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Today's survey results point the way ahead to build 'pensions fit for purpose' - pensions that must attract higher contributions than at present...

SURVEY FINDS SIX OUT OF TEN EMPLOYERS BACK AUTOMATIC ESCALATION SCHEMES TO BOOST PENSION SAVINGS

30 December 2013 – A major survey of pension trends conducted by the Association of Consulting Actuaries (ACA) has found pension savings into workplace defined contribution schemes have largely flatlined over the last decade, with average rates of contribution set to fall over the next few years because of low initial auto-enrolment contributions¹. However, close to six out of ten employers support the idea of 'auto escalation schemes'², where pension scheme members are encouraged to increase their rate of contributions at a future date often in line with increases in earnings.

The 2013 ACA Pension trends survey, following a questionnaire broadcast in the summer of this year, received responses from 308 employers with over 430 pension schemes covering every size of business. As well as examining trends in pension contributions, the survey looks at firms' experiences and expectations from auto-enrolment and views on the Government's latest workplace pension proposals.

Key survey findings in today's report are:

- **Employers responding to the survey report average rates of contributions into defined contribution pension schemes have changed very little over the last decade – contribution rates are generally failing to keep pace with the pension costs of longer life-spans and an economic climate with low investment returns.**
- **Employer contributions into defined contribution pension schemes across our sample are averaging between 4½% and 7% of earnings as a whole, with relatively small variances below (generally smaller employers) and above this figure (generally larger employers). Employee contributions hover between 4% and 4½% of earnings, again with employees of larger firms typically contributing above this figure and those of small employers below.**
- **Close to six out of ten employers (57%) support the idea of 'automatic escalation schemes' where pension scheme members are encouraged to increase their pension contributions at a future date often in line with increases in earnings.**
- **The processes involved in preparing for auto-enrolment is ranked as the most problematic area of auto-enrolment, followed by regulatory complexity (ranked top problem by smaller employers), with communications ranked fourth (but second by large firms).**
- **Eight out of ten smaller employers have not yet budgeted for the likely increase in costs arising from auto-enrolment (see Figure 2, over page).**

¹ Under auto-enrolment at present a minimum of 2% of qualifying earnings (split evenly between the employer and employee) is required on earnings between £5,668 and £41,450 (2013/14 levels) for eligible employees aged at least 22 and under SPA, who earn at least £9,440 per annum. From October 2017 employers will be required to contribute a minimum of 2% on qualifying earnings as part of a total minimum contribution of 5%. The minimum employer contribution will rise to 3% in October 2018 supplemented by the jobholder's own 4% contribution and 1% in tax relief.

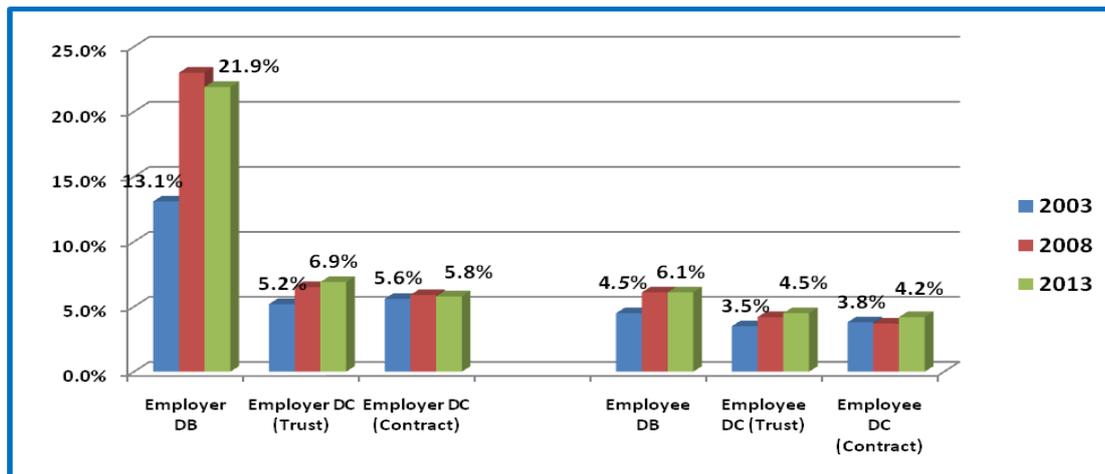
² Auto-escalation encourages people to commit to increasing their pension contributions at a future date, often in line with salary increases. Once signed up, an individual no longer has to take active decisions to increase their contributions – that happens automatically. By synchronising the point of increase in contributions with an increase in earnings, individuals not only defer to a later date the loss of immediate income that an increase in contributions represents, but also know that when it comes, it will be tempered by their overall income increase.

