

Projections of entitlement to Income Related Benefits to 2050

Introduction

This note presents DWPs latest projections of Pension Credit entitlement under the reformed state pension system (Pensions Act 2007) and presents, for the first time, projections of entitlement to Housing Benefit, Council Tax Benefit and to any one or more of the three income related benefits. It also describes the possible interaction between private pensions, after reforms, and entitlement to the income related benefits.

Projections take into account the latest population projections published by the Office for National Statistics, showing a larger, older pensioner population. They also take into account improvements to the modelling capability of PENSIM2, the Department for Work and Pensions' principal tool for projecting forward entitlement to income related benefits. PENSIM2 has been enhanced so that it now produces projections of entitlement to Housing Benefit and Council Tax Benefit as well as Pension Credit.

Section one presents updated projections of entitlement to Pension Credit under the reformed state pension system. Section two presents newly available projections of entitlement to Housing Benefit and to Council Tax Benefit, also under the reformed state pension system. Section three contains some initial projections of entitlement to any one of these income related benefits under the state pension reforms. Section four briefly discusses the sensitivity of the projections to underlying assumptions and section five illustrates the effect of changes in state pension policy on the projection of entitlement to any income related benefit. Finally, section six describes the potential interaction between the private pension reforms in the Pensions Bill 2007 and entitlement to income related benefits.

Guide to interpretation

Projections have been presented in both tabular and chart form.

The charts are constructed using un-rounded projections in each year from 2005 to 2050. They are intended to show only the broad trends in entitlement over time – individual year on year fluctuations are not significant.

The tables have been constructed using projections from selected years that have been rounded to the nearest 5 percentage points. They represent the best estimates of the percentage of pensioner households entitled to income related benefits for the years shown - as a result of the rounding the broad trends can be distorted in these tables.

Combining projections for individual benefits together will not give correct estimates of the size of a broader group as it will not take account of the possible overlaps between benefits. For example, adding together projections of the proportion eligible to Housing Benefit and Council Tax Benefit will not give you a robust projection of the proportion eligible to Housing Benefit or Council Tax Benefit as some households will be eligible to both.

These projections in themselves cannot be used to calculate the number or proportion of individuals who could expect different levels of return from saving; being eligible for an income related benefit in retirement does not necessarily result in low returns. Various other factors would need to be taken into consideration, such as take-up of benefits, individuals' contribution histories, the impact of taking lump sum payments on retirement, and the effect of working age benefit receipt.

Section 1: Entitlement to Pension Credit

This section presents projections of entitlement to Pension Credit under the reformed state pension system. Pension Credit has two elements: (i) the guarantee credit and (ii) the savings credit. Guarantee credit ensures that pensioners with low incomes are brought up to a minimum income level regardless of their circumstances. Savings credit ensures that pensioner households who have incomes around the guarantee credit level and some saving or a second pension are rewarded¹. Chart 1, shows how the proportion of pensioner households entitled to Pension Credit and its sub-components are projected to decline over time. Table 1 sets out the projections for selected years.

Chart 1: Proportion of pensioner households entitled to Pension Credit, under the reformed state pension system

