieved unless the large regional disparities in older-age participation rates are reduced through a levelling-up towards the rate in the South East. As older workers are less geographically mobile than younger workers (QQ842-4), this levelling-up will require an increase in older-age employment rates in regions of low participation.

4.26. We note that a number of regional initiatives exist, via Action Teams for Jobs and Employment Zones, to help older people move back into employment.[50] However, we believe the scale of the problem may justify a more aggressive policy response.

4.27. **We recommend that the Government incorporate explicit targets with respect to older age employment in their Regional Economic Strategies and in the priorities they set for Regional Development Agencies.**

Diversity in patterns of participation: the impact of ethnicity

4.28. In so far as older members of the black and minority ethnic communities reside in areas which have generally low participation rates for persons over 50, they will experience a regional employment disadvantage. However, the impact of ethnicity exists independently of this regional effect.

4.29. Unemployment rates among black and minority ethnic populations are higher for all age groups than among the white population. However, this disadvantage appears to be compounded by age. In the late 1990s, the unemployment rate for whites was 5 per cent for both 35-44 year olds and for people aged between 45 and state pension age. For blacks it was 12 per cent among 35-44 year olds, and 16 per cent among those between 45 and state pension age, and for members of the Pakistani/Bangladeshi communities it was 13 per cent among the 35-44 age group, but 26 per cent among persons aged between 45 and state pension age.[51]

4.30. Ms Maureen Fraser (Commission for Racial Equality) told us that, although direct information is scarce, because of a dearth of representative survey data on the black and minority

[49] Christina Beatty and Stephen Fothergill, volume II, p 429

[50] DWP, *Simplicity, security and choice* (2002), p 96

[51] PRIAE, volume II, p 200

ethnic population, it appears that many black and minority ethnic persons aged between 45 and state pension age experience both an "ethnic penalty" and an "age penalty" in their interaction with the labour market (Q527).

4.31. We note that the Government have developed policies to improve both the employability and the participation rates of ethnic minorities, as outlined in the Cabinet Office Strategy Unit report on *Ethnic Minorities and the Labour Market*.[52] However, much of the policy energy is to be directed at labour market entrants and younger workers.

4.32. **We recommend that, as part of the Government's evolving strategy for improving the position of ethnic minorities in the labour market, particular attention should be paid to the "double disadvantage" of age and ethnicity encountered by members of ethnic minorities aged over 50.**

Diversity in patterns of participation: the impact of gender

4.33. There have been very significant changes over time in the participation rates of women; these changes have affected successive cohorts of women, and have been closely related to women's experience of childbearing. As is the case with many other important social adjustments, the rise in female participation rates has occurred gradually over a number of decades without substantial social disruption, and this reflects the extent to which British society can adapt successfully over time to new social norms.

4.34. Professor Heather Joshi (Centre for Longitudinal Studies, Institute of Education, University of London) provided us with evidence about the labour market experience of successive cohorts of British women born between 1910 and 1970 (and thus reaching state pension age between 1970 and 2035). If one excludes absence from the labour market for reasons of childcare, women in the 1910 cohort worked for less than two thirds the amount of time as men. For the 1958 cohort (that is, those entering the labour market in the mid-1970s) and subsequent cohorts, however, women have worked to virtually the same degree as men, excepting time out of the labour market for birth and childcare. [53]

4.35. An even greater change over time relates to the length of the employment break associated with birth. For the 1910 cohort, the average mother returned to work 13 years after the birth of her child, but for the 1970 birth cohort half of mothers had returned to work within a year of birth. This represents a revolution in the way in which motherhood interacts with employment

4.36. There is, however, a growing divergence over time in the experience of mothers according to their level of qualification. Mothers with higher qualification essentially now pursue continuous careers, whilst mothers with no qualifications typically take employment breaks of 4 to 5 years after the birth of a child. This diversity in female employment patterns has a significant impact on women's economic resources in old age, an issue discussed in chapter 8 below.

Explanations of early retirement: supply and demand

4.37. The reasons for the diversity in age-specific participation rates are more difficult to discern than is the diversity itself. It is clear that both supply-side factors (the skills, capacities, motivations and preferences of workers) and demand-side factors (the needs and preferences of employers) are important, but the relative weight that should be given to each is disputed. Different witnesses emphasised different causes. (The issues of individual capacity and skills and of employer preferences are discussed below in chapters 5 and 6 respectively.)

4.38. The CBI emphasised the disincentives to employment that are created by some elements of the benefits system, noting particularly the fact that recipients of Incapacity Benefit (IB) have received little encouragement from the Benefits Agency and the Employment Service to seek work; that the higher rate of IB compared to Jobseekers Allowance provides a strong incentive to move on to IB; and that once on IB it is difficult to move off it, since older IB recipients would typically take home only about 25 to 35 per cent more from work than from IB.[54]

4.39. The TUC, on the other hand, viewed high rates of receipt of Incapacity Benefit more as a consequence of restricted employment opportunities for older manual workers in those part of the country that have experienced significant restructuring of their historic industries (Q347). However, the TUC also noted that many European countries, even those with low overall levels of unemployment, experience large numbers of older people on long-term benefits, so the level of

[52] Cabinet Office Strategy Unit, *Ethnic Minorities and the Labour Market* (2003)

[53] Professor Heather Joshi, volume II, pp 137-8

[54] CBI, volume II, p 220

aggregate demand in the labour market cannot be the only explanation of high levels of long-term benefit receipt (Q347). We give further consideration to the impact of health on employability in chapter 5 below.

4.40. Some early withdrawal from the labour force is entirely voluntary. The Department for Work and Pensions (DWP) has noted that there is no definitive evidence on the causes of inactivity amongst older workers, or on the extent to which early withdrawal from the labour market is voluntary. Among inactive people aged 50+, about 20 per cent say they have retired early, and they may have done so voluntarily, since many of these individuals are drawing occupational or personal pensions.[55]

4.41. People with good pension coverage are more likely to be able to self-finance their early retirement, but on the other hand, some employers may use company pension schemes to shed older workers. The CBI noted that this had been a common practice in the 1980s, when many companies made use of surpluses in their pension funds to restructure their labour force by offering generous early retirement pensions to their older workers (Q606).

4.42. A further issue which needs to be considered in the evaluation of the relative role of supply-side and demand-side influences on participation rates at older ages is the extent to which individuals are prepared to be flexible with respect to wages. Professor Richard Disney and the CBI both noted that one reason for lower participation rates at higher age might be because some older workers are not prepared to accept employment at lower wages than younger workers, even if their skills and productivity are lower than those of younger workers.[56]

4.43. Regardless of the causes of early retirement, there is evidence that individual choice about when to withdraw from work is important for well-being. According to evidence from Professor Peter Warr (Institute of Work Psychology, University of Sheffield) up to age 60/65 the happiness of employed and of early-retired people is, on average, identical if they have chosen their status. Early retirement is more desired by those who dislike their job, have poor health, or who will have an adequate income after retirement.[57]

4.44. It is also clear that many individuals who have left the labour market continue to perform socially and economically valuable roles. They may provide unpaid child care or elder care for family members (thereby enabling others to be economically active) or participate in the voluntary sector. According to evidence provided by Dr Justin Davis Smith (Institute for Volunteering Research), in 1997 40 per cent of people aged 55-64, 45 per cent of those aged 65-74, and 35 per cent of those aged 75+ participated in formal voluntary activity. These rates are lower than for prime–age adults (57 per cent for persons aged 45-54), but they display a much less rapid rate of decline by age than do employment rates.[58]

4.45. The evidence we have received suggests that there are many potential reasons for the non-participation of older people, including:

- a preference for leisure rather than work on the part of individuals who are in receipt of an adequate income from private or public resources
- an imposition on older persons by employers who use various institutional mechanisms to induce them to retire
- poor health
- a reluctance of older workers to accept a realistic wage for their labour services
- a fundamental lack of demand in the local labour market

4.46. We note, however, that there is no agreed ranking of the importance of these various causes of non-participation. Both the Department for Work and Pensions and other researchers have identified the problem of a lack of definitive evidence on the causes of labour force inactivity among older persons. If the Government are to make progress towards their goal of increasing participation rates for people aged between 50 and the state pension age, we believe that they will need better information on the causes of non-participation.

4.47. **We recommend that the Government commission further research and analysis into economic inactivity among persons aged 50+, in order to produce a clear basis of evidence on**

[55] DWP, volume II, p 3

[56] Professor Disney, volume II, p.299; CBI, volume II, p 220

[57] Professor Warr, volume II, p 486

[58] Institute for Volunteering Research, volume II, p 447

which to build policies to promote higher rates of labour force participation among older persons.

CHAPTER 5: AGEING AND WORK II: PRODUCTIVITY AND SKILLS

Introduction

5.1. This chapter reviews evidence on the extent to which poor health or inadequate or inappropriate skills may reduce the employment chances of older people. It also considers the extent to which age alone, independently of health or skill, adversely affects job performance. This is a crucial issue for our ageing society, and one about which it is often assumed we know the answer. Our evidence indicates that empirical evidence about the relationship between productivity and age is thin, and we conclude that more research in this area needs to be undertaken as a matter of urgency.

Age and work capacity: the impact of health status

5.2. It is clear that some people below state pension age do not work because of reported poor health. A report in 2000 by the Cabinet Office Performance and Innovation Unit noted that, of the 2.8 million people aged between 50 and state pension age who were outside the labour market, 1.25 million were long-term sick or disabled, and only 0.29 million were currently seeking work.[59]

5.3. The number of people aged over 50 who are long-term sick or disabled has increased over time. This increase should be viewed in relation to the long-run improvement in life expectancy and in health status. Mr Mullan noted that there is unequivocal evidence that health status is improving at all ages, yet there has been a paradoxical increase over time in self-reported illness and in claims for disability benefits (Q137).

5.4. It was noted above (paragraph 4.24) that sickness-related benefit claims among older workers are regionally concentrated in areas of declining industry. Mr David Coats (TUC) suggested that part of the explanation for the paradox of improved average health status and rising disability rates is cultural (Q350). As the structure of the economy has changed, some workers from old industrial sectors have seen themselves as unfit for different types of jobs in the service sector, and employers have also seen them as unsuitable (Q348). Thus perceptions of physical fitness and suitability for specific types of work may be as important as objectively determined health status.

5.5. These divergent trends in age-specific sickness and number in receipt of long-term sickness or disability benefit indicate that many benefit recipients could work if conditions and incentives were appropriate. Only about 50 per cent of Invalidity Benefit claimants originally left work primarily because of ill health rather than other reasons, such as redundancy; their move on to benefit appears to have followed a period of unsuccessful job search.[60] However, Dr Sarah Harper (Director, Oxford Institute of Ageing) noted that current cohorts of older workers may have internalised the notion of early retirement as a normal phase of the life course, and thus may be particularly resistant to policy initiatives aimed at reintegrating them into the labour market.[61]

5.6. It is possible for employers to respond to any decline in the health status of older workers by redesigning the job task or the workplace. Dr Philip Taylor (Executive Director, Cambridge Interdisciplinary Research Centre on Ageing) noted that job redesign had been promoted in Japan as an effective policy response to the ageing of the workforce (Q1006); Baroness Greengross pointed to the effectiveness of similar policies in Scandinavian countries (Q114). Mr Mullan pointed out that it is possible to reorganise the division of labour within work teams so that individuals who have less physical capability – whether or not it is age related – can still fully contribute to the work process (Q162). The TUC noted that many older workers desire flexible employment, and it is therefore in the interests of employers to change the organisation of work so that they can make best use of the growing number of older workers.[62]

5.7. **We recommend that the Government, employer and labour organisations collect information and disseminate "best practice" guidelines on ways in which jobs and workplaces can be redesigned to facilitate the employment of older workers who have activity-limiting health status.**

5.8. **We further recommend that employers should actively evaluate and instigate the redesign of job tasks and workplaces in order to maximise the opportunity for retention and recruitment of older workers.**

[59] Cabinet Office Performance and Innovation Unit, *Winning the Generation Game* (2000), p 21

[60] Ibid, p 25

[61] Dr Harper, volume II, p 462

[62] TUC, volume II, p 119

Age and work capacity: the impact of education and skills

5.9. The employability of any individual will in part be determined by their level of skill. Economic development changes the mix of skills required by employers, with demand for high-skill workers rising relative to low-skill workers. This trend can adversely affect older workers in particular if their skills have not been upgraded since leaving full-time education.

5.10. The CBI reported that low skills are a barrier to the employment of people aged over 50. A third of people aged 50-64 have literacy and numeracy problems, compared to around a fifth of 26-35 year olds. Among the economically active population, 37 per cent of 50-64 year olds are not qualified to level 2 (equivalent to five or more GCSEs at C Grade or above), compared with 27 per cent of 20-34 year olds. Given that the number of low-skill jobs in the economy is shrinking, this educational deficit among older workers acts as a barrier to employment.[63]

5.11. Ms Susan Anderson (Director of Human Resources Policy, CBI) noted that this educational deficit is a particular disadvantage to older persons who become unemployed. On average, a younger job applicant will be more skilled than an older job applicant; thus younger job applicants are more likely to be recruited than older applicants. This effect occurs for economic reasons quite independently of any ageism that may exist on the part of employers (Q611).

5.12. Mr Bruce Warman (Employment Policy Director, Vauxhall Motors) pointed out that there is no separate labour market for the over 50s, nor is there a typical over-50 person. However, the new jobs that are being created are more likely to be in the service sector, involve team work and require skills in dealing with customers. These are very different from typical manual industrial skills. Quite apart from literacy and numeracy levels, some older workers find it difficult to adjust to the different type of skill required in new service-sector jobs. This may be less of a problem for younger people, who are less likely to have had experience in manual industrial employment, and who may possess more up-to-date basic skills due to their recent exposure to formal education (Q612).

5.13. The relative role of poor education and low qualifications can account for some of the high rates of non-employment among persons over 50, but cannot account for the regional pattern of non-employment. Ms Anderson noted that problems of literacy and numeracy are prevalent in all labour markets across the United Kingdom without any particular regional black spots (Q600).