- **When budgeting for the cost of auto-enrolment, the median band of large firms (with 5000 or more employees) expected employee opt-out rates to be between 6% to 10%, however the median band of small employers (with 49 or fewer employees) are budgeting on the basis of employee opt-out rates of between 26% to 30% (see Figure 3, over page).**

Commenting on the survey results **ACA Chairman, Andrew Vaughan** said:

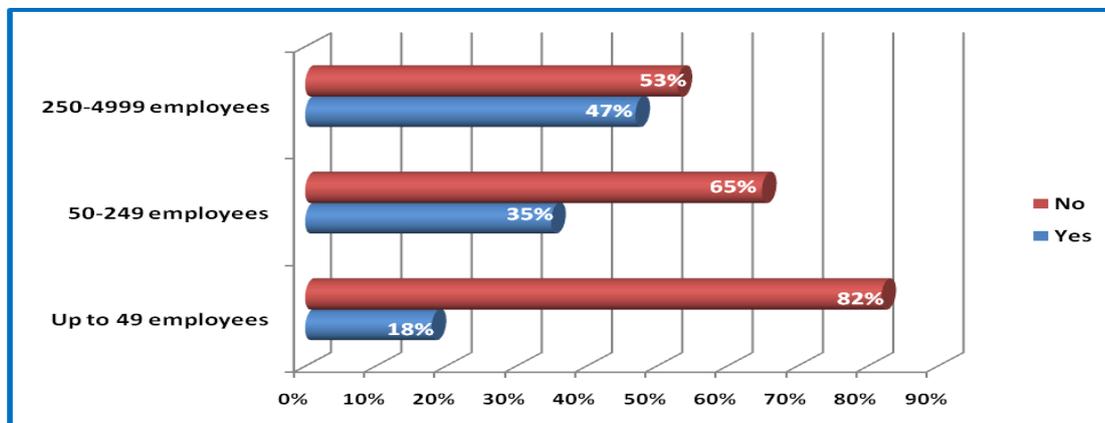
“With most employers seemingly auto-enrolling at the minimum level of contributions (2% of qualifying earnings)³, we can expect average contributions to decline over the next few years before climbing in 2018, when the minimum of 8% of qualifying earnings will be required in all firms. Auto-enrolment on its own isn’t enough. That is why we support the ‘Defined Ambition’ agenda and the survey is also encouraging in showing employers’ support for auto-escalation schemes. In our survey report, we explore the virtues of a ‘Save More Tomorrow’ initiative⁴, which has worked in the USA and is worthy of consideration as a means of encouraging higher pension contributions over the years ahead as the economy grows – increased contributions that are essential as lifetimes in retirement extend. And with the State Pension Age moving towards 70 for today’s younger employees, the added value of higher private pension savings is becoming clear. It is certainly time to save more for tomorrow.”

Figure 1: Comparison of average employer and employee contributions 2003 - 2013 (as a percentage of earnings)



(Source: ACA 2013 Pension trends survey, Second Report, Table 4, page 25 and ACA 2003 and 2008 Pension trends survey)

Figure 2: Have you budgeted for the likely increase in costs that could arise from auto-enrolling all eligible jobholders into your chosen scheme?

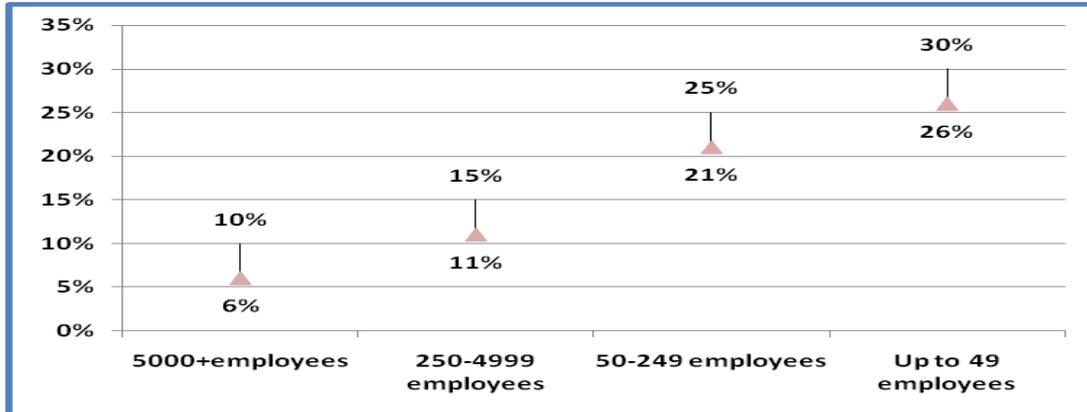


(Source: ACA 2013 Pension trends survey, Second Report, Table 13, page 29)