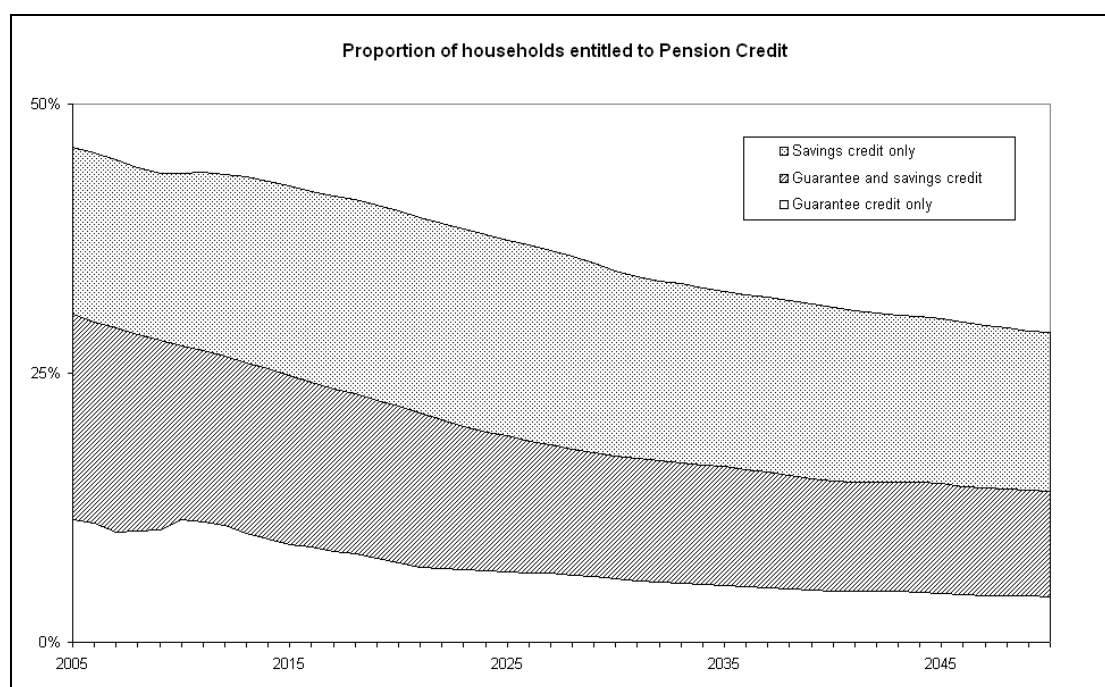


Table 1: Proportion of pensioner households entitled to Pension Credit in selected years, under the reformed state pension system

	Guarantee Credit only	Guarantee and Savings Credit	Savings Credit only	Pension Credit*
2005	10%	20%	15%	45%
2010	10%	15%	15%	45%
2020	5%	15%	20%	40%
2030	5%	10%	15%	35%
2040	5%	10%	15%	30%
2050	5%	10%	15%	30%

Notes: Figures rounded to nearest 5 percentage points. Components may not sum to totals due to rounding. Projections from 2010. Total number entitled to any element of Pension Credit*

¹ Pensioners on the savings credit face a deduction of 40 pence for every £1 of extra income.

Following reform of the state pension system:

- Around 30 per cent of households are projected to be entitled to Pension Credit in 2050 compared with around 45 per cent today.
- Around 5 per cent of households could be entitled to the Guarantee Credit only in 2050 compared with around 10 per cent today.

These projections have been tested for sensitivity to plausible changes in assumptions on life expectancy, employment and private pension accumulation, which taken together produce variations in the overall level and distribution of pensioner incomes. Based on these tests the proportion of households entitled to Pension Credit in 2050 could vary by around five percentage points.

Section 2: Entitlement to Housing Benefit and Council Tax Benefit

This section presents projections of entitlement to Housing Benefit and Council Tax Benefit under the reformed state pension system. In addition to supporting pensioners directly with low incomes, income-related benefits are also provided for additional and varying spending commitments, such as rent and council tax. Pensioners can gain support where they are deemed to have insufficient income to meet these extra demands.

Chart 2, shows how the proportion of private pensioner households² entitled to Housing Benefit and Council Tax benefit is projected to decline over time. Table 2 sets out the projections for selected years.

Chart 2: Proportion of private pensioner households entitled to Housing Benefit and Council Tax Benefit, under the reformed state pension system