5.14. The literacy and numeracy deficit of people over 50 is, to some extent, a cohort effect related to the educational and employment history of people born in the 1940s and early 1950s, rather than a simple age effect, so it may be diminished among future cohorts of the over-50s (Q1015). On the other hand, if access to workplace training is rationed by age, then a skills deficit among older persons is likely to persist across future cohorts, since workplace training plays an important role in maintaining and updating the skills of the working population. Dr Philip Taylor suggested that employers are less willing to train older than younger workers (Q1015). Mr Neil Churchill (Communications and Marketing Director, Age Concern) referred to survey evidence which indicates that the proportion of 50-65 year olds who receive workplace training is approximately half that of younger age groups (Q298).

5.15. Professor Disney indicated that the cost-effectiveness of training may be an issue of concern to employers, since the potential pay-back period is greater if the training is provided to a younger worker, provided that that worker stays with the employer.[64] Evidence supplied by the Engineering Employers' Federation, however, indicates that the median length of time a worker stays with any particular employer is 5 years 6 months, with shorter tenure the norm for younger workers.[65] Furthermore, Mr Churchill pointed to research which shows that the benefits for the employer of job-related training are usually reaped in the first year, so any age-related rationing of workplace training would appear to be a function of non-economic management decisions.

5.16. The Government are actively promoting life-long learning for current and future cohorts through a combination of public provision, individual effort and workplace training. Dr Taylor pointed out that life-long learning, and other policy measures designed to increase the employability of older persons, will be most successful if directed at the entire life course. It is more effective to enhance the skills of 30 and 40- year-olds to assist them in maintaining continuous employment, rather than to attempt to revive the skills of people in their 50s once they have become detached from the labour market (Q1006). Nevertheless, it does not follow that there is no point in reviving or enhancing the skills of people in their 50s and older.

[63] CBI, volume II, p 219

[64] Disney, volume II, p 299

[65] Pension Provision Group, *Pensions and the Labour Market*, (2001) p.23; with thanks to the Engineering Employers' Federation

5.17. **We recommend that the Government and employers work together to develop mechanisms to promote equal access to workplace training and life-long learning for workers regardless of their age.**

The relationship between age and job performance

5.18. The ageing of the population will increase the number of older workers relative to younger workers in the United Kingdom labour market. If older workers are close or perfect substitutes for younger workers, then this shift in the age structure of employment can be achieved with minimal economic disruption. If, on the other hand, older workers differ significantly from younger workers in their skills, trainability, productivity and reliability, an ageing of the workforce may have significant economic impact. It is therefore important to determine whether, and in what ways, older workers differ from younger workers in their workplace performance.

5.19. A survey conducted by the Engineering Employers' Federation (EEF) of its member companies revealed that most employers who expressed a view about older workers generally considered them to be more loyal, committed, reliable, trustworthy, accurate and stable than younger staff. On the other hand, in the context of manufacturing production, workers under 40 were considered to be faster, more efficient, more physically and mentally able and to have better sickness records.[66]

5.20. Some EEF members also noted that health and safety issues deter them from recruiting older staff to do heavy physical work because they are "not physically up to the pace over an extended period."[67] Mr Warman (Vauxhall Motors) agreed that health and safety considerations were important for some, but not all, industries. He said that he was "very uncomfortable about having people over 60, generally, working on a production line" (Q612).

5.21. Mr John Philpott (Chief Economist, Chartered Institute of Personnel and Development) noted that most employers do not have direct information on individual productivity; this is extremely difficult to obtain from workplace studies, because in most organisations the output is the joint product of many individual workers (Q772). Professor Peter Warr (Institute of Work Psychology, University of Sheffield) pointed out that workplace studies do not necessarily provide unambiguous evidence of the relationship between age and job performance, because the process of self-selection means that individuals who detect changes in their own performance, motives and capabilities may move to less demanding work, or may withdraw entirely from the labour force.[68]

5.22. Despite this difficulty in interpreting research results, Professor Warr informed us that extensive research has shown that, on average, there is no significant difference between the job performance of older and younger workers. Although the average association between age and performance in a job is about zero, in some cases older employees clearly perform better and in others they are clearly less effective than younger ones. However, these conclusions are derived from studies which typically designate older workers as those aged 40-55. Little research has been conducted on the work effectiveness of people aged 55 and above. [69]

5.23. Mr Neil Churchill (Age Concern) pointed out that, although productivity is difficult to measure, it is clear that older workers can bring to the workplace characteristics such as knowledge of the institution which are of value to employers, and which younger workers are less likely to possess (Q284). Thus a workforce with a diverse age structure may possess a broader and richer array of skills than a workforce comprised solely of young or of old workers.

5.24. Dr Philip Taylor (Executive Director, Cambridge Interdisciplinary Research Centre on Ageing) noted that, despite the research findings that age has no net effect on workers performance, when supervisors and managers are asked to rate the performance of workers, they consistently rate the performance of older workers below that of younger workers. Dr Taylor suggested that this may reflect the way in which socially constructed age stereotypes operate in the workplace (Q1006).

5.25. It is clear to us that there appears to be little robust evidence on the relationship between individual age and worker productivity, despite the importance of this issue.

5.26. **We believe it is essential to improve knowledge of the relationship between individual age and worker productivity in order to provide a sound foundation for evidence-based policy. We therefore recommend that the Government commission research on the relationship**

[66] EEF, *Summary of Responses to EEF Age Discrimination Questionnaire*, p 1

[67] Ibid

[68] Warr, volume II, p 484

[69] Ibid

between individual age and worker productivity in order to strengthen the evidential base for future policy initiatives in the area of older-age employment.

CHAPTER 6: AGEING AND WORK III: AGE DISCRIMINATION

Introduction

6.1. Age discrimination in the labour market can impose significant economic costs on individuals who may be prevented from undertaking paid employment, on employers who may inadvertently restrict the pool of workers from which they recruit, and on the economy as a whole because of a misallocation of labour. In this chapter we survey evidence on the existence and extent of age discrimination in the United Kingdom labour market. We then turn to consider the implications for employers and workers of the implementation by 2006 of the EU directive on age discrimination.

The extent of age discrimination

6.2. Discrimination in the labour market on grounds of age can occur both directly and indirectly (Q282). Direct age discrimination occurs when, for example, an employer attaches an upper or lower age limit to a particular job, or selects staff for voluntary redundancy on grounds purely of age, rather than work competence. Indirect age discrimination occurs when, for example, career progression is contingent on the possession of specific formal qualifications which have been in existence for only a limited period, and which therefore are unlikely to be held by persons over a particular age.

6.3. Age discrimination can be deliberate, but it is often unconscious. For example, if an employer adopts general employment criteria which have a differential impact on certain people because of their age, but which are not relevant to job performance, then age discrimination is likely to result (Q763).

6.4. Some jobs have formal age thresholds that are sanctioned by law for reasons of health, safety or morality – for example, minimum ages for employment in licensed premises, or driving heavy goods vehicles. These do not fall within conventional definitions of age discrimination.

6.5. Evidence about the existence or prevalence of age discrimination in the labour market is far from straightforward. As noted in the two previous chapters, there are many factors influencing both the supply of and the demand for workers which may affect the age structure of employment in a particular company or economic sector, quite apart from any conscious or unconscious discrimination on the part of the employer. The fact that persons of a particular age may be under-represented in a specific employment cannot, on its own, be taken as evidence of age discrimination in that employment.

6.6. Nevertheless, we have received evidence that large numbers of older people believe they have been discriminated against in the labour market because of their age. The Chartered Institute of Personnel and Development (CIPD) reported that its surveys consistently provide evidence of employer discrimination against older people. Ms Dianah Worman (Diversity Adviser, CIPD) described age discrimination as “pervasive” in almost all sectors of the labour market (Q754).

6.7. A CIPD survey of ageism conducted in 2001 found that 10 per cent of respondents aged 45-54 believed they had been rejected for a job they had applied for in the previous 12 months because they were considered “too old”, though few had any hard evidence of discrimination. At the other end of the age range, 7 per cent of respondents aged 16-24 had been told explicitly that they were “too young” for a job they had applied for, while a further 6 per cent suspected age was the reason they were rejected. Thus age discrimination is perceived to exist among both younger and older workers (though the determination of who is viewed as “young” and who as “old” appears to vary across industries and sectors).[70] A subsequent survey conducted for the CIPD in February 2003 found that 40 per cent of persons interviewed believed they had been discriminated against at work. Significantly, age appeared to be the primary reason for discrimination, and was cited by one third of all respondents who believed they had experienced discrimination, compared to 14 per cent who cited gender, 5 per cent who cited disability and 2 per cent who cited race.[71]

6.8. Mr Ian Brinkley (Chief Economist, TUC) suggested that explicit age discrimination, such as when age limits are included in job advertisements, is now unusual. A larger problem is that within companies many managers are unaware that the processes and procedures they adopt may discriminate on the basis of age. He thought that awareness of age discrimination significantly lagged behind awareness of discrimination on grounds of race or sex (Q335). Dr Philip Taylor agreed that although there is evidence of employers actively responding to negative stereotypes of older workers there is also much evidence that age discrimination in the workplace is the result of unintended outcomes:

[70] Chartered Institute of Personnel and Development, *Age discrimination at work*, p 11

[71] CIPD, *Age, pensions and retirement: Attitudes and expectations*, p 11

employers "often have not heard of age discrimination and they would not know whether they were doing it or not" (Q1018).

6.9. Ms Susan Anderson (Director of Human Resources Policy, CBI) agreed that ageism exists among the employer community just as in society as a whole (Q611). She noted that some stereotypes about the ageism of particular employers have historical roots and reflect the fact that during the industrial restructuring of the 1980s there was frequent agreement among employers, trade unions and the Government to encourage older workers to leave the labour market and make way for younger workers (Q614).

6.10. The TUC queried whether the targeting of older workers for redundancy, which was common in the 1980s, has really been reversed. The offer of early retirement can still be an important way for firms to adjust the size of their workforce in both traditional and newer industries such as telecommunications.[72] Mr Churchill (Age Concern) believed that a shift of employer attitudes against older workers in the 1980s, which occurred for historically specific reasons, has still not been reversed. In the 1980s and 1990s, employers who operated occupational pension schemes often found it easier and cheaper to shed older rather than younger workers, because the pension fund could bear much of the cost of early retirement. The decline in investment values over the past four years has reduced or eradicated the surpluses that had accumulated in many pension funds, so this option is now less appealing to employers than in the past, but it continues to provide some scope for low-cost restructuring (Q282).

6.11. The Government have been active in raising consciousness of age discrimination within the employer community. In 1999, they issued a Code of Practice on Age Diversity. This appears to have increased awareness of age discrimination among the business community, and has helped to reduce the deliberate practice of excluding people from employment on the basis of age (Q763).

6.12. However, the Government's track record in countering age discrimination within the public sector is, at best, mixed. Retirement at age 60 is still the norm within the Civil Service, although the Government have stated that the normal retirement age for public employees should increase from 60 to 65 for new entrants, with protection for those who are within 10 years of retirement (Q1082). The Secretary of State for Work and Pensions noted that "in many respects the public sector has not been as flexible on these matters as the more enlightened people in the private sector" (Q1082).

6.13. Age discrimination in employment is deplorable in itself and harmful to the economy.

6.14. **We conclude from the evidence available that there is significant age discrimination in employment, and that this discrimination occurs throughout the economy and in both public and private sectors.**

6.15. **We further conclude that few employers operate overtly ageist recruitment and retention policies (except in so far as they use fixed retirement ages). Age discrimination is frequently the unconscious outcome of an employer's more general human resource management policy and procedure.**

6.16. The apparent infrequency of direct age discrimination through the implementation of overtly ageist recruitment and retention policies is, we believe, a positive signal that most employers have rejected the use of strict age thresholds as being inappropriate to the workings of a modern flexible labour market. However, the apparent extent of unconscious ageism in employment remains a major challenge, since the eradication of unconscious discrimination will require a fundamental cultural change on the part of employers and workers. We discuss this issue further in paragraph 6.46 below.

6.17. Evidence from the voluntary sector indicates that age discrimination affects participation in non-waged as well as waged work. Research conducted in 1998 by the Institute of Volunteering Research revealed that almost one in five voluntary organisations applied upper age limits to their volunteers. Many voluntary organisations cited the difficulty of obtaining insurance cover for older volunteers as the reason for their use of an upper age limit, though it is likely that in some organisations this is used as an excuse for not taking on older volunteers.[73]

6.18. We also investigated the appointment policies and practices of a number of non-governmental public bodies to determine whether participation in these organisations is affected by any form of age discrimination. Although participants in many such bodies receive allowances and out-of-pocket expenses, they are often not formally remunerated. Even when remunerated, for example as in the case of BBC governors, their service is conditioned by a letter of appointment rather a contract of employment. Thus participation in these bodies is not normally deemed to constitute employment.

[72] TUC, volume II, p 114

[73] Institute for Volunteering Research, volume II, p 448

6.19. Scrutiny of the available information on the ages of members of many public bodies such as the BBC, Sport England and the General Medical Council suggests possible age discrimination in appointments. Overwhelmingly, people appointed to such bodies are aged between 45 and 65, and being appointed at an older age or serving beyond the age of 70 seems to be virtually impossible.

6.20. We were concerned to find that there appears to be no common practice of recording and reporting on the age profile of participants in non-governmental public bodies. For example, no information is available on the age structure of those currently serving as special constables, whereas for the lay magistracy the Department for Constitutional Affairs was able to state that of the more than 28,000 lay magistrates, under 4 per cent are aged under 40 and almost 35 per cent are aged 60-69.[74]

6.21. We received evidence from Dame Rennie Fritchie, the Commissioner for Public Appointments, about the procedures followed by Departments in making appointments to public bodies. She noted that appointments are intended to be as inclusive as possible, and that age should not be a criterion for the assessment of suitability for appointment or reappointment. She reported that, in the case of magistrates, there is a statutory upper age limit of 70, and she suggested that this limit should be reviewed to determine whether it now has (or has ever had) a functional justification (Q1167).[75] We condemn such discrimination in the appointment of magistrates.

6.22. In response to the suggestion that there is a widespread belief among actual and potential applicants that in practice upper age limits appear to be applied to applicants for public appointment even when no formal age limits exist, Dame Rennie suggested that there may be procedural problems within Government Departments, where sponsor teams may have inadequate experience of managing the process of public appointments, and may be unaware of what may constitute either direct or indirect age discrimination (Q1170).

6.23. Age discrimination in public appointments should be condemned and brought to a halt. We note in particular the disproportionate impact on women, who tend, because of career breaks resulting from caring responsibilities, to become available for such appointments later in life.