³ The DWP’s *Automatic Enrolment evaluation report 2013*, published November 2013, Research Report No.854, notes ‘in order to manage contribution costs, the majority of larger employers (have) set their contributions at the minimum level required’, page 28.

⁴ See Second Report of *ACA 2013 Pension trends survey – Time to save more for tomorrow*, pages 8-9.

Figure 3: Assumed employee opt-out rates when budgeting for auto-enrolment (median band of employee opt-out rates by employer size)

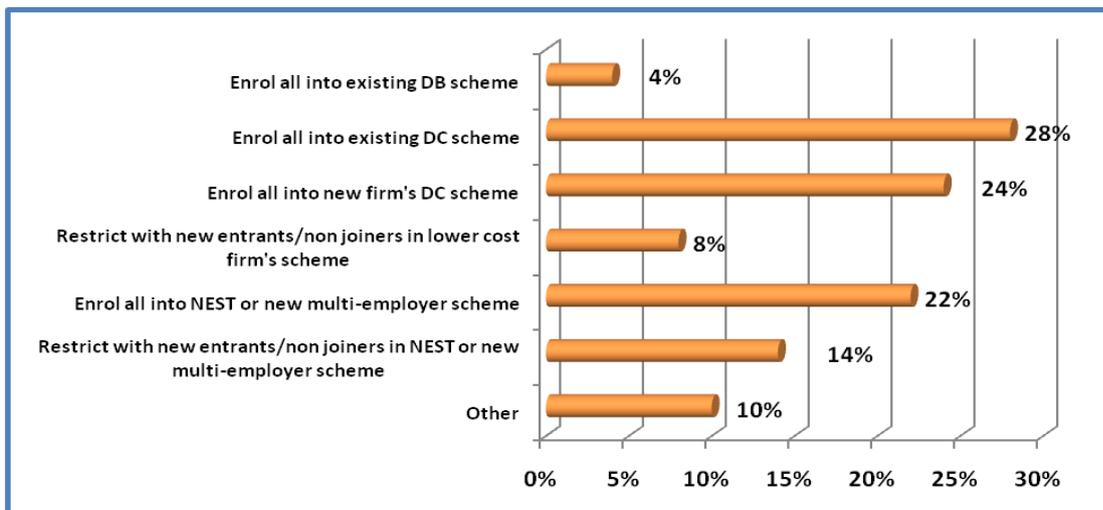


(Source: ACA 2013 Pension trends survey, Second Report, Table 13, page 29)

Other survey findings

- A majority of employers (61%) expect their payroll costs to rise by up to 2% as a result of auto-enrolment, but close to half of smaller employers (46%) expect payroll costs to rise by more than this.
- As a result of auto-enrolment, whilst just over a half of employers expect to enrol all eligible jobholders into either an existing or new defined contribution scheme sponsored by the firm, a fifth expect to enrol employees into NEST or a new multi-employer scheme (see Figure 4 below). However, half of small employers (up to 49 employees) have not yet made a decision on their auto-enrolment scheme provider.
- A fifth of employers expect to restrict previous non joiners and new entrants to a lower-cost scheme sponsored by the firm or a multi-employer scheme or NEST.
- Whereas, at present, around eight out of ten employers say their employees typically retire at age 65 or younger, by 2020 two-thirds expect the typical retirement age to be 66 or later. Not far short of a half then expect typical retirement ages to move out to between age 68 and age 75 by 2028.

Figure 4: As a result of auto-enrolment what has been/will be your most likely change to your workplace pension arrangements?