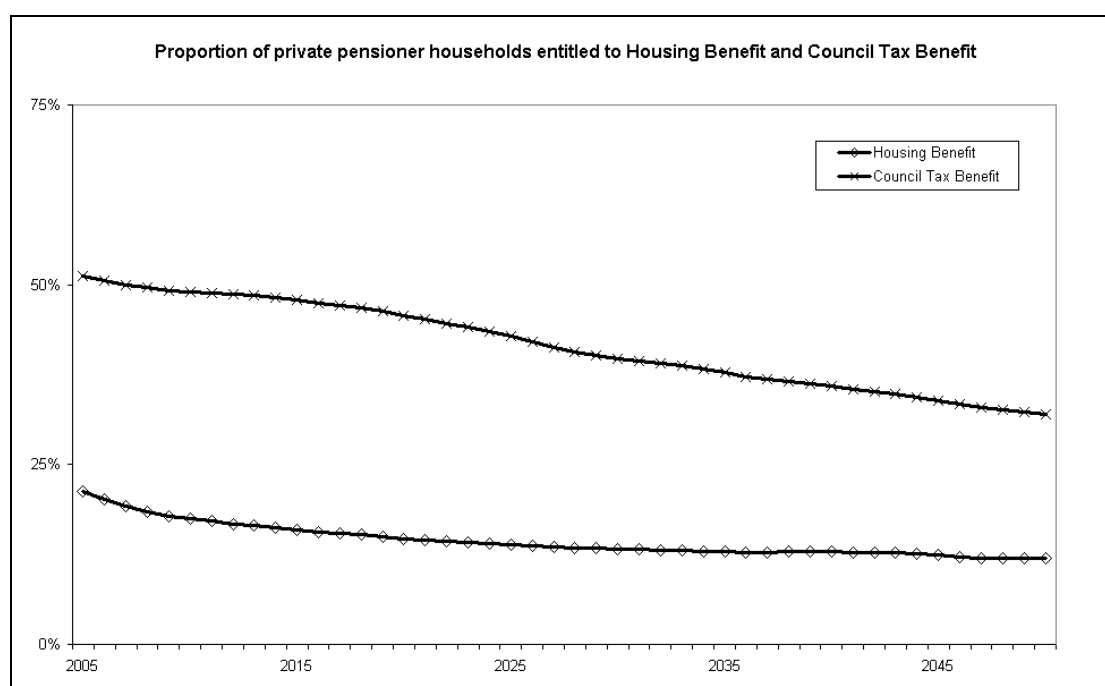


Table 2: Proportion of private pensioner households entitled to Housing Benefit and Council Tax Benefit in selected years, under the reformed state pension system

	Housing Benefit	Council Tax Benefit
2005	20%	50%
2010	15%	50%
2020	15%	45%
2030	15%	40%
2040	15%	35%
2050	10%	30%

Notes: Figures rounded to nearest 5 percentage points. Projections from 2010.

Following reform of the state pension system:

- Around 10 per cent of private pensioner households could be entitled to Housing Benefit in 2050 compared with around 20 per cent today.

² Private households excludes those in residential institutions

- Around 30 per cent of private pensioner households could be entitled to Council Tax Benefit in 2050 compared with around 50 per cent today.

Like projections of entitlement to Pension Credit, the Housing Benefit and Council Tax Benefit projections have been tested for plausible changes in assumptions on the level and distribution of pensioner incomes. In addition they have also been tested for sensitivity to plausible changes in the growth in rents and council tax liability. Housing Benefit and Council Tax Benefit projections appear to be more robust to changes in these assumptions than the Pension Credit projections with little noticeable variation between tests.

Projections of entitlement to each of the individual benefits (Pension Credit, Housing Benefit and Council Tax Benefit) cannot be added together to provide an accurate estimate of the proportion of households entitled to any income related benefit because of the overlaps between the benefits (i.e. individuals in households can be entitled to more than one means tested benefit in retirement). See section 3 for some initial projections of entitlement to any income related benefit.

Section 3: Entitlement to any Income Related Benefit

This section presents projections of entitlement to any income related benefit. Low income pensioners can be entitled to one or more of Pension Credit, Council Tax Benefit and Housing Benefit, depending on their circumstances.

Chart 3, shows how the proportion of pensioner households entitled to any one of the income related benefits is projected to decline over time. Table 3 contains the detailed projections for selected years.