6.24. **We recommend that ageism in public appointments, whether directed against those considered too old or too young, should be brought to an end, and that an explicit commitment to age diversity in public appointments should be made by the Government and all sponsoring Departments. We believe that this can best be achieved by ensuring that the process of appointment to any public body complies with the terms of the forthcoming legislation on age discrimination in employment, even in those cases in which such appointments do not constitute formal employment.**

6.25. **We further recommend that the Commissioner for Public Appointments be given statutory authority to seek out cases of ageism in public appointment procedures, and should also have powers which would lead to the diminution and eventual eradication of ageism.**

6.26. We were concerned to hear that the remit of the Commissioner for Public Appointments does not extend to all public bodies. For example, it does not include Privy Council nominations to various bodies (Q1194). We were also concerned to hear that appointments to hospital boards, which currently fall within the Commissioner's remit, will no longer do so in the case of foundation hospitals.

6.27. **We recommend that in relation to ageism the remit of the Commissioner for Public Appointments be extended to include appointments to those publicly funded bodies which currently or prospectively lie outside this remit.**

The legislative environment

6.28. Discrimination in employment on grounds of age is not at present illegal in the United Kingdom. However, EU Employment Directive 2000/78 provides a common framework of protection against discrimination at work on the grounds of sexual orientation, religion or belief, disability and age. The age strand of this Directive has to be implemented by December 2006.

6.29. The Government, through the Department of Trade and Industry, has been conducting an extensive consultation exercise since July 2003 specifically on the age clauses of this Directive, with a view to having legislation in place (but not in force) by December 2004 so that individuals and employers will have two years to prepare for changes to employment practices. [76]

[74] Department for Constitutional Affairs, volume II, p 441; Home Office, volume II, p 447

[75] We note, however, that the Commissioner's narrow remit does not cover the appointment of magistrates.

[76] Secretary of State for Work and Pensions, volume II, p 404

6.30. In the absence of draft legislation, there appears to be considerable difference of opinion about the likely impact of the Directive for employment policies and practices in the United Kingdom. Dr Katherine Rake (Fawcett Society) was of the view that the legislation would prohibit employers specifying age in relation to any decision with respect to employment, recruitment or retention. On the other hand Ms Anderson (CBI) believed that differential treatment on grounds of age could be permissible, if appropriately justified (Q620).

6.31. These differences of opinion arise from uncertainty about how the Government will implement Article 6 of the Directive, which allows Member States' implementing legislation to permit practices that otherwise amount to direct age discrimination where they are "objectively and reasonably justified by a legitimate aim, including legitimate employment policy, labour market and vocational training objectives, and if the means of achieving that aim are appropriate and necessary."[77]

6.32. The Government will not determine how to incorporate the provisions of Article 6 into United Kingdom legislation until the recent *Age Matters* consultation has been assessed. However, the Secretary of State for Work and Pensions suggested that he thought the criteria for "objective justification" for discriminatory practices would be narrowly defined (Q1101). We therefore believe that employers should prepare for the forthcoming legislation on the assumption that direct age discrimination will not normally be permitted.

6.33. Particular concern was raised over the issue of "succession planning" in businesses which have a number of people approaching retirement at the same time (Q586). We note that the Government have identified this as one of a small number of specific circumstances which might justify exceptional treatment under the forthcoming legislation, as long as an "objective justification" is provided.[78]

6.34. **We recommend that the Government should be as explicit as possible in providing illustrations of the circumstances in which exceptional treatment may be justified, in order to provide the clearest possible guidance to both employers and workers.**

6.35. An additional area of uncertainty relates to the stipulation of a "normal retirement age". This is another issue that is being considered in the current consultation exercise, and it is one on which the Government note that there is no clear agreement about the best way to implement legislation.

6.36. In evidence to us, the CBI noted that its colleagues in other EU states believe that they will continue to be able to set and implement a normal retirement age. The CBI counselled the Government to ensure that the implementation of the EU Directive in the United Kingdom is not out of line with that adopted in other EU countries, since otherwise UK employers might be disproportionately burdened with complex and costly legislation (Q621).

6.37. Both the CBI and the EEF noted that the use of a normal retirement age can be advantageous to both worker and employer. For the employer, it provides certainty with respect to succession planning, and for the worker it provides an administratively simple and socially acceptable mechanism for withdrawal from the labour force. Mr Martin Temple (Director General, EEF) noted that "it is often a form of celebration when somebody has reached retirement and is moving on", and he expressed concern that the abolition of normal retirement age might replace a dignified and harmonious process of exit with conflict, acrimony and litigation (Q578). Mr Warman (Vauxhall Motors) felt that the abolition of a normal retirement age might particularly affect smaller companies, because they are likely to have less scope for redeploying older workers in alternative roles, and fewer resources in their personnel divisions to deal with issues specific to ageing workers (Q617).

6.38. Concern was also raised by the CBI that, in the absence of a normal retirement age, there might be frequent resort to industrial tribunals to resolve disputes over decisions about which workers should stay and which should go, particularly if the cost to the worker of initiating a tribunal claim were low (Q619). Professor Peter Warr noted that concern about potential legal claims against subsequent alleged unfair dismissal might discourage some employers from employing older people; thus it is conceivable that the anti-discrimination legislation could reduce rather than enhance employment opportunities for some older people.[79]

6.39. On the other hand, the point was forcefully made by the Equal Opportunities Commission and the Fawcett Society that for the new legislation on age discrimination to be effective, it needs to be backed by a powerful enforcing body (QQ374; 496). Enforcement is unlikely to be effective in the absence of clear legal sanction.

[77] Secretary of State for Work and Pensions, volume II, p 404

[78] DTI, *Equality and Diversity: Age Matters* (2003) p 16

[79] Warr , volume II, p 486

6.40. We recognise these concerns about the potential costs to all parties of extensive resort to litigation to resolve disputes arising from the legislation on age discrimination. We were reassured to hear the Secretary of State for Work and Pensions express the desire of the Government that this legislation should be carried forward "with large measures of common sense and a minimum amount of intrusive bureaucracy" (Q1104).

6.41. **In order to minimise the cost to all parties of disputes relating to age discrimination, we recommend that the Government should incorporate in the forthcoming legislation on age discrimination the option of rapid and low-cost arbitration of disputes.**

6.42. We also recognise the legitimacy of arguments for retention of a normal retirement age, but on balance we believe that any such retirement age may impose restrictions on the efficient functioning of the labour market in our ageing society. We believe it is for firms and their employees to devise their own retirement systems, and we further believe that these systems should be based on performance criteria rather than chronological age. We have taken note of the fact that in both the United States and Australia the introduction of legislation on age discrimination has proscribed the use by employers of a normal retirement age, yet this has had only a marginal impact on the employment patterns and retirement behaviour of older workers (Q995).

6.43. **We therefore recommend that the Government should not permit the continued use of a normal retirement age by employers, whether at age 65 or 70 or 75, unless the employer can provide a reasoned and objective justification for the use of age rather than performance criteria in the determination of employability. We further recommend that the Government set an example of good practice by explicitly removing upper age limits in all public-sector employment in advance of the implementation of the forthcoming legislation on age discrimination.**

6.44. We are concerned, however, that the implications of the legislation on age discrimination have yet to be fully appreciated by most employers and most workers in the United Kingdom. The proscription of the use by employers of age as a criterion for recruitment, promotion, training, redundancy or retirement will have a profound impact on employment practices. The Chartered Institute of Personnel and Development noted that this impact would be greatest on those "command-type organisations" in which mandatory retirement is a convenient device for easing the process of promotion and facilitating natural wastage.[80] We believe that many private-sector organisations, and much of the public sector, is characterised by this style of personnel management.

6.45. When age cannot be used directly or indirectly as a criterion for determining employment decisions, it will be necessary for employers to adopt clear performance criteria to determine which individuals should be recruited, promoted, demoted or made redundant. This will require the further development of worker appraisal throughout a person's working career, and other systems of worker evaluation. Baroness Greengross noted that difficulties will be encountered in developing more thorough-going appraisal systems, but that this was an inevitable stage of moving towards a more age-diverse labour market (Q112).

6.46. **We conclude that a move from age-based to competency-based criteria for recruitment, promotion and retirement will require a profound cultural shift on the part of both workers and employers. Long-established conventions about seniority-based promotion and pay will have to be challenged, employers will have to operate transparent and justifiable personnel policies, and employees will have to accept regular monitoring and assessment of their job performance.**

6.47. We are concerned that the time scale for the implementation of the legislation on age discrimination will allow employers and workers at most two years to revise their procedures and expectations to conform with the new legislation. This is a very short period, given the scale of the cultural shift required, and it may impose a particularly onerous burden on small businesses.

6.48. **We therefore recommend that, as soon as the draft legislation on age discrimination is in place, the Government, in conjunction with both employer and worker organisations, should embark on a major campaign to raise awareness of the impending legislation, and of its likely effects.**

6.49. **We recommend that, just as legislation is now scrutinised for possible infringements of, for example, human rights, it should become routine for such scrutiny to cover the issue of age diversity, and for Ministers to certify that policy and legislation do not contain an ageist element.**

[80] CIPD, volume II, p 269

CHAPTER 7: AGEING AND CONSUMPTION

7.1. The relationship between consumer spending and age falls well within the remit of our inquiry, but the need to concentrate on a limited number of topics has meant that we have not dealt in detail with the impact of ageing on spending patterns. We do, however, have evidence that suggests some degree of market failure and discrimination. That gives rise to several questions that we feel we have a duty to raise. In particular, we feel that this is an aspect that the competition authorities should address.

7.2. People's consumption habits change with age. This is true of both the goods and services people buy and the places in which they buy them. Some of the changes are connected with preferences and needs, and others are dependent on circumstances.

7.3. The circumstances are frequently economic in nature, the obvious example being that the scale and source of incomes varies with age. Also, of course, retired people have more leisure, and may demand more leisure goods. But it is important not to ignore the change in non-economic circumstances, such as the probability of living with dependants, or of being dependent on others. Above all, of course, average health status deteriorates with age, although most older persons remain fit and active.

7.4. The subject of age discrimination in retail markets was raised by representatives of Age Concern (Q292), who referred to the difficulties that older persons experience in hiring cars, and argued that those difficulties were the result of discrimination. They also referred to insurance companies whose premiums for homes and their contents are set too high for older, poorer people. Age Concern has worked to rectify this failure of the market, and has successfully entered the insurance market (QQ293, 296). Age Concern also said that firms that sell products such as information technology equipment and motor cars rarely address their designs or their marketing at older consumers. Its representatives claimed that businesses do not fully recognise the purchasing power of older people and exaggerate the risks involved in selling to them in the case of, for example, travel and motor insurance, and therefore forgo possible profitable sales.

7.5. A particular problem that confronts some older people is the location of shops. To the extent that shops are concentrated in places that require access by motor cars, this will produce difficulties for those who can no longer drive, and will make them dependent on others. The problem is exacerbated if in rural areas, for example, local shops are disappearing and public transport is infrequent or non-existent. Supermarkets often sell a wider range of products at lower prices than independent high street shops, and in so far as older people find access to out-of-town supermarkets difficult, they are likely to face a higher overall cost of living than that of the population at large. Given the restricted mobility of some older people, a matter of greatest importance to them is the possible disappearance of local retail pharmacies, to be replaced by pharmacies in supermarkets.

7.6. References to these problems are to be found in the Competition Commission report *Supermarkets* and the Office of Fair Trading report *The control of entry regulations and retail pharmacy services in the UK*. The Competition Commission took evidence from Age Concern, and states: "A decline in smaller retail outlets serving a local community could be especially detrimental to elderly people, some of whom may rely on them for a lifeline of interaction … We raise elsewhere in this chapter a number of supermarket practices that bear on access to groceries by low-income and elderly consumers".[81]

7.7. The OFT report on pharmacy services recommended that the control of entry regulations for community pharmacies should be ended.[82] Objections were raised to easing entry on the grounds that doing so might reduce the viability of high-street pharmacies and adversely affect older people. The Government rejected the full thrust of the OFT's recommendations, saying in a parliamentary statement: "We do not believe that simple deregulation is the best way to achieve our aims. The OFT made a strong case that the current control of entry rules impede competition and reduce benefits for consumers. But given the current shortage of pharmacists, which will persist for some years until measures which we as a government are taking increase supply, and the Government's desire to see pharmacies given a new and strong role in the modern NHS, the Government does not believe that this is the time to move to a fully deregulated system. It therefore intends to move cautiously in the direction recommended by the OFT."[83]

7.8. Because we have not explored these questions in the detail they deserve, we do not make any substantive recommendations relating to them. Instead we draw the attention of the Office of Fair

[81] Competition Commission, *Supermarkets* (2000), Volume 2, p 311, and Volume 1, p 55

[82] Office of Fair Trading, *The control of entry regulations and retail pharmacy services in the UK* (2003), p 6

[83] Parliamentary statement on community pharmacies, July 2003, www.dti.gov.uk

Trading and the Competition Commission to the possible existence of discrimination and market failure as it affects older people.

7.9. One last example of apparent market failure which arises in the public sector relates to the age limit on the availability of student loans. Presumably the age limit is based on the assumption that entrance to higher education must be judged in narrow economic terms, and is not valuable in its own right. It is perhaps assumed that older undergraduates and post graduates will not re-enter the labour force and earn an income high enough to repay the loan. Such an assumption is contrary to the Government's stated policy goal of increasing the economic participation of older persons. Furthermore, it should be noted that younger age groups also contain people who will neither re-enter the labour force nor earn enough to repay the loan.

7.10. **We conclude that the restriction of student loans to people below the age of 54 is blatant discrimination.**

7.11. **We recommend that the Department for Education and Skills should explain why age discrimination exists in the provision of student loans.**

CHAPTER 8: AGEING AND RETIREMENT I: INDIVIDUAL AND HOUSEHOLD CIRCUMSTANCES

Introduction

8.1. The structure of British society has experienced fundamental change since the National Insurance system was introduced in 1948. That system, which was based on the social insurance model proposed in the 1942 Beveridge Report, was premised on a world in which:

- cohabitation and divorce were rare
- family units consisted of a working husband, a non-working wife and dependent children
- men were in full-time employment between leaving school and retiring at age 65
- immigration was minimal, and thus all (male) workers could be expected to accumulate a full NI contribution record across their working life

8.2. That world, if it ever existed, certainly exists no more. This chapter considers the way in which the very different social and economic context of the early 21st century poses new challenges with respect to the financing of retirement and old age. Particular attention is paid to the economic and social circumstances of women and ethnic minorities.

