Published by
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PPI'S AUTOMATIC ENROLMENT DAY: A SUCCESS WORTH BUILDING ON

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The Pensions Commission

The Pensions Commission, established in 2002, was set up by the Government to review the UK pension system. The Commission was led by Lord Adair Turner, Professor John Hills CBE and Baroness Jeannie Drake CBE. The Commission published two reports and made recommendations in their second, 2005 report, for policy changes to the State and private pension system. Among these were the recommendation of the creation of a National Pension Savings Scheme (NPSS) applying the principle of automatic enrolment at the national level. There have recently been calls for a new Pensions Commission to be set up, with the current Pensions Minister, Guy Opperman MP, suggesting it be asked to consider future State Pension age rises and future minimum contribution levels into private pensions.

Source: Pensions Commission (2005) *The second report of the pensions commission*

Personal Accounts

In 2006 the Department for Work and Pensions (DWP) published two White Papers: "Security in retirement: towards a new pensions system" and "Personal accounts: a new way to save". These introduced the reforms to State and private pensions that the Government wished to make in response to the Pensions Commission's reports. The Papers set out the framework for automatic enrolment including: an earnings threshold, contribution bands and a national pension savings scheme "Personal Accounts" (that was later to become NEST) which would provide a pension for lower earners who may not be attractive to commercial pension schemes.

Source: DWP (2006) *Security in retirement: towards a new pensions system; DWP (2006) Personal accounts: a new way to save*

Personal Accounts Delivery Authority (PADA)

PADA was set up in 2007 to provide advice and make recommendations to the Government on the personal accounts policy. PADA was later given the remit of developing, delivering and managing the personal accounts scheme. PADA was chaired by Baroness Jeannie Drake and its Chief Executive was Tim Jones. In 2010, PADA was wound up and replaced by the NEST Corporation who provide the personal accounts scheme under the name National Employment Savings Trust.

National Employment Savings Trust (NEST)

NEST replaced PADA in 2010 and opened its doors to members in March 2012. NEST, a master trust Defined Contribution (DC) scheme, was provided with a loan from Government for set up costs and is currently paying the loan back. NEST charges members 1.8% on contributions in order to repay its loan and 0.3% on funds under management in order to meet running and investment costs. NEST has a public service obligation to accept any employer who wants to use the scheme to meet their automatic enrolment duties, or any self-employed individual who wishes to join. NEST is designed around the needs of new savers with low incomes and low financial capability and has developed a set of easy to understand terms and principles for communication with its membership.

The rise of master trusts

A small number of pure Defined Contribution (DC) master trusts operated in the UK throughout the 20th century (less than 15 schemes at any given time). The introduction of automatic enrolment, which brought millions of new people into workplace pension saving, increased the motivation for private sector companies to provide master trust schemes for employers to use. The number of master trusts increased from around 10, in 2010, to around 90, by April 2019. The number of active savers in master trusts grew from around 0.2 million total members in 2010 to around 8.1 million active members in 2019 (around 61% of total active DC scheme membership). A new master trust authorisation regime was introduced in 2019 in order to ensure that master trust schemes are well funded and administered; several schemes have exited the market as a result. 38 schemes have applied for authorisation.

Source: Pension and Lifetime Savings Association (2018) *Master trusts: made simpler guide; Silcock, D. (PPI) (2019) The PPI DC Future Book Pensions Policy Instiute*

2010 review – Making automatic enrolment work

In 2010, the DWP commissioned three experts (Paul Johnson CBE, Frontier Economics and Institute for Fiscal Studies, David Yeandle OBE, Engineering Employers' Federation, and Adrian Boulding, Legal & General) to consider whether the proposed scope for automatic enrolment and the policy of establishing NEST properly serves the automatically enrolled population. The panel made several recommendations with a view to ensuring that automatic enrolment operates effectively, including a recommendation that the earnings eligibility threshold be raised from £5,000 to £10,000 (covered below) and that the Government and regulators explore options for making pot transfers between employers more straightforward.