Chart 3: Proportion of pensioner households entitled to any income related benefit, under the reformed state pension system

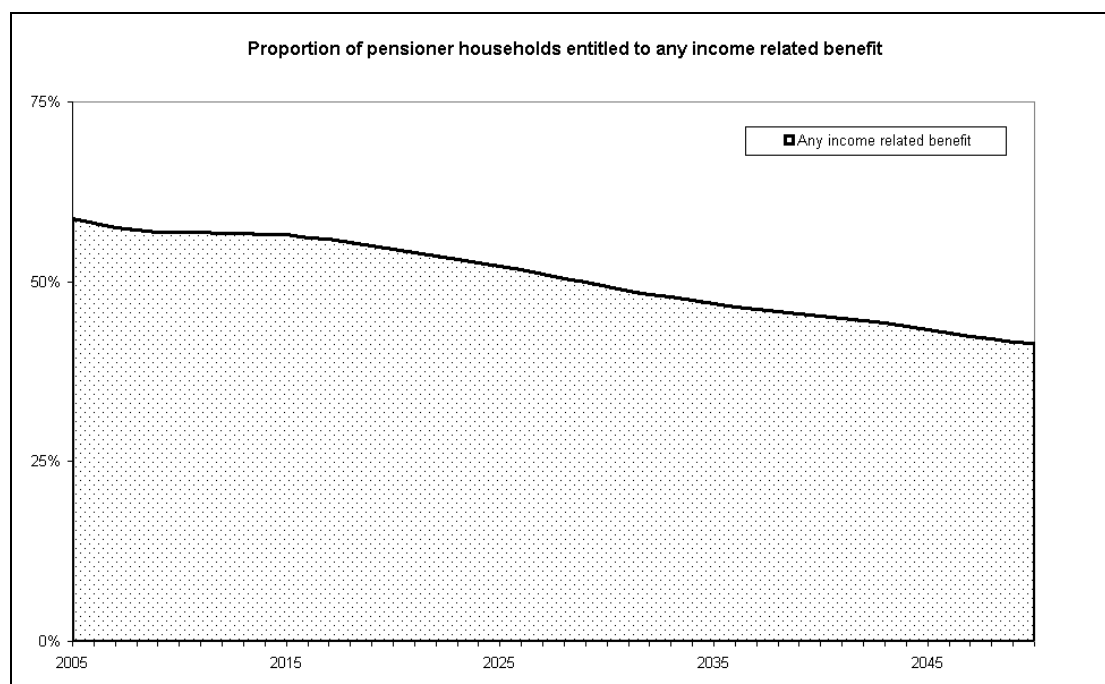


Table 3: Proportion of pensioner households entitled to any income related benefit in selected years, under the reformed state pension system

	Any income related benefit
2005	60%
2010	55%
2020	55%
2030	50%
2040	45%
2050	40%

Notes: figures rounded to nearest 5 percentage points. Projections from 2010.

Following reform of the state pension system:

- Around 40 per cent of pensioner households could be entitled to any one of the three income related benefits compared to around 60 percent of pensioner households today.

These projections have been tested for sensitivity to plausible changes in assumptions about the future level and distribution of pensioner incomes and about the future growth in rents and council tax liability. Based on these tests the proportion of pensioner households entitled to any of the income related benefits in 2050 could vary by around five percentage points.

Estimating the extent of entitlement to different combinations of income related benefits and how these will evolve over time is a complex task. DWP has attempted to ensure estimates are robust by modelling individual's incomes and additional needs to provide direct evidence of the potential scale of overlaps.

Section 4: Testing the sensitivity of the projections

The projections presented in sections 1-3 have been tested for sensitivity to plausible changes in underlying assumptions about the future level and distribution of pensioner incomes and future growth in rents and council tax liability (see Annex A for further details).