Women

8.3. Most pensioners are women; thus an effective economic regime for retirement will be one that fully accommodates and responds to the fact that women's life histories, in terms of work and caring responsibilities, are on average different from those of men. We agree with Ms Jeannie Drake (Equal Opportunities Commissioner) that a pension system that fails women is one that must be judged to fail in its overall performance (Q487).

8.4. Women pensioners are more likely than men to be poor because of:

- greater longevity
- lower earnings during work
- fewer years in employment
- more years in part-time employment when in work
- less access to occupational pension schemes
- more retirement years lived as single people [84]

8.5. Changes in women's employment patterns and earnings means that it is likely that women with high educational qualifications and earnings potential will in the future retire with pension entitlements close to those of men, even if these women have children. Women with mid or low-level qualifications will continue to accumulate much lower pension entitlements, and having children will continue to have a strong negative impact on their pension accumulation.[85] Improvements to women's employment opportunities and relative pay will help to reduce the male-female pensions gap, but it is likely to remain large.[86]

8.6. The most important cause of women's low pension accumulation is the time they spend out of the labour market (or in part-time employment) in order to provide care for family members (children, sick, disabled and elderly). The contribution-based nature of the basic state pension means that people who do not have a full contribution record cannot qualify for a full basic pension. Fifty per cent of those currently in retirement do not qualify for a full basic state pension in their own right (Q398). Dr Jay Ginn (Centre for Research on Ageing and Gender, Sociology Department, Surrey University) noted that carers (whether male or female) are entitled to carer credits within the state pension system, but that such credits do little or nothing to lift such persons above the means-tested income threshold in retirement, because the basic state pension to which the carer credits contribute is paid at such a low level (Q390).

8.7. A further problem with the existing system of carer credits is that to receive the credit for care other than for a child, the recipient has to demonstrate that the need for care is sufficiently severe to

[84] Equal Opportunities Commission, volume II, p 175; WBG/Fawcett Society, pp 131-132

[85] Joshi, volume II, p 139

[86] EOC , volume II, p 176

require the payment of a care or attendance allowance. Professor Heather Joshi noted that there is a great deal of caring activity which lowers people's earnings, but which falls outside of the strict qualifying criteria of the carer credit (Q393).

8.8. **We conclude that the contribution basis of the basic state pension acts as a significant barrier to the acquisition by women of full state pension entitlements.**

8.9. It would be possible to remedy this problem through a more extensive and more sophisticated system of carer accountancy, but we think there is little to be gained by further complicating an already complex National Insurance contribution system. In fact, we see little purpose in this contribution system, which appears to be a now largely dysfunctional legacy of the post-war Beveridge welfare plan.

8.10. Virtually all citizens make positive contributions to the economy and society through their paid and unpaid work in the period between the end of their formal education and their retirement. The Government's success in operating an active labour market policy to extend employment opportunities to all groups and ages within the population means that few people can now shirk their responsibility to contribute positively to the economic welfare of the country. Thus there seems little reason to operate a complex accounting system to track NI contributions and credits over each persons working life in order for them to qualify for a full or partial basic state pension which, in any case, will be supplemented in retirement by means-tested benefits for between a half and three-quarters of all retirees (see paragraph 10.19 below).

8.11. **We therefore recommend that the basic state pension should be paid on the basis of citizenship rather than contribution record.**

8.12. Many current women pensioners and older women workers have relied on their husbands/partners to make appropriate pension provisions. The financial position of this group needs to be protected, even as pension provision for the future shifts over to an individualised basis (Q487). We believe that our recommendation of a shift to citizenship-based entitlement will do much to protect and enhance the interests of current women pensioners who have derived rather than individual pension entitlements.

8.13. A citizenship pension will also serve, to some degree, to protect the income in retirement of divorced women, but the impact of divorce on pensions extends well beyond the scope of the state pension. The United Kingdom has the highest divorce rate in the EU, and it is estimated that four out of every ten marriages entered into in the United Kingdom in 1996 will end in divorce. Few retirees have yet experienced old age as divorcees, but the proportions are growing.[87]

8.14. The Welfare Reform and Pensions Act 1999 now allows courts to share pension entitlements on divorce. We received evidence from Debora Price, a barrister, which suggested that this law may have little impact on the pension entitlements of most women, for two separate reasons. First, even if pension entitlements are split on divorce (and since this is enabling legislation, there is no legal requirement for judges to consider the retirement prospects of both parties), the value of such entitlements at the median age of divorce (late 30s) is typically low. Secondly, divorced women have a low probability of participating in pension accumulation after divorce because they frequently have young children to care for.[88]

8.15. We recognise that the issue of pension splitting on divorce is complex, and we believe it warrants further detailed consideration. We also recognise that the prevalence of long-term cohabitation also poses issues for the allocation of pension entitlements (Q422). We believe that these are issues that have important implications for gender equality, and thus may fall within the remit of the Equal Opportunities Commission.

8.16. An additional issue of gender equality relates to the market for annuities. The purchaser of an annuity makes a lump-sum payment to the provider (an insurance company) in return for a guaranteed income stream. Since older women can, at any age, expect to live for more years than men, they have to pay a larger lump sum for any given income stream, since they are likely to receive that income for longer. Some witnesses argued that higher annuity costs for women at any given age amount to discrimination. It was pointed out that although there is a clear sex differential in survival rates at 65, there are also clear differentials by socio-economic class, ethnicity, education and occupation, yet these categories are not used to determine annuity rates (QQ432-5, 511).

8.17. The issue of whether annuity rates should continue to be gender specific, or whether they should be provided on a gender-neutral basis, is of growing significance, because the rapid move of

[87] Debora Price, volume II, p 467

[88] Ibid, p 470

occupational pension schemes from defined benefit to defined contribution principles means that many more retirees in the future will obtain their private pension income from an annuity (Q511).

8.18. Furthermore, defined benefit pension schemes offer survivor benefits for dependents (most frequently paid in the form of a widow's pension), whereas most annuities are purchased on a single-life basis, which means that when the annuitant dies, there is no continuing income for any dependent (Q505). It is unclear whether married couples realise the implication for surviving dependents of single-life annuities. The Fawcett Society and Women's Budget Group suggested that when an annuity is purchased by a married person, it should normally be a joint-life annuity unless the non-purchasing spouse explicitly agrees to the purchase of a single-life annuity (Q431).

8.19. We recognise the importance of these criticisms of the way the annuity market currently operates, but we are wary of suggesting any changes which might be seen as imposing greater costs on this market. We agree with the Equal Opportunities Commission that the whole area of gender and annuities requires further investigation and analysis.

Minority ethnic communities

8.20. Public and private pension entitlements among minority ethnic elders are low. This is a function of:

- the impact of immigration on the number of years of contribution
- high levels of unemployment
- low wages
- high rates of participation in the informal economy
- cultural norms which prioritise intra-familial resource sharing rather than individual accumulation.[89]

8.21. Although the low income of today's minority ethnic elders is largely the result of the specific labour market experience of this cohort, the current high rates of unemployment and low skills among younger members of some minority ethnic groups (especially black and Pakistani/Bangladeshi) makes it likely that low pension entitlements will endure well into the 21st century for new cohorts of retirees.[90]

8.22. The problem of unemployment and low earnings is compounded by a lack of targeted information about long-run saving. According to the Policy Research Institute on Ageing and Ethnicity, "the financial services sector does not currently connect with the ethnic minority community."[91] However, PRIAE pointed out that the DWP is now developing information on state pensions that is specifically targeted at minority ethnic communities, particularly in response to concerns about the low take-up of means-tested benefits by minority ethnic elders (QQ536-42).

8.23. In general, minority ethnic elders are much more likely to be in receipt of means-tested benefits than are white elders. Data for the period 1991-96 suggest that, whereas one third of white people aged 60+ were in receipt of means-tested income support, 45 per cent of Indian, 58 per cent of black Caribbean and 76 per cent of Pakistani and Bangladeshi elders received means-tested income support.[92] Our proposal for a basic pension based on citizenship rather than a full NI contribution record would significantly improve the economic position of these ethnic elders.

8.24. A citizenship pension could also be designed to ensure that current and future immigrants who, because of their age on arrival, cannot accumulate a full NI contribution record, would qualify for an adequate basic pension without the need for a means test. We believe that this would provide a significant incentive for such people to accumulate additional voluntary savings.

[89] CRE, volume II, p 194; PRIAE, volume II, p 198

[90] PRIAE, volume II, p 200

[91] Ibid, p 198

[92] Ibid, p 201

CHAPTER 9: AGEING AND RETIREMENT II: PRIVATE RESOURCES

Introduction

9.1. This chapter examines the variety and extent of private opportunities to accumulate financial resources for retirement. The Government have emphasised the importance of creating a simple and secure environment in which individuals can exercise choice about how much to save for their retirement. We review evidence submitted to the Committee which raises questions about the extent to which the Government's aspirations for an increase in voluntary pension saving are likely to be achieved.

Opportunities for private provision for retirement

9.2. Saving for retirement is currently a matter of individual choice, beyond the compulsory contributions to the National Insurance scheme, and to the State Second Pension or an appropriate contracted-out pension scheme. Payment into an occupational, personal or stakeholder pension is the most common means of making additional financial provision for retirement. However, people may save for retirement in many different ways, including buying their home or investing in their business.[93]

9.3. Use of home equity to finance retirement is still unusual in the United Kingdom, despite the substantial resources tied up in owner-occupied housing (over 59 per cent of persons aged 35-59 own a house worth more than £100,000).[94] One reason for the low take-up of equity release is a lack of consumer confidence in the products being sold (Q734-5). The FSA told us that equity release provided through a lifetime mortgage will come under FSA regulation from 2004, but that equity release through home reversion plans will remain outside the FSA's regulatory remit.

9.4. **In order to strengthen consumer confidence in equity release products, we recommend that all such products be brought within the FSA's regulatory jurisdiction as soon as is practicable.**

9.5. Pension plans are the most popular means of saving for retirement, but this type of saving may not be appropriate for all people, either because of their life-cycle stage or their low level of income. Although there are clear financial benefits in commencing pension saving at a young age, many people in their 20s and 30s face significant levels of debt repayment (because of previous periods of study, or property purchase) and experience increased expenditure with new family responsibilities; thus their financial capacity for retirement saving may be severely circumscribed.[95] The saving capacity of people on relatively low incomes is also likely to be limited.[96] Furthermore, evidence from the Actuarial Profession suggests that, on the basis of the current UK pension regime, for persons earning below about £20,000 per annum the rate of return on any additional pension savings they make may be very low (Q965).

9.6. The majority of people not currently saving explain their behaviour in terms of a lack of spare money. Some of these face binding financial constraints; others value current consumption more highly than the future consumption which their savings will permit. The prospect of more means-testing in old age, and the recent experience of poor returns on equities, serves to shift preferences towards current consumption and away from saving.[97] A survey conducted in 2002 by the Consumers' Association revealed that 65 per cent of respondents thought they were not saving enough for a comfortable and secure future, or were unsure as to whether their savings were adequate, but the great majority of that 65 per cent said that they could not afford to save more.[98]

9.7. A rising level of consumer indebtedness is a further barrier to pension saving (Q454). Average personal debt has grown at almost double the rate of average earnings over the past decade, and, according to the Financial Services Authority, 6.1 million families have some difficulty meeting debt repayment.[99]

9.8. The Government encourage pension saving by the provision of tax incentives. According to estimates produced by the Pensions Policy Institute, tax relief on private pension contributions

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[93] Actuarial Profession, volume II, p 340

[94] DWP, *Simplicity, security and choice*, p 156

[95] WBG/Fawcett Society, volume II, p 133; EOC, volume II, p 178

[96] TUC, volume II, p 115

[97] Association of British Insurers, volume II, pp 247-8

[98] Consumers' Association, volume II, p 163

[99] Ibid

currently amounts to about 1.5 per cent of GDP, and much of this tax relief benefits higher-rate taxpayers (Q918). However, the overall tax treatment of pensions is broadly neutral over time, since the tax relief on pension contributions is balanced by the tax levied on pensions paid out.[100] We note, however, that the tax-free lump sum represents an exception to this general principle of tax neutrality (QQ845, 848). Since there is no requirement for the tax-free lump-sum to be used to provide an income stream in retirement, this particular tax advantage does not appear to be an efficient way of encouraging individuals to make private financial provision for their retirement.

9.9. **We therefore recommend that the Government should consider phasing out over time the tax-free lump sum.**

9.10. The Government are committed to sustaining and expanding the voluntary basis of pensions savings and to maximising choice within this voluntary savings regime (Q1114). In 1998, the Government expressed their desire to expand voluntary pension provision, in order to shift the source of retirement income over the next fifty years from a public/private ratio of 60:40 to one of 40:60; this implies a more than doubling of the relative contribution of private resources to total retirement income. The Secretary of State for Work and Pensions suggested that this ratio should be seen more as an indicator of the desired direction of change, rather than as a specific target, since it is not wholly within the Government's power to determine this ratio; much depends on private economic behaviour (Q1123).

9.11. Notwithstanding the Secretary of State's downgrading of this ratio from a target to an "aspiration" (Q1123), it is clear that for the Government's goals to be met, private provision for retirement will need to increase substantially above current levels. We received evidence from Mr John Hawksworth (Head of Macroeconomics, PricewaterhouseCoopers) which suggested that, although the level of private pension income as a share of GDP is likely to rise over the next four decades, it will do so more slowly than the rate at which the population aged 65+ is expected to increase (Q243). Projections of this sort are always subject to a wide margin of error, but we are concerned that the Government's objective of a substantially higher level of private pension saving may not be attained. A shortfall in anticipated financial resources in retirement could have a negative impact on the welfare of future retirees, and also on public finances if some future Government were called upon to fill the savings gap.