Source: *Johnson, P. Yeandle, D. & Boulding, A. (2010) Making automatic enrolment work: A review for the Department for Work and Pensions*

Automatic enrolment staging

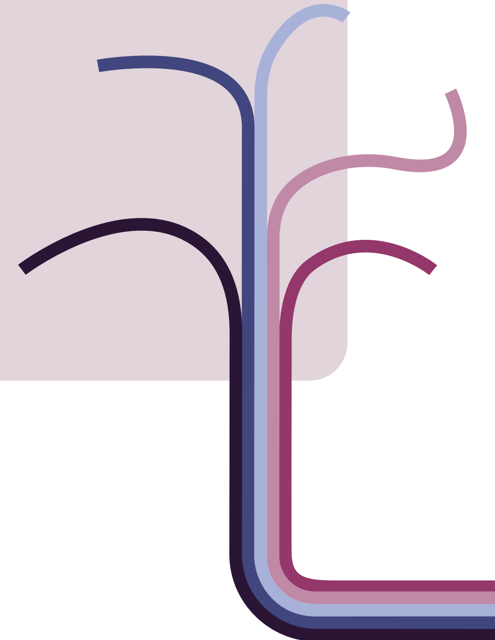
Automatic enrolment was introduced in a staged process in order to trial enrolments first with larger employers, allow smaller employers more time to prepare, and to allow time for support infrastructure to be developed to help employers enrolling for the first time. The staging timetable was set as follows:

1 October 2012 to 1 February 2014:	250 or more employees
1 April 2014 to 1 April 2015:	50 to 249 employees
1 August 2015 to 1 October 2015:	30 to 49 employees
1 January 2016 to 1 April 2017:	Less than 30 employees
1 April 2017 to 1 February 2018:	Employers without PAYE schemes and new employers

Automatic enrolment contribution phasing

Required minimum contributions were phased in, in order to allow employers and employees time to adjust to the increased expenditure, with the aim of full minimum contributions comprising 3% from employer, 4% from employee, 1% from Government through tax relief on a band of earnings (£6,136 to £50,000 in 2019/20). Contribution increases were phased in according to the following timetable, though the final two increases were pushed back from their original scheduled dates of October 2017 and October 2018.

Date	Employer	Employee	Government	Total
1 Oct 2012 to 5 Apr 2018	1%	1%	0.2%	2%
6 Apr 2018 to 5 Apr 2019	2%	3%	0.6%	5%
6 Apr 2019 onwards…	3%	4%	1%	8%



Eligibility criteria

Automatic enrolment policy requires employers to enrol "eligible" employees into a qualifying workplace pension scheme and to pay minimum contributions for those who do not opt out. In order to be eligible, an employee must be between age 22 and State Pension age and must be earning £10,000pa or more.

- The minimum age for eligibility was set at age 22 because people under this age are likely to have higher job turnover and automatically enrolling them could cause administrative complications for both employee and employer. It was also believed that employment for those under age 22 was more sensitive to non-wage costs.
- The earnings eligibility trigger was intended to prevent those on very low earnings being automatically enrolled and having contributions deducted from their pay that they could not afford to make. The threshold was raised from £5,000 to £10,000 before the policy was introduced, as it was believed that most of those with working-life incomes below £10,000 would be able to maintain working life living standards in retirement on State Pension and benefits and that saving into a workplace pension would reduce working-life living standards and could reduce their entitlement to means-tested benefits in retirement (see 2010 review).

Source: DWP (2006) *Personal accounts: a new way to save;* DWP (2006) *Security in retirement: towards a new pensions system;* Johnson, P. Yeandle, D. & Boulding, A. (2010) *Making automatic enrolment work: A review for the Department for Work and Pensions*

Qualifying pension schemes

Employers were/are required to choose "qualifying schemes" to use when fulfilling their automatic enrolment duties. In order for a scheme to qualify it must meet minimum quality standards which differ between Defined Contribution (DC) and Defined Benefit (DB) schemes. For example, in order to qualify, a DC contract-based scheme must: be subject to regulation by the Financial Conduct Authority; have its operations carried out in the UK by a person who is an authorised person or an exempt person under section 19 of the Financial Services and Markets Act 2000; provide money purchase benefits; and, have certain types of agreements in place between the employer, the jobholder and the provider of the personal pension scheme.

