

# Autumn Statement announcement on a core principle underpinning future State Pension age rises: DWP background note

## Introduction

The Chancellor has today announced the government's position that people should spend, on average, up to one third of their adult life drawing a State Pension.<sup>1</sup>

This note provides further detail on this core principle and how it may be defined in practice. Final details of the methodology that will be used to inform future decisions on State Pension age (SPa) will be announced in due course in the run up to the review itself, which must happen by May 2017.

## How the proportion of adult life spent in retirement is calculated and the variables used in the government's calculation

The proportion of adult life spent in receipt of State Pension can be expressed as follows:

$$\text{Proportion of adult life spent in receipt of State Pension} = \frac{\text{Life expectancy at SPa}}{\text{Life expectancy at SPa} + \text{SPa} - \text{adult life starting age}}$$

From the above it can be seen that there are a number of variables that feed into this formula, including:

- When adult life is considered to begin;
- What measurement of life expectancy is used; and
- How an individual's life expectancy is measured (at a time when life expectancy for men and women is not the same).

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<sup>1</sup> The phrases 'drawing a State Pension' and 'retirement' are used as shorthand to express the concept of adult life spent over State Pension age. Neither are ideal explanations of this concept, as on the one hand individuals may choose to defer drawing their pension past SPa, and on the other, retirement is not necessarily linked with reaching SPa.

## **When adult life is considered to begin**

The government has decided to use the age of 20 as the appropriate starting age for the purpose of calculating the proportion of adult life spent in receipt of State Pension. This is based on OECD convention and is commonly used as a comparator for matters relating to pensions.<sup>2</sup>

## **What measurement of life expectancy is used**

The Pensions Commission recommended that official publications use the cohort measurement of life expectancy when describing current and future trends in longevity.<sup>3</sup> The principal projections of UK cohort life expectancy, published by the Office for National Statistics every two years, allow projected life expectancy at any age to be calculated. The government believes that these projections are the appropriate ones for the purposes of the State Pension age review. The method used calculates the proportion of life spent in retirement at the relevant State Pension age, using the cohort life expectancy for a person of that age in any given year.

## **How a person's life expectancy is measured**

At a time when life expectancies between the sexes remain different (but are converging), the government believes that the appropriate measurement must consider both male and female life expectancies. Therefore, the average life expectancy of both genders, weighted for the different numbers of men and women in the population at the relevant SPa and their respective cohort life expectancies, is used in the "life expectancy at SPa" component of the calculation.

## **State Pension age review**

The government is currently legislating for a review of State Pension age to take place once in every Parliament. This will be based on the principle that individuals should spend a given proportion of their adult life in receipt of a State Pension. As well as the Government Actuary's report on longevity, a person independent of government will be commissioned to lead a report on other factors relevant to setting State Pension age. The government anticipates that these other factors will include, for example, healthy life expectancy, and differences in life expectancy between socio-economic groups. The review will seek to give individuals affected by changes to their State Pension age at least ten years' notice. As now, any

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<sup>2</sup> This is also consistent with the Impact Assessments for the increase to SPa 67.

<sup>3</sup> Cohort life expectancy is used to assess future adult life expectancy, which allows for actual or projected changes in mortality during a person's lifetime. Cohort life expectancies are typically higher than period life expectancies as they factor in continued improvements in longevity. The ONS considers cohort life expectancy to be a more appropriate measure of how long a person of a given age would be expected to live, on average, than period life expectancy.

future changes to State Pension age will have to be made law through primary legislation and will therefore be subject to the full scrutiny of Parliament.

### **Defining a third of adult life**

Working with the Government Actuary's Department, DWP will develop detailed proposals for the methodology which will inform the State Pension age review which will be conducted early in the next Parliament. Our working assumption is that this methodology would provide for SPa to complete any increase in the year in which the proportion of adult life spent in receipt of State Pension at the existing SPa would have reached 33.3% (to the nearest decimal place). Because life expectancy is projected to steadily increase year after year, with any given SPa, successive cohorts will spend more and more time in receipt of a State Pension.<sup>4</sup> When the proportion of adult life spent drawing a pension reaches 33.3%, this is the year in which SPa would complete its transition to the higher SPa.

However, increases in SPa do not happen instantly, but are phased in over a period of time. The government has chosen to retain the phasing-in process adopted for the proposed increase to SPa 67, which takes place over two years,<sup>5</sup> and so the transition to SPa 68 would begin 2 years before the proportion of adult life spent drawing a State Pension at 67 would reach 33.3%. Based on this method and on the most recent set of ONS life expectancy figures, published in 2011, we might expect this process to happen in the mid 2030s. It is likely that the State Pension age review, to be conducted early in the next Parliament, will be based on ONS life expectancy projections published in 2015, which may or may not yield a different date. As mentioned above, the State Pension age review will consider not only life expectancy, but also other relevant factors, and any proposed changes to the State Pension age will still have to be put in primary legislation and receive the approval of Parliament before becoming law.

[Find out about the Autumn Statement 2013](#)

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<sup>4</sup> A 'cohort' is defined in this instance as the group of individuals who reach SPa in a single given year.

<sup>5</sup> The proposed increase to SPa 67, for example, begins in April 2026 and completes in March 2028: the full transitional table can be found in Annex 5 of the white paper *The single-tier pension: a simple foundation for saving*.