9.12. We have therefore given some consideration to the conditions under which we believe a voluntary savings regime is likely to be successful. We believe that for voluntarism to succeed, it is necessary that individuals have:

- adequate information to make informed choices
- adequate access to appropriate savings instruments
- an ability to make coherent and consistent long-term financial plans
- an ability to adhere to such plans once made

9.13. We are unconvinced that these conditions apply to a sufficient degree to support the desired expansion of private pension savings within the United Kingdom. We note with approval the plans the Government set out in last December's pensions Green Paper to increase understanding and knowledge of pension savings.[101] We also recognise that the Government are far from complacent with respect to these issues: the Secretary of State for Work and Pensions agreed that the Government have "a long way to go" in their information campaign with respect to pensions (Q1111). We nevertheless believe that the Government can and should do more to create a more supportive environment for voluntary pension savings.

9.14. A fundamental requirement for coherent pension planning is that individuals should have full information about the way in which private pension systems work, about how they are financed, and about the cost of alternative pension outcomes. We received consistent evidence from employer organisations and actuaries that members of occupational pension schemes have "no concept of how valuable their pension is" (Q948), give little consideration to the value of pension benefits when they are involved in job search (Q592), and only begin to consider the details of their membership once they reach their mid-40s (Q632). This implies that a large segment of the labour market is characterised by potential inefficiency: workers who do not take account of the non-wage element of their remuneration package may select sub-optimal employment; and employers who make substantial

[100] Actuarial Profession, volume II, pp 340-1; p 344

[101] DWP, *Simplicity, security and choice*

contributions to their workers' pension schemes may not benefit from this non-wage expenditure in terms of enhanced recruitment and retention of employees.

9.15. The Government have advocated the issuance of an annual "total benefit statement" by employers to help employees recognise the value of employer pension contributions.[102] While this is a laudable aim, it may also have considerable cost implications for employers. A simpler option would be to include employer pension contributions on pay slips, and to explicitly state the value of employer pension contributions in all salary calculations, whether on pay slips or in job advertisements. We believe that this would facilitate rational decision making on the part of workers engaged in job search, enhance awareness of the value of employer pension contributions, and encourage take-up of pension scheme membership.

9.16. **We therefore recommend that the Government set an example by explicitly including information on the value of employer pension contributions in pay slips and in recruitment material for all public- sector jobs. We further recommend that a timetable be established for extending this practice to private-sector employment.**

9.17. A further barrier to private pension saving is a perceived difficulty in obtaining unbiased financial advice.[103] Many consumers believe commission-based advice is biased, but there is a reluctance to pay up-front fees. The Government have made it clear that they would like employers to take a role in providing information on pension planning to their staff.[104] However, a number of witnesses noted that FSA rules relating to financial advice serve to prevent employers from taking on this role (QQ464, 674, 742).

9.18. The FSA acknowledged that its rules governing the provision of financial advice are a major barrier to the effective provision of detailed pensions advice by employers, and pointed out that it is working with DWP to develop an employer information pack (QQ868-875). We were persuaded by the argument that many workers would rather receive advice about pension planning from their employer, with whom they are likely to have a long-term economic relationship, than from an itinerant financial adviser.

9.19. **We conclude that the Government's policy goal of encouraging the delivery of more financial advice to individuals via the workplace is to a significant degree frustrated by the Government's policy goal of ensuring that financial advice is provided according to FSA rules.**

9.20. **We recommend that the Government, in co-operation with the FSA, take action to resolve this conflict of policy goals in order to facilitate the provision of financial advice by employers and make clear the basis on which employers may provide advice, without lowering standards.**

9.21. A huge variety of products is available in the private pensions market, provided by a large number of suppliers, but we received evidence from a number of witnesses to suggest that this variety does not necessarily ensure adequate access to appropriate savings instruments. The Consumers' Association drew attention to the conclusion of the Sandler report that competitive forces in this market do not always work effectively to deliver value (Q465).[105] Professor David Blake pointed out that there is a trade-off between cost and choice. The multiplicity of personal pension schemes means that they cannot reap economies of scale, and thus on average their annual administrative costs are four times higher than for a typical final salary occupational pension scheme, and 14 times higher than the state pension scheme (Q225).

9.22. Professor Blake further argued that the choice offered by many pension schemes is the wrong sort of choice. Suppliers tend to offer choice about the internal structure of a pension plan, such as the type of fund in which to invest, whereas the key choice, in terms of the ultimate value of the pension, is over what rate of contribution to pay into the scheme (Q226).

9.23. The Consumers' Association suggested that collective pension schemes, such as the industry-based schemes that are common in the Netherlands, or the US Federal Thrift Savings Plan, could provide a more efficient and appropriate mechanism for personal pension saving, especially for low income individuals, than existing products available in the United Kingdom (including stakeholder pensions) (Q478).

102 DWP, *Simplicity, security and choice*, p 71

103 Consumers' Association, volume II, p 163-4

104 DWP, *Simplicity, security and choice*, p 73

105 Ron Sandler, *Medium and Long-Term Retail Savings in the UK: A Review* (HM Treasury, 2002)

9.24. We note that some progress is being made towards the development of a suite of "simple and comprehensible" long-term saving products, as recommended by the Sandler review.[106] However, an additional barrier to higher levels of private pension saving is the loss of trust in private pension providers that has resulted from the recent decline in equity values, a number of mis-selling scandals, and the collapse of Equitable Life (Q 261-2, 460).[107]

9.25. **We believe that there is a role for Government in providing a simple, secure and guaranteed long-term savings instrument which can be used by lower-income individuals who do not wish to expose themselves to the costs and risks involved in purchasing a commercial pension product. We recommend that the Government provide such a product, in the form of a pensions bond with a real rate of return linked to the economy-wide growth rate and administered by National Savings.**

9.26. Better information, and better access to appropriate saving products, will help individuals develop coherent long-term saving strategies only if they can make sense of the information they are given. Many people appear to have quite unrealistic expectations of their pension future. A survey carried out by the Consumers' Association in 2002 found that on average respondents wanted to retire at 58 on a pension equal to three-quarters of their final salary, yet 46 per cent of them were not contributing to a pension at the time of the survey.[108] The FSA noted that most of the population find long-run financial planning "incomprehensible and deeply dull" (Q866). Although this attitude is in some cases the result of financial illiteracy, many otherwise financially literate people prefer to postpone any serious consideration of pension savings until middle age. As the example in Box 3 shows, such a decision has a huge impact on the required contribution rate.

Box 3

Required contributions into a pension scheme

The contribution rate required to generate any given level of pension rises steeply with the age at which saving begins, for two separate reasons. First, if contributions are postponed, there are fewer years of contribution available to finance a given period of retirement. Secondly, contributions accumulate compound interest for a shorter period of time.

The following example has been provided by Professor David Blake, and is based on a model in which a defined-contribution pension of two-thirds of final salary is provided at age 65.[109]

Starting age	25	35	45	55
Male contribution rate (% of salary)	17	24	37	72
Female contribution rate (% of salary)	19	27	42	84

The required contribution rate (as a percentage of salary) is higher for women than men, because women have a higher life expectancy at age 65, and thus need to accumulate a larger capital sum to support a given level of pension.

This example is based on the plausible assumption that the long-run rate of growth of real earnings is 2% p.a., and the rate of real return on assets is 3% p.a. Small changes in these assumptions would alter the required age-specific contribution rates, but would have little impact on the relativities between contribution rates at different ages.

9.27. A further barrier to increased pension saving is that pension products are inflexible, since they offer little or no liquidity during the accumulation phase; thus they diminish the opportunity for flexible financial planning during the working phase of the life-course. Since taxation of pensions is broadly neutral, the incentive to save via a pension product rather than, say, an ISA, is slight. Continuing change to historic patterns of household formation and dissolution (noted in chapter 8 above), together with the further development of labour market flexibility, increase the potential cost

[106] DWP/Treasury, *Proposed product specifications for Sandler "stakeholder" products: Consultation document* (February 2003)

[107] Actuarial Profession, volume II, p 341

[108] Consumers' Association, volume II, p 163

[109] Professor Blake, volume II, p 60

to an individual of allocating a major part of total financial savings to a product that cannot be accessed until some fixed date in the future.

9.28. A number of witnesses argued that, given these problems relating to information about, access to and public understanding of long-term pension savings, it is unlikely that the scale of voluntary pensions savings will rise at the rate desired by the Government, and that therefore compulsion would be necessary (Professor Blake: QQ 214-5); Consumers' Association: Q471; Equal Opportunities Commission: Q487). Other witnesses, while often recognising the barriers to more extensive voluntary pension provision that exist within the United Kingdom pension regime, strongly opposed compulsion. Mr Gordon Lishman (Managing Director, Age Concern) noted that compulsion is "a blunt instrument" which might adversely affect young people who could be better served by paying off debt or investing their disposable income in developing their qualifications (Q317). Professors Booth and Disney noted that there is a strong economic argument for enough compulsion to take an individual off means-tested benefits, since otherwise non-savers can deliberately impose the cost of their non-saving on others (that is, taxpayers), but that there is little economic sense in imposing compulsion beyond that point (Q821).

9.29. Professors Booth and Disney also suggested that discussion of the role of compulsion in pension savings should not focus on issues of principle, but on details of practice, since the United Kingdom already imposes compulsory pension savings on all contributors to the National Insurance system. These contributions (to the basic state pension, and to either the state second pension or to an approved contracted-out pension scheme) currently amount to around 8 per cent of earnings (Q821).

9.30. The Secretary of State for Work and Pensions agreed that there already exists "significant compulsion in the system", but he also expressed the view that further compulsion should not be viewed as a panacea for the perceived problem of under-saving (Q1113). He pointed out that the Government had appointed an independent Pensions Commission, chaired by Adair Turner, to monitor the scale of voluntary pension savings, and to determine whether there might be a case for moving beyond the present voluntary system.

9.31. We are concerned that current levels of voluntary pension saving in the United Kingdom are too low to generate the levels of retirement income that working people say they expect to receive in the future, and we recognise that more compulsion could help to close this savings gap. On the other hand, we recognise the force of the argument that compulsion distorts the market, and imposes unnecessary costs on some individuals. Given the high and growing degree of means-testing among the pensioner population, we think it likely that an extension of compulsory pension savings might particularly disadvantage lower-income individuals who would receive extremely low returns from their additional pension saving.

9.32. **On balance, therefore, we conclude that a general extension of compulsion in pension savings should be avoided. However, that requires the Government to take action to provide a higher minimum state pension. We discuss this issue further in chapter 10.**

Uncertainty and private pensions

9.33. We received a considerable amount of evidence relating to the growing degree of uncertainty surrounding the outcome of private pension saving. This concerns us for two reasons. First, uncertainty of outcome is likely to make individuals less enthusiastic about committing their long-run savings to a pension scheme; thus uncertainty tends to exacerbate the problem of under-saving. Secondly, uncertainty of outcome in the private pension sector indirectly places a greater burden on the state pension to provide a guaranteed income in retirement.

9.34. The uncertainty of defined contribution private pension outcomes has become more obvious in recent years because of the sharp decline in equity prices and adverse movement in annuity rates. This uncertainty is exacerbated by the separation of the accumulation and decumulation phases of a private pension: the accumulation phase is frequently undertaken by a different company from that which manages the decumulation phase via the sale of an annuity (QQ208, 726).

9.35. We note that some of the popular concern about the recent decline in annuity rates fails to appreciate that this is in part the inevitable result of the welcome improvements in life expectancy at older ages discussed in chapter 2 above. Furthermore, some of the concern derives from "money illusion": annuity rates would be higher if inflation and nominal interest rates were higher, but annuitants would be no better off in real terms. The Government's success in generating an economic environment of low and stable rates of inflation and interest is, in general, beneficial to the pensioner population, since low inflation preserves the capital value of savings.

9.36. We recognise, however, that popular concern about the uncertainty of investment returns and annuity rates is compounded by a widespread lack of trust in the financial services industry. Mr John Hawksworth (PricewaterhouseCoopers) explained that many people "feel they have been sold things so someone can make commission, so that somebody can meet their sales target for the month rather than because there is any kind of commitment to actually delivering the product" (Q262).

9.37. We believe that the financial services industry needs actively to rebuild a relationship of trust with purchasers of its products, and that in so doing it should seriously analyse the extent to which trust and consumer confidence can be made compatible with commission-based selling. As noted in paragraph 9.18 above, we believe that consumer confidence in pension products would be increased if advice on these products could be delivered more effectively through the workplace. We note, however, that workplace-based advice cannot reach that large number of adults, primarily women, who at any one time are not engaged in paid employment (Q487). We recognise the merit of the suggestion by the Consumers' Association that such persons might best be served by a community-based national financial advice network (Q461).

9.38. **We recommend that the Government explore with the voluntary sector and the financial services industry the possibility of developing a national financial advice network for low-income individuals.**

9.39. Defined benefit occupational pensions can provide more secure pension outcomes than defined contribution schemes, because the employer carries much of the downside risk of inadequate investment returns. However, it is clear that many employers have already decided to limit the extent of this risk by closing their defined benefit schemes to new members, or by winding them up. Evidence from the Engineering Employers' Federation, the National Association of Pension Funds, and the Actuarial Profession indicated that an important factor has been regulation which has converted what were hitherto discretionary benefits relating to indexation and survivors' pensions into guarantees. This regulation, while providing improved benefits for members, has served to increase the cost to employers of providing defined benefit pensions by anything up to 40 per cent, and has removed from them discretion over the level to which they fund their pension scheme (QQ 592, 642, 665, 943).

9.40. Opinion is divided as to whether there is a future for defined benefit occupational pension schemes. One view is that a growing perception among shareholders of the cost of defined benefit pensions, and among managers of the slight advantages such schemes convey in terms of retention and recruitment, means that the drift away from defined benefit pensions will gather speed. Mr Ronnie Bowie (Senior Partner, Hymans Robertson), giving evidence on behalf of the Actuarial Profession, was of the opinion that that recent decisions by the Government to further restrict employer discretion over the winding-up of schemes would seal the fate of defined benefit pensions (Q943). Mr Terry Faulkner (Chairman, National Association of Pension Funds) reported that in a recent survey of 255 finance directors, 41 per cent reported that their final salary defined benefit pension scheme had been closed to new members in the last year, and that only around one fifth of such schemes are now open to new members (Q642). He thought that many more defined benefit schemes were likely to close in the future, particularly now that internal decisions about company pension schemes are driven more by issues of corporate finance than those of human resource management (Q643).