(Source: ACA 2013 Pension trends survey, Second Report, Table 15, page 30. Note: More than one answer given by some respondents)

The survey report notes that over the next 18 months, around a further 35,000 employers with 50 or more employees will be required to auto-enrol eligible jobholders, with many other employers covered by later staging dates working through exactly how they will comply. This is a ten-fold increase in employers subject to auto-enrolment duties compared to the first year. However, from June 2015, a further 1 million small (5 to 49 employees) and micro employers (4 or fewer employees) must auto-enrol eligible employees in just over a two-year period. This represents about a 170-fold increase in the number of employers subject to auto-enrolment duties compared to the last 12 months! The report questions whether it would not be wise to have a pause in staging ahead of micro employers being subject to auto-enrolment duties whilst providers, advisers and the Pensions Regulator take a breather.

The first report of the *ACA 2013 Pension trends survey* found support for some of the principal ideas outlined in the Government's consultation paper⁵ on 'Defined Ambition' workplace pensions published in November 2013. Larger employers expressed support for legislation that would allow 'core' defined benefit schemes, the ability for employers to adjust pension ages in a timely way and for leavers' benefits to be automatically converted into a defined contribution scheme. Smaller employers said scheme membership and pension contributions would be significantly higher if defined contribution schemes secured a guaranteed pension income building up year by year (see *Appendix* for a summary of the First Report's findings).

For a copy of the survey report 'Time to save for tomorrow', published on 2 January 2014, and 'The unfinished agenda: growing workplace pensions fit for purpose', published on 7 November 2013, go to www.aca.org.uk (see 'Research and Surveys' page).

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About the Association of Consulting Actuaries (ACA)

The **Association of Consulting Actuaries (ACA)** is the representative body for consulting actuaries, whilst the Institute and Faculty of Actuaries is the professional body. The ACA has 1,750 members working in around 80 firms. ACA Members are all qualified actuaries and all actuarial advice given by members is subject to the Actuaries' Code. The ACA forms the largest national grouping of consulting actuaries in the world.

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⁵ *Reshaping workplace pensions for future generations*, published 7 November 2013 (Cmnd 8710).

Appendix: Summary of results of First Report of ACA 2013 Pension trends survey

The survey report, '*The unfinished agenda: growing workplace pensions fit for purpose*⁶, forms part one of the *ACA's 2013 Pension trends* survey. It focuses on questions posed to employers over the summer based on the initial reform ideas first outlined in the DWP's workplace pension reinvigoration paper⁷, published in November 2012.

Key findings

- **Whilst most smaller employers expressed no view on the principal Defined Ambition (DA) ideas that look to retain an element of defined benefit⁸, firms employing 500 or more employees said they were supportive of legislation to permit the following designs :**
 - ✓ **Core defined benefit schemes with no requirement to index benefits on an annual basis,**
 - ✓ **An option for a defined benefit scheme where employers could automatically convert leavers' benefits to a defined contribution scheme (and possibly retirees' benefits to an annuity),**
 - ✓ **An ability for employers to adjust scheme pension age in line with changes in State Pension Age or some other objective index.**
- **Six out of ten employers said they thought there would be a significant difference in the number of employees who would consider joining (or staying in) a defined contribution scheme or who would pay higher contributions if the qualifying default fund secured a guaranteed pension income building up year by year.**
- **A clear majority of employers support a fixed-term pension enabling retirees to draw an income from a small pension pot over a few years rather than converting their pot into what might otherwise amount to a small monthly or annual retirement annuity (Note: *The Pensions Minister has said recently that he intends to set up a task force to look into new ways scheme members can draw down their pension savings*).**
- **A significant number of employers felt that a fixed-term pension should be restricted to only those retirees who defer their State pension (which is then paid at a higher level), with others also saying that such a facility should not be available to those retiring earlier than State Pension Age.**
- **Six out of ten employers oppose the Government taking a role in encouraging consolidation of schemes in the pensions market, with smaller firms most strongly opposed to such an initiative.**
- **Over three-quarters of larger employers (with 1,000 or more employees) said they would not offer a multi-employer scheme, whereas over three-quarters of smaller employers (499 or fewer employees) agreed that a decision to opt for a larger multi-employer arrangement was either likely or possible in their circumstances.**

⁶ For a copy of the Report, published 7 November 2013, go to www.aca.org.uk (Research and Surveys page).

⁷ *Reinvigorating workplace pensions*, published by the Department for Work and Pensions, November 2012 (Cm 8478).

⁸ For a summary of the principal DA ideas see DWP paper, *Reshaping workplace pensions for future generations*, pages 6-8 and pages 16-48.