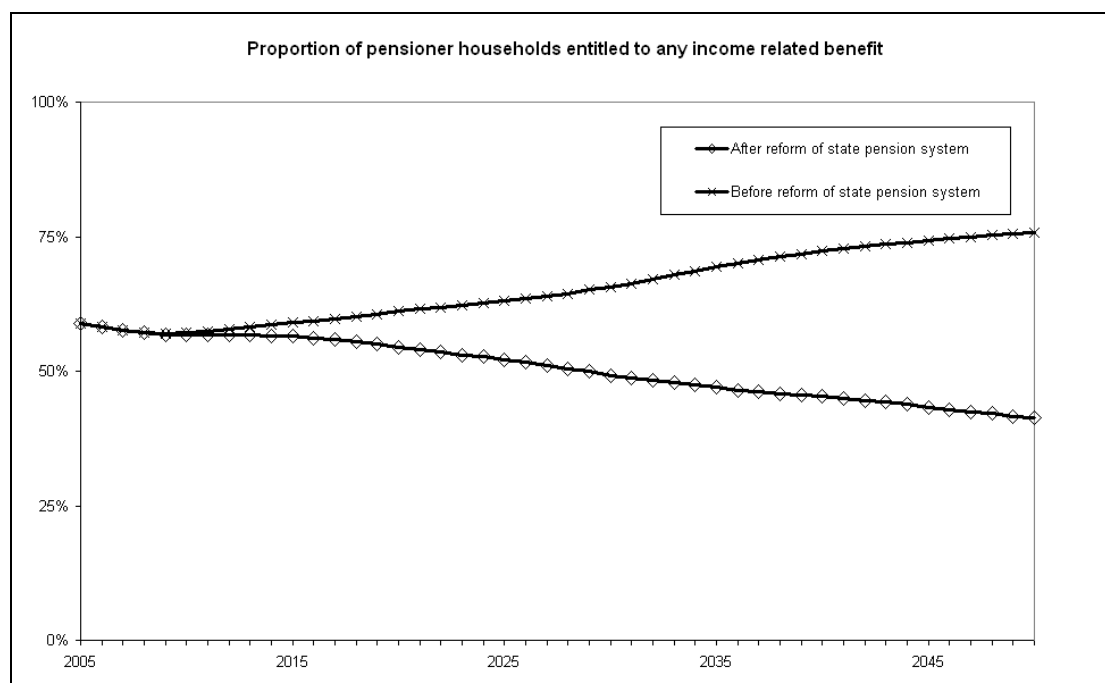
Based on these tests the proportion of pensioner households entitled to income related benefits in 2050 appear to be robust to the changes in assumptions, with pension credit varying by around five percentage points and housing benefit and council tax benefit changing little between tests.

Part of the explanation for this is that in practice pensioner income growth, and in particular state pension income, is quite stable. The extension of coverage of the state pension provides a stable underpin that is relatively unaffected by variations in assumptions. Also variability in private pension income has a small impact on entitlement as private pensions represent a relatively minor source of income for those within the scope of income related benefits.

Section 5: Policy scenarios

The measures introduced with the Pensions Act 2007 significantly reduce the proportion of pensioner households that could be entitled to any income related benefit in 2050 from around 75 per cent³ to around 40 percent – see Chart 4.

Chart 4: Proportion of pensioner households entitled to any income related benefit, before and after reform of the state pension system



However income related benefits are an important part of the pension system as they provide valuable resources to meet extra costs. Even substantial further change could still lead to income related benefits for a significant proportion of pensioners. For example, Table 4 shows how the projection of entitlement to any income related benefit presented in section 3 changes if the level of Basic State Pension is increased by 25 per cent, 50 per cent and 100 per cent from 2012.

Table 4: Proportion of pensioner households entitled to any income related benefit in 2050, following reform of state pensions, plus increases in the level of Basic State Pension

	Following reform of the state pensions	+ 25% increase in the level of BSP from 2012	+ 50% increase in the level of BSP from 2012	+ 100% increase in the level of BSP from 2012
Any income related benefit in 2050	40%	35%	30%	25%

Notes: figures rounded to nearest 5 percentage points. Projections from 2010.

- Doubling the level of the Basic State Pension, which would cost in the region of £150bn (in today's prices) net of savings in income related benefits by 2050, leaves around a quarter of pensioner households eligible to an income related benefit.

³ Assuming the Guarantee Credit continues to be uprated in line with the growth in average earnings.