9.41. An alternative view, proposed by the Government, is that a reduction in regulatory and compliance costs will stimulate growth in employer provision. The Secretary of State for Work and Pensions told us that the Government's proposed simplification of the taxation and regulation of occupational pensions would "encourage companies to continue running good schemes and to start new schemes" (Q1113). He further pointed out that a "good" occupational pension scheme could equally be based on the principle of defined contribution or defined benefit (Q1109).

9.42. **We conclude that the proposed reform to the regulatory and tax environment of occupational pensions will come too late to reverse, or even stem, the tide of closure of defined benefit pension schemes.**

9.43. This concerns us, because, as noted by the Secretary of State for Work and Pensions, many employers use a shift from defined benefit to defined contribution pensions to reduce the level of their contributions to the pension scheme (Q1109).

9.44. **We further conclude that the closure of defined benefit pension schemes seems to be associated with a reduction in overall pension savings, which will have the effect of reducing the value of future pension entitlements.**

CHAPTER 10: AGEING AND RETIREMENT III: PUBLIC RESOURCES

Introduction

10.1. This chapter reviews the extent and nature of the public pension system in the United Kingdom. This system is extremely complex, and this complexity is seen to act as a significant barrier to public comprehension of pension issues. A major element of complexity relates to the extensive and growing use of means-testing to allocate pensioner income. This is seen as a significant barrier to the further development of voluntary pension savings. An additional impediment to voluntary savings is the uncertainty created by the lack of political consensus about the purpose and structure of the state pension system. We make recommendations to address each of these problems.

Complexity and uncertainty

10.2. The United Kingdom pension system is complex – arguably the most complex of any industrialised economy. The Basic State Pension (BSP) is provided to all persons above state pension age who have an adequate National Insurance (NI) contribution record. There is also a State Second Pension (S2P) which has replaced SERPS as a supplementary pension for low earners. Income from these sources may be inadequate to provide a minimum acceptable income, in which case the income guarantee element of the Pension Credit (PC) acts to top up pensioners' income, as do a range of other means-tested benefits. In addition, workers have the option of "contracting out" of SERPS/S2P, and instead putting their NI rebate into a personal pension (PP) of which there are 12 different types, or a contracted-out occupational pension scheme, of which there are 10 different types which can be either defined benefit (DB) or defined contribution (DC).[110] Employers who do not run occupational pension schemes are now required to offer Stakeholder Pensions to their workers. Pension professionals find this structure complex; non-experts find it impenetrable. In the words of Dr Deborah Cooper (Retirement Research Unit, Mercer Human Resource Consulting Ltd), speaking on behalf of the Actuarial Profession, "a huge obstacle to saving at the moment is not a lack of incentive, it is just the maze that you have to go through in order to make the decisions, and it is just too difficult. It is difficult for us to understand exactly what it all means so I dread to think what the ordinary lay person thinks" (Q962).

10.3. All independent witnesses were of the opinion that the complexity of the state pension system, and the complexity of the way it interacts with private pensions to produce a retirement income, creates a significant barrier to better and more widespread understanding of pensions issues among the United Kingdom population. This viewpoint was expressed by, amongst others, the Engineering Employers' Federation (Q595), the Confederation of British Industry (Q635), the National Association of Pension Funds (Q647), the Association of British Insurers (Q742), Age Concern (Q309), the Fawcett Society (Q408), the Financial Services Authority (Q896) and the Equal Opportunities Commission (Q518). We are extremely concerned to find that the Department for Work and Pensions and the Treasury appear not to recognise or give due attention to these widely and deeply held concerns about the complexity of the state pension system. It is striking that the commitment to a "simpler pensions framework" embodied in the 2002 pensions Green Paper[111] is confined almost wholly to simplifying the tax rules relating to private pensions (Q408).

10.4. We acknowledge the validity of the distinction drawn by the Secretary of State for Work and Pensions between the internal complexity of the rules of a pension system and the ease with which that system can be used by consumers (Q1119). However, we are disappointed to find that he does not seem to recognise the strength of the views of consumers, employers, and the pensions industry that the current pension system in the United Kingdom fails the test of "ease of use". Many of the concerns of users relate to the interaction between private sources of retirement income and the means-tested elements of the state system. We discuss this issue of means-testing in more detail below.

10.5. The problem of complexity which pervades the state pension system is compounded by the problem of uncertainty. Pension outcomes are inherently uncertain because pension provision involves very long run formal or implicit contracts, and long-run economic and political outcomes are subject to a wide variety of risks. However, uncertainty about the outcomes of the public pension system has been exacerbated by a lack of political consensus about pensions, which has led to major reform of the United Kingdom public pensions system at least once a decade since the National Insurance system was inaugurated in 1948.[112] Further uncertainty is generated by the sensitivity of the value of public pensions to technical issues such as indexation, which are not well understood among the general

[110] Consumers' Association, volume II, p 163

[111] DWP, *Simplicity, security and choice*, pp 37-9

[112] National Association of Pension Funds, volume II, p 233; PricewaterhouseCoopers, volume II, p 83

population. Thus, according to Dr Katherine Rake (Director, The Fawcett Society) many people "do not trust the state but they trust private pension providers even less" (Q451).

10.6. **We conclude that the state pension system is too complex to function effectively, and that the Government have taken insufficient notice of widespread concern about this complexity in their formulation of pensions policy.**

Purpose

10.7. Institutional and administrative complexity obscures the purpose of the state pension system. It is not clear whether it is supposed to offer a (semi-contractual) return to insurance contributions; or a system of income support and poverty prevention; or a (minimal) foundation for private pension accumulation. Elements of each of these intentions can be found in the existing public pension system. The requirement of a full National Insurance contribution record for full pension entitlement preserves Beveridge's concept of a contribution-based insurance system. The income guarantee element of the Pension Credit which is used to raise the income of the poorest pensioners to a subsistence level reflects a primary concern with poverty prevention. The facility for individuals to "contract out" of all but the basic state pension, together with the long-run decline in the value of this pension, which is expected to fall from 16 per cent of average earnings to just 6 per cent over the next 50 years, suggests that the state system is designed to do little more than provide a minimal (and increasingly residual) foundation for private long-term saving.[113]

10.8. The lack of clear purpose renders it impossible to determine an unambiguous set of criteria by which the level of the public pension, or the state pension age, or pension eligibility criteria, might be set. It is thus difficult to evaluate the desirability or otherwise of the Government's 1998 aim to shift the balance of public and private sources of income in retirement from 60:40 towards 40:60 (see paragraph 9.10 above).

10.9. It was suggested to us by Steve Webb MP that rather than set targets and evaluate achievements by reference to the broad source of retirement income, a more relevant criterion might be the proportion of people of working age who are likely to achieve an income in retirement that at least equals some agreed percentage of their pre-retirement income (Q1062).

10.10. While we do not wish to endorse any specific criteria for evaluation of the Government's overall pensions policy, we believe that such criteria should give due weight to the performance of the pension system in meeting the welfare needs and goals of individuals, as well as meeting higher level objectives relating to the funding mix.

10.11. This lack of a clear purpose to the state pension system also makes it difficult to impute any clear meaning to the concept of the "fiscal sustainability" of the pension system. According to evidence from the Treasury, a general measure of fiscal sustainability is a stable ratio of debt to GDP over time (Q92). However, the fiscal sustainability of the pension system appears to be interpreted by the Government as meaning a stable or slowly declining ratio of public pension expenditure to GDP, falling from 5 per cent today to 4.4 per cent by 2051 (QQ14-5). It should be noted that this decline in expenditure share is projected to occur over a period in which the proportion of the population above state pension age will rise from 18 per cent to 24 per cent.[114]

10.12. In the absence of clear criteria relating to the purpose of the state pension scheme, we cannot see why an expenditure share that rises in line with the increase in the size of the pensioner population, and the need to raise additional tax or national insurance revenue that this would imply, should be any less "fiscally sustainable" than the course the Government have mapped out. We make this point not because we believe that state pension expenditure necessarily *should* rise in line with population, but because the Government's use in this context of the term "fiscal sustainability" appears to us to be vacuous.

10.13. **We recommend that the Government produce a clear set of pension performance criteria which include indicators of the outputs of the pension system (present and expected future pensioner income) as well as the inputs to the system (the scale and source of pension finance). We further recommend that the Government's success in meeting these objectives be regularly monitored and published.**

10.14. Even less clear is the logic behind other age-specific public benefits such as subsidised or free travel on public transport. Baroness Greengross suggested that, as we move towards a society in which competence rather than age determines employability, and need rather than age determines

[113] ABI, volume II, p 249

[114] GAD, *National Population Projections, 2000-based*, pp 56-7

receipt of public resources, age-related benefits such as heating allowances, free television licences for the over-75s and the bus pass seem increasingly anachronistic (Q130).

10.15. **We recommend that the Government should provide an explanation of the rationale for the continuation of age-related benefits such as subsidised travel.**

Means testing and public pensions

10.16. Many witnesses identified the nature and extent of means-tested benefits for pensioners as a fundamental weakness of the United Kingdom public pension system. The primary means test until October 2003 applied to the Minimum Income Guarantee (MIG), which was the name used for income support for the over 60s. In October 2003 the MIG was replaced by the Guaranteed Income Top-Up of the Pension Credit. At least three separate problems with this system were identified by witnesses:

- The marginal tax rate faced by pensioners
- The number of pensioners subjected to this means test
- The difficulty of giving unambiguous financial advice to persons who may qualify for the Pension Credit

10.17. In 2003-04 the basic state pension for a single person was £77.45 per week, and the MIG was £102.10 per week. Under the MIG, any pensioners who received a non-state income of up to £24.65 per week saw no net benefit from this private income because their MIG was reduced pound for pound. Thus they faced a marginal tax rate on the first £24.65 of private pension income of 100 per cent. The Pension Credit was designed to remove the 100 per cent marginal tax rate. It does this by providing pensioners with a savings credit which is reduced at the rate of 40 pence per £1 of additional income, up to a total weekly income of £139 for a single person, and £203.80 for a pensioner couple. Thus pensioners with incomes in this range will now face a marginal tax rate of 40 per cent. However, Mr Graham Vidler (Policy Adviser, Association of British Insurers) pointed out to us that this 40 per cent marginal tax rate is a minimum. A pensioner who receives the savings credit but who also pays tax at the basic rate will face a marginal tax rate of 53 per cent, and if their receipt of the savings credit leads to withdrawal of housing benefit and council tax benefit the marginal tax rate could reach 93 per cent (Q743).

10.18. The Pension Credit has removed the absolute penalty of saving that was imposed by the MIG, but it still leaves pensioners who are on an income of barely 30 per cent of national average earnings facing a marginal tax rate that is otherwise reserved for persons earning over £35,000 per annum. The Rt Hon Frank Field, MP, pointed out to us that the impact of these high marginal tax rates on poor pensioners sends out a message that "under the present system it is not safe to save" (Q1055).

10.19. Because the savings credit element of the Pension Credit now extends further up the income scale than did the MIG, it affects more people. At the point of introduction, around 50 per cent of all pensioners became eligible for some means-tested income supplement under the Pension Credit. Because the savings credit element of the Pension Credit is likely to be indexed to earnings, the number of pensioners who will qualify for means-tested savings credit is expected to rise over time. The Government have estimated that 65 per cent of pensioners will qualify by 2050; Mr John Hawksworth (PricewaterhouseCoopers) provided us with an alternative estimate of 70 per cent coverage by that date, and noted that the Institute for Fiscal Studies has produced an estimate as high as 80 per cent. It is clear, therefore, that the means-testing of pensioners in order to provide them with a savings credit income supplement will become the norm.

10.20. Older pensioners are, and will continue to be, particularly prone to means testing, because income in retirement tends not to increase as fast as real earnings – largely because many private pensions, and the basic state pension, are indexed to prices. If a pensioner's income is indexed to prices, then after 20 years in retirement, their income is likely to be around 50 per cent lower than the income of a new retiree. This means many pensioners with incomes above the Pension Credit threshold on retirement will fall into the Pension Credit means-test during retirement (Q914).

10.21. It is very difficult to predict how the Pension Credit will affect any individual who retires in the future, for two reasons. First, there is uncertainty about how the various income and savings thresholds of the Pension Credit will be indexed. Secondly, there is uncertainty about how much pension income an individual's lifetime savings will generate if these are paid into a defined contribution pension, because this income will depend on long-term investment performance and on annuity rates at the point of retirement. This dual uncertainty makes it very difficult to provide unambiguous financial advice for that half to three-quarter of the population who are likely to be eligible for the Pension Credit during their retirement. FSA rules require that individual financial advice should be thorough and appropriate, but it is extremely difficult to provide such advice given the uncertainty of the way in which private savings may interact with the Pension Credit. Mr Peter Tompkins (PricewaterhouseCoopers) told us that "virtually all people in the industry would like to see the state bedrock pension taking people clear of means-testing, so that the advisory process can be simple" (Q248).

10.22. The Government appear to believe that the high marginal tax rate faced by Pension Credit recipients does not necessarily reduce the incentive to save. The Secretary of State for Work and Pensions noted that while the theoretical argument about the savings disincentive is clear, there is no empirical evidence to demonstrate that these tax rates in practice affect people's long-term saving behaviour, and therefore the Government have decided to initiate research on this subject (Q1117).

10.23. We are pleased that the Government are commissioning research in this area, but we believe that the disincentive to save comes not simply through the level of the marginal tax rate. Indeed, given the complexity of the Pension Credit system, we suspect that among current recipients few can calculate for themselves the marginal tax rate imposed on their savings, and among current workers almost none will be able to predict the marginal tax rate they may face in retirement. We concur with evidence from the Association of British Insurers that "the effect of means testing on the incentive to save is slightly more subtle than that, and it is mediated through people's vague awareness of the existence of means testing and in particular the way that that impacts on financial advisers' perceptions and the advice they can give" (Q743).

10.24. We also believe that people who are among the poorest in our society should not face marginal tax rates on their very modest private income in retirement that are at least as high, and in some cases considerably higher, than the tax rates faced by persons earning over £35,115 (the current threshold for the 40 per cent income tax band).