Source: The Pensions Regulator (2019) *Detailed guidance for employers*

2012 Automatic enrolment is introduced

In October 2012, the largest employers (with 250 or more employees) began automatically enrolling eligible employees into a workplace pension scheme, though some started enrolling before their designated staging date. The majority of large employers offered pension membership and employer contributions prior to the introduction of automatic enrolment and were therefore likely to have some of the required payroll and HR infrastructure in place to support their new duties. However, all employers needed to make adjustments in order to ensure they were complying with automatic enrolment regulations, assessing employee eligibility correctly and that their chosen pension scheme qualified.

Enrolments, re-enrolments and ineligibility

- As of December 2019, 10.2 million employees had been automatically enrolled.
- As of December 2019, 9.6 million employees had been found ineligible for automatic enrolment due to their age or earnings.
- Employers are required to re-enrol employees who opt out or stop contributing, within three years of the date they stop contributing. As of December 2019, 709,000 employees had been automatically re-enrolled.

Source: The Pensions Regulator (2020) *Automatic enrolment declaration of compliance report, January 2020*

Opt outs and cessations

Employees are permitted to opt out of their pension scheme within one calendar month of being automatically enrolled and receive back any contributions that have been deducted from their pay. If an employee opts out, they will not receive the contributions that their employer made on their behalf. People are permitted to stop contributing to their pension after the opt out period, though they will not be eligible to receive back their contributions and will retain membership in their pension scheme. People cease contributing for several different reasons, for example, because they change jobs or because their economic circumstances have changed and they feel they can no longer afford to make pension contributions.

- Opt out rates remained consistent at an average of 9% across all schemes through to 2017, (post 2017 opt out data is not yet available).
- Around 16% of employees who were automatically enrolled in 2016/17, and did not opt out, ceased saving during the year, 67% of these cessations were as a result of moving jobs.

Source: DWP (2018) *Employers' Pension Provision Survey 2017*

Opt ins

Employees under the earnings threshold or outside the age bands are allowed to request to be enrolled in their employer's chosen pension scheme (this is "opting in"). Employers are required to make minimum contributions on behalf of employees who opt in as long as they are paid above the lower level of the contributions earnings band, £6,136 in 2019/20. It is difficult to determine levels of opt in as some employers automatically enrol all employees whether they are eligible or not. In 2016/17, 8% of employers had enrolled some ineligible employees and in 37% of these cases, employees had requested to be opted in, rather than being automatically enrolled.

Source: DWP (2018) *Employers' Pension Provision Survey 2017*

The charge cap

From 6 April 2015, a cap was placed on the amount that members of default strategies in schemes used for automatic enrolment could be charged. The cap is set at 0.75% per year of funds under management, excluding transaction costs. This measure was introduced in order to address perceived market failures including a weak buyer side (as employers make the choice of automatic enrolment scheme rather than the member) and an extremely complex product that is difficult for lay people to understand. The Office of Fair Trading raised concerns about the variability of pricing in the market and the high charges among some legacy schemes. Therefore, a cap on charges was introduced in order to ensure that those who are automatically enrolled are not disadvantaged through joining a scheme with high charges that will significantly erode the value of their pension savings over time.

Source: DWP (2013) *Better workplace pensions: a consultation on charging*

2017 automatic enrolment review

In 2017, the Government held a review, supported by an independent advisory group (chaired by Ruston Smith, Chair of the Tesco Pension Fund and Tesco Pension Investment Ltd; Jamie Jenkins, Head of Pensions Strategy, Standard Life; and, Chris Curry, Director, Pensions Policy Institute) to consider how to build on the success of automatic enrolment for the future. The review put forth several reform proposals for automatic enrolment, the most notable of which are:

- Lowering the age of eligibility from age 22 to age 18, in order to make pension saving the norm from when people start work.
- Lowering the minimum level of the contribution earnings band to £0, so that contributions by employer and employees are calculated from the first pound earned, in order to increase overall contribution levels, incentivise those with multiple jobs to opt in, and simplify employer assessments.
- Testing targeted interventions on the self-employed, in order to identify the most effective options to increase pension saving among the self-employed.