Section 6: Impact of the private pension reforms

The measures described in the Pensions Bill 2007 aim to encourage more private saving for retirement through automatic enrolment into a qualifying workplace pension including personal accounts with a compulsory minimum employer contribution. This section examines the extent to which these reforms affect the population who are in households entitled to income related benefits in retirement. The analysis uses the same underlying assumptions as the impact analysis published in *Pensions Bill - Impact Assessment*⁴.

Table 5: Proportions of selected populations entitled to income related benefits in 2050 following state and proposed private pension reforms

	Pension Credit	Pension Credit: <i>Guarantee Credit only</i>	Housing Benefit	Council Tax Benefit	Any Income Related Benefit
All pensioner households following reform of state pensions but in the absence of reform of private pensions	30%	5%	10%	30%	40%
All pensioner households following reform of state and private pensions	25%	5%	10%	30%	40%
Pensioner households with any private pension income* following reform of state and private pensions	20%	-	10%	25%	35%

*Notes: figures rounded to nearest 5 percentage points. In cells marked with “-”, the percentage is less than 2.5. * Excludes households who contributed to but trivially commuted private pensions.*

Following reform of both the state and private pension systems:

- Around 25 per cent of all pensioner households could be entitled to Pension Credit in 2050 compared with around 30 per cent following reform of state pensions only. Much of this difference is due to rounding - the proportion of pensioner households entitled to Pension Credit in 2050 falls by a marginal amount following the reform of the private pension system.
- Pensioners in households with any private pension income are less likely than the pensioner population in general to be entitled to income related benefits in 2050.

Note that the analysis for those with any private pension income excludes those households where individuals may have contributed to private pensions but have trivially commuted their private pension on retirement. Including these cases increases the proportion entitled to income related benefits towards (but not up to) the figures for all pensioner households.

⁴ published 5th December 2007

Annex A: Key modelling assumptions and alternative scenarios underpinning the projections in sections 1-3

	Base case assumptions	Alternative scenario 1 Lower IRB entitlement	Alternative scenario 2 Higher IRB entitlement
Life expectancy	Standard mortality assumptions	High mortality assumptions	Low mortality assumptions
Employment rates	Trend in employment rates consistent with HMT cohort employment model with base case assumptions. Approximate overall employment rate 75%.	As in base case but with rates scaled linearly from 2006-2015 and by 80/75 from 2015. Approximate overall employment rate 80%.	As in scenario 1 but with rates scaled by 70/75 from 2015. Approximate overall employment rate 70%.
Private pensions			
- DB/DC	DB/DC shift continues so that ratio applying to new scheme entrants reaches 30% DB and 70% DC in 2049	DB/DC shift remains at current level: 53% DB and 47% DC	DB/DC shift continues so that ratio applying to new scheme entrants levels off at 10% DB and 90% DC in 2044
- Annual membership rates (stock)	16% of private sector employees are members of occupational pension schemes 13% of private sector employees are members of personal pensions	19% of private sector employees are members of occupational pension schemes 13% of private sector employees are members of personal pensions	15% of private sector employees are members of occupational pension schemes 9% of private sector employees are members of personal pensions
- Contracting out (DC contracting out abolished in 2012 for all scenarios)	Private sector DB: consistent with the assumed DB/DC shift and the AP forecasting model assumptions on employees in contracted out DB schemes.	Private sector DB: no basis for improvement so same as the base case.	Private sector DB: faster decline in contracting out
- scheme change	90% of public sector employees remain in schemes if they change jobs 25% of private sector employees remain in the same scheme if they change jobs 0% of people remain in the same scheme if they change sectors.	Same as base case	Same as base case
- Rate of return on funds	3.5% pa real	4% pa real	3% pa real
- Annuity rates	Current levels, adjusted for projected mortality improvements	Current levels, adjusted for projected high mortality (so higher annuity rates than base case)	Current levels, adjusted for projected low mortality (so lower annuity rates than base case assumptions)
Rents/council tax	Grow in line with average earnings	Grow in line with average earnings minus 0.5 percentage points	Grow in line with average earnings plus 0.5 percentage points