10.25. **We therefore conclude that the Government's heavy and growing reliance on means-testing the pensioner population is regrettable because it:**

- unduly penalises current pensioners who have struggled hard to provide a small private income for themselves in retirement
- sends a clear signal to many current workers that it is not in their interests to save for their own old age
- is unfair to tax some of the poorest members of our society at marginal rates as high as or higher than those imposed on the rich

10.26. Many witnesses suggested that the extensive means testing of the pensioner population should be avoided, and that this might best be achieved through the payment of a non-means tested state pension at a level around, or slightly above, that of the MIG (roughly 20-22 per cent of national average earnings). Age Concern (Q303), the TUC (Q353), the National Association of Pension Funds (Q675) and the Pensions Policy Institute (Q909) all supported some variant of this idea on the grounds that it would provide a simple, stable, and comprehensible foundation for additional private pension saving.

10.27. We find the arguments for a basic pension paid at or marginally above a minimum subsistence level compelling. Such a pension would permit the removal of the complex and costly apparatus of means-testing for pensioners, and would send a clear signal to workers that any saving they make during their working years will be theirs to keep and use during retirement. We believe that it will not be possible for the Government significantly to increase the scale of voluntary retirement saving unless and until it can make a credible commitment that it will not claw back this saving at a later date via a means test. We believe, however, that the state pension should continue to be treated as taxable income.

10.28. **We therefore recommend that as a top priority the Government should consider introducing a non-means-tested state pension paid on the basis of citizenship to all persons of pension age. We believe that the provision of this baseline state pension is a necessary element for the development of a more extensive system of voluntary pension saving in the United Kingdom.**

10.29. In addition to providing an adequate, simple and comprehensible pension for retirees, a non means-tested universal pension would enable the extremely complex system of "contracting out" to be abolished, thereby enormously simplifying the administration and regulation of occupational pension schemes.

10.30. We recognise that such a pension would have significant costs, and may have to be phased in over a number of years. There are many ways in which the costs of such a pension might be spread across current and future cohorts of workers, and it is not our place to determine a preferred path. We note, however, that in the short run it would be possible to remove some of the poorest and most vulnerable pensioners from means-testing by paying the basic pension at the level of the income guarantee to all pensioners aged 80 and above. The Rt Hon Frank Field, MP, Mr Steve Webb, MP and Mr David Willetts, MP, all persuasively argued the case for using age, rather than income, as the targeting mechanism (Q1055). The Pensions Policy Institute informed us that the cost of this would be in the region of 0.2 per cent of GDP (Q916). Though this is a non-trivial sum, if it is correct, it is small enough for this policy change to be introduced in the short run.

10.31. **We therefore recommend that the Government should expeditiously develop a fully costed proposal for the payment of the basic state pension at the level of the minimum income guarantee for all pensioners aged 80 and above.**

The concept of a "pensions crisis"

10.32. The concept of a "pensions crisis" has recently received a good deal of media attention, and it was explicitly analysed earlier this year by the Work and Pensions Committee of the House of Commons.[115] We believe that the concept of a general pensions crisis is too loose to have clear analytical meaning.

10.33. As noted in paragraph 3.7 above, we conclude that there is no general economic crisis of ageing in the United Kingdom now or in the foreseeable future. If there is a pensions crisis, it must relate not to the aggregate economic impact of population ageing, but instead to the specific institutional characteristics of the United Kingdom pension system.

10.34. It is clear that there is no crisis of affordability in the current United Kingdom public pension system. State spending on pensions in the United Kingdom is projected to remain at roughly its current level of 5 per cent of GDP to 2050, whereas the average across EU countries is projected to rise from 10 per cent to 13 per cent (QQ58, 918). However, the large size (relative to EU countries) of the private pension sector in the United Kingdom means that total United Kingdom expenditure on pensions is currently around 11.5 per cent of GDP, compared to 12.5 per cent for the EU average (QQ58-9).

10.35. Mr David Willetts, MP, questioned the reliability of the Government's projection that state expenditure on pensions in the United Kingdom will remain at or around 5 per cent of GDP for the next 50 years. We are not in a position to evaluate these different claims, but it is clearly important to establish reliable and consistent projections which are open to independent scrutiny.

10.36. We believe that there may be a crisis of adequacy with respect to pensions. The pensioner population is expected to rise substantially over next 50 years, and thus average state pension payments per pensioner must decline relative to per capita GDP if state pension expenditure remains at 5 per cent of GDP (paragraph 10.11). For pensioners to maintain their living standard relative to workers, private pension saving as a proportion of GDP must rise substantially (paragraph 9.10). However, short-run trends indicate that private pension saving is declining rather than rising (paragraph 9.24).

10.37. We believe that there may be a crisis of confidence about pensions. Mis-selling of financial products, the collapse of Equitable Life, the fall in stock market values and in annuity rates, and employer withdrawal from defined benefit occupational pensions has created massive loss of public trust in the financial services sector (paragraphs 9.36, 9.37). Frequent Government meddling with public pension arrangements has undermined confidence that public pension promises made today will be honoured in the future (paragraph 10.5).

10.38. We believe that there may be a crisis of incentives. The extension of means-testing to a majority of pensioners (via the Pension Credit) reduces the incentive to forego current consumption and make private provision for old age (paragraph 10.23).

10.39. As noted in paragraphs 8.10, 9.32 and 10.28 above, we believe that the best way to respond to the problems of adequacy and incentives is to develop an adequate, universal and simple basic pension, based on citizenship rather than contribution record, which will act as a foundation for an expansion of voluntary pension saving. However, we believe that the problem of a lack of public confidence in the United Kingdom pensions regime requires additional intervention. A number of witnesses, including Age Concern, the CBI, the Fawcett Society, the National Association of Pension Funds and the Association of British Insurers lamented the way in which, over the last 30 years, pensions have repeatedly become a political football, and have suffered from an excess of short-run

[115] Work and Pensions Committee, 3rd Report (2002-03): *The Future of UK Pensions* (HC 92-I), pp 8-10

political opportunism rather than coherent and stable long-run cross-party agreement (QQ 310, 448, 637, 708, 747).

10.40. We have been dismayed to see, in the latter stages of our enquiry, considerable differences emerging between political parties over the future direction of pension policy in the United Kingdom. With such evident disagreement between (and sometimes within) political parties over such crucial issues as the level of the basic state pension, the role of means–tested benefits for pensioners, and the desirability or otherwise of compulsory pension contributions, it is hardly surprising that many people appear to have deferred committing themselves to any long-term saving strategy. People accumulate pension assets and entitlements over 40 or more years of paid and unpaid work, and can expect to draw pension benefits for 20 or more years in retirement. A stable institutional environment is necessary for individuals to make coherent savings plans over such a long time period.

10.41. We believe that stability could be enormously enhanced by distancing state involvement in pensions from the immediacy of the political process. A number of witnesses suggested that an independent authority should be established to monitor and report on pensions policy, in a manner similar to that in which the Monetary Policy Committee of the Bank of England monitors and reports on the Government's economic policy with respect to inflation and interest rate targets (QQ273, 897, 924, 1076).

10.42. **We recommend that, in order to increase the level of consensus associated with long-run pension planning, the Government should establish an independent authority to monitor, undertake research and make recommendations on pensions policy.**

10.43. For an independent authority of this sort to operate effectively, it would be necessary to establish a clear set of criteria by which the performance of the pension system could be evaluated (hence our recommendation at paragraph 10.13 above). It would also be necessary to establish a much simpler state pension system in which the level of benefit is set relative to some clear criteria, rather than being subject to political interference and the complex workings of a means test (hence our recommendation at paragraph 10.28 above).

CHAPTER 11: CONCLUSIONS AND RECOMMENDATIONS

The future impact of immigration on population ageing

11.1. Although net immigration will tend, in the short run, to increase the relative proportion of younger persons within the population, it is neither appropriate nor feasible to attempt to counter the trend towards a more aged society in the United Kingdom through a manipulation of immigration policy (paragraph 2.17).

Reliability of population projections

11.2. The Government should, when publishing long-range population projections, or pension or other expenditure projections which incorporate population projections, always report the "funnel of doubt" created by the variance between high and low assumptions about mortality and other key demographic variables (paragraph 2.24).

Ageing and aggregate labour productivity

11.3. Population ageing does not pose a threat to the continued prosperity and growth of the United Kingdom economy; in this sense, therefore, there is no looming "crisis" of population ageing in the United Kingdom (paragraph 3.7).

11.4. This does not mean that the future growth of the economy is in any sense guaranteed; that depends on how we manage our economic resources. A failure, for example, to sustain historic rates of technological progress and productivity growth might drastically reduce future growth rates below those projected here. We conclude, however, that such risks exist independently of any demographic pressures on the economy (paragraph 3.8).

Ageing, inflation, saving and capital accumulation

11.5. Population ageing may affect savings, interest rates and capital accumulation, but its effect is likely to be small relative to the large range of other economic and political factors which determine the course of these economic aggregates (paragraph 3.18).

Participation rates below pension age

11.6. Official projections of future age-specific labour force participation rates are inconsistent with the Government's stated objectives and policy intentions of increasing the employment rates of older people (paragraph 4.12).

11.7. The Government should pay full attention to the need for their labour force projections and policy objectives to be consistent and compatible with each other, bearing in mind that each interacts with the other (paragraph 4.14).

Participation rates above state pension age

11.8. The Government should formally review the state pension age every five years in the light of trends in life expectancy beyond age 65, and in the light of their own desire to increase participation rates at older ages. Our own judgment is that the state pension age should be raised (paragraph 4.21).

Diversity in patterns of participation: regional effects

11.9. The Government should incorporate explicit targets with respect to older age employment in their Regional Economic Strategies and in the priorities they set for Regional Development Agencies (paragraph 4.27).

Diversity in patterns of participation: the impact of ethnicity

11.10. As part of the Government's evolving strategy for improving the position of ethnic minorities in the labour market, particular attention should be paid to the "double disadvantage" of age and ethnicity encountered by members of ethnic minorities aged over 50 (paragraph 4.32).

Explanations of early retirement: supply and demand

11.11. The Government should commission further research and analysis into economic inactivity among persons aged 50+, in order to produce a clear basis of evidence on which to build policies to promote higher rates of labour force participation among older persons (paragraph 4.47).

Age and work capacity: the impact of health status

11.12. The Government, employer and labour organisations should collect information and disseminate "best practice" guidelines on ways in which jobs and workplaces can be redesigned to facilitate the employment of older workers who have activity-limiting health status (paragraph 5.7).

11.13. Employers should actively evaluate and instigate the redesign of job tasks and workplaces in order to maximise the opportunity for retention and recruitment of older workers (paragraph 5.8).

Age and work capacity: the impact of education and skills

11.14. The Government and employers should work together to develop mechanisms to promote equal access to workplace training and life-long learning for workers regardless of their age (paragraph 5.17).

The relationship between age and job performance

11.15. We believe it is essential to improve knowledge of the relationship between individual age and worker productivity in order to provide a sound foundation for evidence-based policy. We therefore recommend that the Government commission research on the relationship between individual age and worker productivity in order to strengthen the evidential base for future policy initiatives in the area of older age employment (paragraph 5.26).

The extent of age discrimination

11.16. We conclude from the evidence available that there exists a significant degree of age discrimination in employment, and that this discrimination occurs throughout the economy and in both public and private sectors. (paragraph 6.14)

11.17. Few employers operate overtly ageist recruitment and retention policies (except in so far as they use fixed retirement ages). Age discrimination is frequently the unconscious outcome of an employer's more general human resource management policy and procedure (paragraph 6.15).

11.18. Ageism in public appointments, whether directed against those considered too old or too young, should be brought to an end, and an explicit commitment to age diversity in public appointments should be made by the Government and by all sponsoring Departments. We believe that this can best be achieved by ensuring that the process of appointment to any public body complies with the terms of the forthcoming legislation on age discrimination in employment, even in those cases in which such appointments do not constitute formal employment (paragraph 6.24).

11.19. The Commissioner for Public Appointments should be given statutory authority to seek out cases of ageism in public appointment procedures, and should also have powers which would lead to the diminution and eventual eradication of ageism (paragraph 6.25).

11.20. In relation to ageism, the remit of the Commissioner for Public Appointments should be extended to include appointments to those publicly funded bodies which currently or prospectively lie outside this remit (paragraph 6.27).

The legislative environment

11.21. The Government should be as explicit as possible in providing illustrations of the circumstances in which exceptional treatment may be justified, in order to provide the clearest possible guidance to both employers and workers (paragraph 6.34).

11.22. In order to minimise the cost to all parties of disputes relating to age discrimination, we recommend that the Government should incorporate in the forthcoming legislation on age discrimination the option of rapid and low-cost arbitration of disputes (paragraph 6.41).

11.23. The Government should not permit the continued use of a normal retirement age by employers, whether at age 65 or 70 or 75, unless the employer can provide a reasoned and objective justification for the use of age rather than performance criteria in the determination of employability. The Government should set an example of good practice by explicitly removing upper age limits in all public-sector employment in advance of the implementation of the forthcoming legislation on age discrimination (paragraph 6.43).

11.24. A move from age-based to competency-based criteria for recruitment, promotion and retirement will require a profound cultural shift on the part of both workers and employers. Long-established conventions about seniority-based promotion and pay will have to be challenged, employers will have to operate transparent and justifiable personnel policies, and employees will have to accept regular performance monitoring and assessment (paragraph 6.46).

11.25. As soon as the draft legislation on age discrimination is in place, the Government, in conjunction with both employer and worker organisations, should embark on a major campaign to raise awareness of the impending legislation, and of its likely effects (paragraph 6.48).

11.26. Just as legislation is now scrutinised for possible infringements of, for example, human rights, it should become routine for such scrutiny to cover the issue of age diversity, and for Ministers to certify that policy and legislation do not contain an ageist element (paragraph 6.49).

Consumption

11.27. The restriction of student loans to people below the age of 54 is blatant discrimination (paragraph 7.10).

11.28. The Department for Education and Skills should explain why age discrimination exists in the provision of student loans (paragraph 7.11).

Women

11.29. The contribution basis of the basic state pension acts as a significant barrier to the acquisition by women of full state pension entitlements (paragraph 8.7).

11.30. The basic state pension should be paid on the basis of citizenship rather than contribution record (paragraph 8.10).

Opportunities for private provision for retirement

11.31. In order to strengthen consumer confidence in equity release products, we recommend that all such products be brought within the FSA's regulatory jurisdiction as soon as is practicable (paragraph 9.4)

11.32. The Government should consider phasing out over time the tax-free lump sum (paragraph 9.9).

11.33. The Government should set an example by explicitly including information on the value of employer pension contributions in pay slips and in recruitment material for all public-sector jobs. We further recommend that a timetable be established for extending this practice to private-sector employment (paragraph 9.16).