Source: DWP (2017) *Automatic Enrolment Review 2017: Maintaining the Momentum*

Adequacy of contributions

Current saving behaviour may not result in people achieving adequate incomes in retirement. Many automatically enrolled savers are paying minimum contributions with their employer. However, minimum contributions of 8% of band earnings are unlikely to be sufficient to allow people to replicate working-life living standards through State and private pension income alone. A median earner contributing 8% of band earnings into a pension scheme every year from age 22 until State Pension age would have only a 50% chance of achieving the same standard of living in retirement that they experienced during working life (from State and private pension income). Those who start contributing later or take time out will need to contribute at even higher levels than those contributing steadily from age 22 to have even a 50% chance of achieving working life living standards in retirement. There are several proposed methods and product trials designed to boost contribution rates.

Source: PPI Modelling

Adequacy 1.1: auto-escalation

Auto-escalation is the name for a policy that can be implemented in several different ways. Auto-escalation involves contributions from members (and potentially their employers) rising automatically in line with other changes, such as pay rises or length of time working. For example, a member could agree that their pension contributions will rise by 1% every two years or whenever they receive a pay rise of more than 2%, until they reach a certain total amount. The Save More Tomorrow (SMarT) programme in the United States (US) involves members signing up to initially low contribution rates but agreeing to increase in the future as salary increases through, for example, splitting any future wage increases between pension contributions and take home pay. Many US schemes are adopting SMaRT. In trials of SMaRT, members were more likely to choose to raise contributions in future through the programme than raise them immediately, following the advice of an adviser. More than 50% of members chose to raise contributions through SMaRT, and the majority of these were still in the programme 4 years later.

Source: Thaler, R. H., & Benartzi, S. (2004). *Save more tomorrow™: Using behavioral economics to increase employee saving.* Journal of political Economy, 112(S1), S164-S187

Adequacy 1.2: raising minimum contributions

One of the criticisms of auto-escalation is that it is not a universal policy, so may leave some people out, and that those who change jobs will potentially have their contributions reset at a minimum level. An alternative approach to contribution increases is raising the minimum contributions required under automatic enrolment for everyone, though this may mean that contributions become less affordable for some of those on lower incomes. Increases to minimum contributions do not necessarily need to come solely from employees. Employers could see their minimum required contributions rise as well in order to spread the additional cost burden. An increase of minimum automatic enrolment contributions from 8% to 12% could result in additional contributions from employees and employers of £5.6 billion per annum, assuming no behaviour change. The Pensions and Lifetime Savings association proposed, in their Retirement Living Standards work, that employer and employee minimum contributions be each raised to 6% by 2030, in order to help pensioners achieve adequate incomes.

Source: Jethwa, C. (PPI) (2019) *Understanding the Gender Pensions Gap, Pensions Policy Institute; PLSA (2019) Retirement Living Standards*

Earnings trigger

The £10,000 earnings trigger has come under criticism for leading to a disproportionate number of certain groups: women, ethnic minorities, those in multiple jobs, and carers, being found ineligible for automatic enrolment. There have been calls to reduce the earnings trigger or remove it altogether. However, the original concern that lowering or removing the trigger would result in people who can't afford to save, and who will be able to replace working-life income with State Pension and benefits remains. The next few sections describe the impact of the earnings trigger on women, ethnic minorities, carers and those in multiple jobs.

Earnings trigger 1.1: women

Women are less likely than men to meet the qualifying criteria for automatic enrolment. Of 13m employed women in the UK, around 4m (32%) do not meet the qualifying criteria for automatic enrolment, compared to 16% of male workers. 2.7m women earn below the earnings threshold of £10,000. This may be due partly to women being more likely to work in low-skilled (and low paid) jobs than men. Women are more likely than men to work part-time or in multiple jobs. If the income from both first and second jobs was taken into account when assessing eligibility for automatic enrolment, then a further 80,000 people (60,000 women and 20,000 men) would earn enough to meet the qualifying criteria.

Source: PPI analysis of Labour Force Survey data 2015

Earnings trigger 1.2: ethnic minorities

91% of the Bangladeshi workers, 80% of Chinese workers, 78% of Indian workers, and 63% of Black/African/Caribbean workers who do not meet the qualifying criteria are earning below the £10,000 Earnings Threshold in their main job, compared to 56% of ineligible white employed people. This result implies that low earnings are a greater problem for those ethnic minority groups than for those from the majority white population. If second jobs were taken into account then a further 5% (6,000) of all Bangladeshi workers and a further 1% (3,000) of all Pakistani workers, would meet the qualifying criteria for automatic enrolment.

Source: PPI analysis of Labour Force Survey data 2015

Earnings trigger 1.3: those in multiple jobs

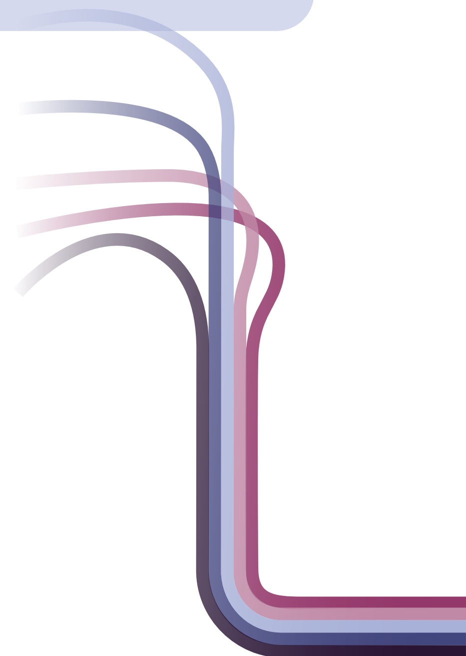
250,000 people in the UK have several jobs which all pay under £10,000 or more. Of these people, 40%, around 100,000, would qualify for automatic enrolment if the income from their different jobs was added together. Of this 40%, the large majority, around 72,000, are women.

Source: Citizens Advice (2017) *People in multiple jobs missing out on a workplace pension, Citizens Advice*

Earnings trigger 1.4: carers

Over three quarters, 81% of employed carers (in receipt of caring related benefits) do not meet the qualifying criteria for automatic enrolment. Many carers work part-time due to their caring responsibilities. 96% of carers who do not meet the qualifying criteria earn below the £10,000 earnings threshold (not including those over or under qualifying age).

Source: PPI analysis of Labour Force Survey data 2015



Taxation: net pay vs. relief at source

Defined Contribution (DC) schemes operate two methods of applying tax relief to pension contributions: net pay vs. relief at source.

- **Net pay arrangements** deduct pension contributions from pay before applying income tax. In net pay arrangements full tax relief at the highest marginal rate is automatically applied to the pension contributions of taxpayers.
- **Relief at source** arrangements deduct 80% of an individual's pension contribution from their salary after deducting income tax and then reclaim 20% tax relief on all contributions from HMRC on a monthly basis. Those who pay higher rate tax, must apply separately to HMRC for any tax relief owed above the 20% rate.

Those who have been automatically enrolled with incomes below the income tax threshold of £12,500 are eligible for Government "tax relief" in the form of extra credits at the basic rate of income tax, to their contributions. As no extra tax relief is contributed to the pensions of those with net pay arrangements, those with incomes below £12,500 miss out on extra Government contributions to their pensions while those in relief at source arrangements receive the extra credits from Government.