11.34. The Government's policy goal of encouraging the delivery of more financial advice to individuals via the workplace is to a significant degree frustrated by the Government's policy goal of ensuring that financial advice is provided according to FSA rules (paragraph 9.19).

11.35. The Government, in co-operation with the FSA, should take action to resolve this conflict of policy goals in order to facilitate the provision of financial advice by employers and make clear the basis on which employers may provide advice, without lowering standards (paragraph 9.20).

11.36. We believe that there is a role for Government in providing a simple, secure and guaranteed long-term savings instrument which can be used by lower- income individuals who do not wish to expose themselves to the costs and risks involved in purchasing a commercial pension product. The Government should provide such a product, in the form of a pensions bond with a real rate of return linked to the economy-wide growth rate and administered by National Savings (paragraph 9.25).

11.37. A general extension of compulsion in pension savings should be avoided. However, that requires the Government to take action to provide a higher minimum state pension (paragraph 9.32).

Uncertainty and private pensions

11.38. The Government should explore with the voluntary sector and the financial services industry the possibility of developing a national financial advice network for low-income individuals (paragraph 9.38).

11.39. The proposed reform to the regulatory and tax environment of occupational pensions will come too late to reverse, or even stem, the tide of closure of defined benefit pension schemes (paragraph 9.42).

11.40. The closure of defined benefit pension schemes seems to be associated with a reduction in overall pension savings, which will have the effect of reducing the value of future pension entitlements (paragraph 9.44).

Complexity and uncertainty

11.41. The state pension system is too complex to function effectively, and the Government have taken insufficient notice of widespread concern about this complexity in their formulation of pensions policy (paragraph 10.6).

Purpose

11.42. The Government should produce a clear set of pension performance objectives which include indicators of the outputs of the pension system (present and expected future pensioner income) as well as the inputs to the system (the scale and source of pension finance). The Government's success in meeting these objectives should be regularly monitored and published (paragraph 10.13).

11.43. The Government should provide an explanation of the rationale for the continuation of age-related benefits such as subsidised travel (paragraph 10.15).

Means testing and public pensions

11.44. The Government's heavy and growing reliance on means testing the pensioner population is regrettable because it:

- unduly penalises current pensioners who have struggled hard to provide a small private income for themselves in retirement
- sends a clear signal to many current workers that it is not in their interests to save for their own old age
- is unfair to tax some of the poorest members of our society at marginal rates as high as or higher than those imposed on the rich (paragraph 10.25)

11.45. As a top priority, the Government should consider introducing a non-means-tested state pension paid on the basis of citizenship to all persons of pension age. We believe that the provision of this baseline state pension is a necessary element for the development of a more extensive system of voluntary pension saving in the United Kingdom (paragraph 10.28).

11.46. The Government should expeditiously develop a fully costed proposal for the payment of the basic state pension at the level of the minimum income guarantee for all pensioners aged 80 and above (paragraph 10.31).

The concept of a "pensions crisis"

11.47. In order to increase the level of consensus associated with long-run pension planning, the Government should establish an independent authority to monitor, undertake research and make recommendations on pensions policy (paragraph 10.42).

APPENDIX 1

Membership of the Committee

The members of the Select Committee were:

	Age at 1 November 2003
Lord Barnett	80
Lord Burns	59
Lord Elder	53
Baroness Hogg	57
Lord Newby	50
Lord Oakeshott of Seagrove Bay	56
Baroness O'Cathain	65
Lord Paul	72
Lord Peston (Chairman)	72
Lord Roll of Ipsden	95
Lord Sheppard of Didgemere	70
Lord Vinson	72

Professor Paul Johnson, AcSS, Professor of Economic History at the London School of Economics and Political Science, was the Committee's Specialist Adviser.

APPENDIX 2

Members' Relevant Interests

Lord Barnett

Chairman, EBS (Education Broadcasting Services) (charitable trust) (unpaid)

Chairman and major investor, Mercury Recycling Group plc (25 April 2001)

Chairman, Mercury Recycling Ltd

Chairman, Atos Origin (UK) Ltd

Trustee, Open University (unpaid) (4 July 2001)

Member, International Advisory Board, EHS and Partners

Lord Burns

Chairman, Abbey National Group plc

Chairman, Dwr Cymru Cyfyngedig

Chairman, Glas Cymru Cyfyngedig

Non-executive Director, The British Land Company plc

Non-executive Director, Pearson plc

Chairman, Governing Body, Royal Academy of Music

President, Society of Business Economists

Vice-President, Royal Economic Society

Governor and Member, Council of Management, National Institute of Economic and Social Research

Chairman, Monteverdi Choir and Orchestra Trustees

Lord Elder

Consultant, The Smith Institute

Consultant, Forth Ports plc

Adviser to Daval International Ltd

Chancellor, Al-Maktoum Institute for Arabic and Islamic Studies

Member of the Action Committee for the Scottish National Photography Centre

Baroness Hogg

Chairman, 3i Group plc

Chairman, Frontier Economics

Council Member, Institute for Fiscal Studies (and CeMMAP)

Council Member, Royal Economic Society

Council Member, University of Lincoln

Governor, BBC

Various education trusts

Non-executive Director, GKN

Non-executive Director, Carnival Corporation and Carnival plc

Lord Newby

Chairman, Live Consulting Ltd (4 October 2001)

Chairman, Reform Publications Ltd

Trustee, Allachy Trust

Trustee, Centre for Reform

Trustee, Coltstaple Trust (4 October 2001)

Lord Oakeshott of Seagrove Bay

Chairman, Coltstaple Trust (charitable trust) (unpaid) (21 March 2001)

Director, *Aubrey Investments Ltd and its subsidiaries (paid) (21 March 2001)

Director, *OLIM Ltd (paid) (21 March 2001)

Director, *Value and Income Trust plc and its subsidiaries (paid) (21 March 2001)

Land and Property: family homes in London, the Isle of Wight and Sussex (no rents received) (21 March 2001)

Member, Finance Committee Mansfield College, Oxford (unpaid) (21 March 2001)

* Shareholdings (more than 1% of the issued share capital) (21 March 2001)

Investment Manager with OLIM Limited (a subsidiary of Close Brothers Group plc)

Baroness O'Cathain

Director, BNP Paribas UK plc

Director, British Airways plc

Director, South-East Water plc

Lord Paul

Ambassador for British Business

Chairman of Trustees, Ambika Paul Foundation

Chancellor, University of Wolverhampton

Co-chairman, United Kingdom-India Round Table

Director and Chairman, Caparo Group Ltd (Lord Paul, Hon Ambar Paul, Hon Akash Paul and Hon Angad Paul are jointly interested in the whole of the issued share capital of the Company through shareholdings registered in the name of Caparo International Corporation, a Company registered in the British Virgin Islands).

Director, Parliamentary Broadcasting Unit Limited (1st October 2001)

Board of the London Development Agency

Member, the Corporation of the Hall of Arts and Sciences (Royal Albert Hall) (January 2002)

Member, Foreign Policy Centre Advisory Council

Member, House of Lords Select Committee on Economic Affairs (1st October 2001)

Member, Industrial Development Advisory Board

Patron, National Children's Centre

Patron, Plan International

Patron, United Kingdom Youth

President, Family Service Units

Vice-president, Engineering Employers' Federation

Chairman of the Board of PiggyBankKids, a children’s charity, and its trading subsidiary PiggyBankKids Projects Limited

Member, Non-executive, Board of London 2012

Lord Peston

Director, Philip Allen Publishers Ltd

Emeritus Professor of Economics, Queen Mary, University of London

Patron, Council for Education in the Commonwealth

Vice-president, Action for Dysphasic Adults

President, Institute of Administrative Management

Lord Roll of Ipsden

Director, Pan Holding S.A. (29 March 2001)

Senior Adviser, UBS Ltd (3 April 2001)

Shareholdings (non-controlling), J. Sainsbury

Non-Financial Interests:

Hon. Fellow, London School of Economics

Vice President, Society of Business Economists

Hon. Member of the Advisory Committee, The Bologna Center, Johns Hopkins

University

Member, Bilderberg Steering Committee

Trustee, the Daiwa Anglo-Japanese Foundation.

Lord Sheppard of Didgemere

Non-parliamentary Consultant, Didgemere Consultants Ltd

Non-executive Chairman, McBride plc (shareholding 1.2%)

Non-executive Chairman, Unipart Group

Non-executive Chairman, Oneclick HR plc (shareholding 6.1%)

Non-executive Chairman, Namibian Resources plc (shareholding 5%)

Non-executive Chairman, GB Railways Ltd

Non-executive Chairman, Advisory Committee of Warnborough Asset Management

Controlling Shareholdings; Didgemere Consultants Ltd

Controlling Shareholdings; Didgemere Farms Ltd (Farmland in Essex)

Other shareholdings below 5%, except Delta Dot Ltd, approximately 7%

Chancellor, Middlesex University (unpaid)

Honorary Fellow, Governor and Member of External Affairs Committee, London School of Economics (unpaid)

President, London First (unpaid)

Director, London Business Board (unpaid)

Vice President, Beer and Pub Association (unpaid)

Vice-President, Blue Cross (unpaid)

Vice-President, United Response (unpaid)

Trustee/Executive Committee Member, Animal Health Trust (unpaid)

Patron, Trees for Cities (unpaid)

Member, UK Cancer Research Charity (unpaid)

Vice-President, Business in the Community (past Chairman) (unpaid)

Past Chairman, The Prince's Trust (and Prince's Youth Business Trust) (unpaid)

Chairman of Trustees, Civilians Remembered Trust (unpaid)

Pensioner, Diageo plc, etc

Lord Vinson

Farmer, (Farm in Northumberland - part of which is in the Northumberland National Park) (9 October 2001)

Trustee and Vice President, Institute of Economic Affairs (9 October 2001)

Past interests have included:

Board Director of Barclays Bank;

Chairman of the Institute of Economic Affairs;

Chairman of a property company;

Chairman of an Investment Trust;

Deputy Chairman of a large venture capital company;

Director of the British Airports Authority;

Chairman of the Rural Development Commission;

experience of building up a business from the age of 21, and floating a company on the Stock Exchange.

Past winner of the Queen's Award for Industry

APPENDIX 3

List of Witnesses

The following witnesses gave written evidence. Those marked * also gave oral evidence.

*Actuarial Profession
*Age Concern
*Association of British Insurers
Association of Retired and Persons Over 50
AXA Sun Life
Barr, Professor Nicholas
Beatty, Ms Christina
*Blake, Professor David, The Pensions Institute
*Booth, Professor Philip
Cabinet Office
*Chartered Institute of Personnel and Development
Civil Service Pensioners' Alliance
*Commission for Racial Equality
*Confederation of British Industry
*Consumers' Association
Continuing Care Conference
Department for Constitutional Affairs
Department for Culture, Media and Sport
Department for Education and Skills
Department of Health
*Department for Work and Pensions
*Disney, Professor Richard
*Engineering Employers' Federation
*Equal Opportunities Commission
*Fawcett Society
*Field MP, Rt Hon. Frank
*Financial Services Authority
Fothergill, Professor Stephen
*Fritchie DBE, Dame Rennie, Commissioner for Public Appointments
*Ginn, Dr Jay
Government Actuary's Department
*Greengross OBE, Baroness
*Grieve Smith, Mr John
Home Office

*HM Treasury

Institute for Volunteering Research

International Longevity Centre UK

*Joshi, Professor Heather

Ministry of Defence

*Mullan, Mr Phil

Murphy BSc FCA, Mr Richard

*National Association of Pension Funds

North East Pensioners Association

Oxford Institute of Ageing

Pension and Population Research Institute

PARITY

*Pensions Policy Institute

*Policy Research Institute on Ageing and Ethnicity

Price, Ms Debora

*PricewaterhouseCoopers

Royal Ordnance Pensioners Association

Scottish Life

*Smith MP, Rt Hon. Andrew, Secretary of State for Work and Pensions

Standard Life Assurance Company

*Taylor, Dr Philip

*Trades Union Congress

Walker, Professor Alan

Wallace, Mr Paul

Warr, Emeritus Professor Peter

Weale CBE, Mr Martin

*Webb MP, Professor Steve

*Willetts MP, Mr David

*Women's Budget Group

APPENDIX 4

Call for Evidence

The Economic Affairs Committee has decided to conduct an inquiry into aspects of the economics of an ageing population, and in particular to consider (i) length of working life; (ii) women; and (iii) fundamentals of pension policy.

Evidence is invited by **1 March 2003**.

The Committee will need to discover the basic factual position, including the extent to which the UK's population is ageing and how the UK compares with other countries in this regard.

The Committee welcomes written submissions which address any or all of the following:

1. To what extent is the UK's population ageing? What effect will this phenomenon have on the supply of labour and capital, wages, interest rates, asset prices (especially housing) and productivity? How do the relevant facts vary by gender and ethnic group?
2. How might policy reverse the recent trend towards early retirement? Should legislation to outlaw age discrimination be introduced? Would it work? Should there be a statutory retirement age? Can the labour market absorb more older workers? To what extent do people choose when to retire?
3. Why do people not save enough for retirement? How might they be encouraged to do so? What new products could the financial services industry offer to support retirement income and to influence retirement decisions?
4. Why are most pensioners who live in poverty women? How might public policy provide for people (mostly women) who cannot make regular and continuous contributions to a pension scheme throughout their working life? What responsibilities do private-sector financial product providers have?
5. What is the role of the basic state pension and does it fulfil that role? How is pension policy influenced by ideology, short-term political considerations, the need to produce consensus and the need to protect existing benefits?
6. How should the following objectives of pension provision be prioritised in formulating pensions policy: adequacy, fairness, protecting incentives, affordability, certainty, simplicity, transparency, practicality and choice? What are the trade-offs?
7. Is it appropriate to have as an explicit policy objective the reduction of public spending on pensions as a proportion of GDP? What is the role and relevance of (i) the institutional framework; (ii) fiscal policy; (iii) regulatory requirements?
8. What effect do means-tested benefits for pensioners have on work and saving incentives? Are there any people for whom zero or low saving is the appropriate economic response to their circumstances?
9. Is the continuing trend away from public and towards private provision economically sustainable? How are we to determine the best public/private balance?