The self-employed

Pension participation for self-employed people, who are not eligible for automatic enrolment, has declined from 27% in 2008/09 to 15% in 2017/18. Half (50%) of self-employed people surveyed say they do not trust pensions as a safe place to invest their money (compared to 42% of employees) and a further 12% of self-employed people say they do not know whether or not they trust pensions. This lack of trust creates additional barriers for self-employed saving as engagement is a particularly significant factor for those who are not automatically enrolled.

Source: DWP (2019) *Workplace pension participation and savings trends of eligible employees official statistics: 2008 to 2018;* Citizens Advice (2015) *Shy of retiring*

The self-employed 1.1 Government trials

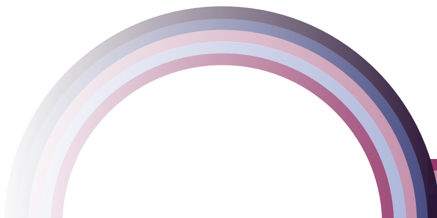
The Government is currently testing a range of approaches (with a range of delivery partners, including NEST Insight, IPSE, Smart Pension, Aegon, Aviva plc, Lloyds Banking Group plc and Barclays plc) designed to gather data on and encourage greater pension participation for, the self-employed. The focal points for these trials are: movements between employment and self-employment; points of contact; and, accessibility of savings. The trials test a range of approaches designed to encourage the self-employed to start saving, (either through short-term savings vehicles, for example, an ISA, or into a pension scheme or other long-term savings product), or to re-start contributions into an existing pension. NEST is currently trialling messaging such as 'save £2.50 a day', or just pay 'what you can when you can' with the self-employed.

DWP (2018) *Enabling retirement savings for the self-employed: pensions and long term savings trials* Department for Work and Pensions

The pensions dashboard

The 2016 Budget, announced the introduction of Pensions Dashboards that would allow individuals to view their own pension portfolios together, including both Defined Contribution (DC) and Defined Benefit (DB) pensions from the public and private sector, and any State Pension entitlement people have accrued. It is anticipated that the dashboards will give people estimates of how much retirement income they might be able to yield from State and private pensions under different scenarios of future contributions. The Government is currently working on providing a publicly run dashboard alongside several industry hosted dashboards.

Source: *www.pensionsdashboardproject.uk/saver/about-the-pensions-dashboard/*



Lessons from Australia

Australia has operated a compulsory automatic enrolment (Superannuation) scheme since 1992. Australian superannuation differs from automatic enrolment in the UK in several significant ways, but one of the most significant is the length of time the policy has been in place, 28 years, in Australia compared to 8 years in the UK. Australian Superannuation minimum contribution rates are currently 9.5% (all from the employer), rising to 12% by 2025. As Australia has had more years to learn from automatic enrolment than the UK, it's useful to consider some of their policy conclusions when looking at future UK policy; these include:

- Size matters: the size and scale of these schemes (each with 2 million plus members), now operating for several decades has allowed cost reductions for members and more investment opportunities, for example into infrastructure.
- Allowing members to choose which scheme their employer pays contributions into has increased competition between schemes to offer better returns. (Instead of capping fees, Superannuation schemes are required to provide transparent data on investment returns net of charges which allows for members and employers to measure performance and compare schemes).
- Making transfers easier encourages choice: members can easily switch between schemes using a national online platform.

Source: *https://www.raconteur.net/hr/can-uk-learn-australias-pension-provision;*
https://www.raconteur.net/hr/can-uk-learn-australias-pension-provision

Questions for further discussion

The following questions will be addressed in today's workshops:

- What are the key lessons from automatic enrolment?
- What could have been done better?
- What policies or behaviours should we encourage/do more of and what elements of the current system do we wish to discourage/do less of?
- What needs to be considered when implementing the 2017 automatic enrolment review recommendations and over what timeline should they be implemented? (Please see section on 2017 review).
- What should be the role for government, industry, and employers in implementing these?
- What type of evidence will be required to inform the policies?
- What outstanding issues still need to be addressed, and what are the potential means for addressing them?