



EMBARGO ON PUBLICATION UNTIL THURSDAY 1 SEPTEMBER 2011

Only just over a quarter of employers have budgeted for the potential increased cost of pension auto-enrolment...27% are likely to mitigate extra costs by reviewing existing pension benefits...smaller employers are expecting 35-40% of employees will opt-out of workplace pensions following auto-enrolment...

MAJOR PENSIONS SURVEY FINDS A THIRD OF LARGER EMPLOYERS ARE LOOKING TO REDUCE THEIR SPEND ON WORKPLACE PENSIONS AS ADDED COSTS OF AUTO-ENROLMENT LOOM

1 September 2011 – A third of larger employers¹ are looking to decrease their spend on workplace pensions at the very time when they need to be considering the possibility of a higher spend, with auto-enrolment looming over the next year or so. Only just over a quarter of employers have budgeted for the cost of auto-enrolment, with those larger employers that have basing their budgets on expecting between 12-17% of employees to opt-out of workplace pensions after being auto-enrolled. Smaller employers are budgeting on between 33-39% of employees deciding to opt-out. Reflecting presumably the pressure on employee incomes over the last 3 years, 21% of employers report that member opt-outs from pension schemes have increased. These are a few of the findings of the initial report of the *2011 Pensions trends survey* conducted by the Association of Consulting Actuaries (ACA).

73% of employers say they are likely to auto-enrol all employees into their existing workplace pension scheme(s), with 21% saying they are likely to enrol all employees into a new scheme. However, 27% of employers say they are likely to review their existing pension benefits to mitigate the cost of higher scheme membership in anticipation of additional costs arising from auto-enrolment, with this rising to over a third (35%) amongst the largest employers².

Conducted over the summer, the ACA survey gathered responses from 468 employers, of all sizes, with scheme assets exceeding £114 billion. At present, around 38% of UK private sector employers provide a workplace pension scheme, but all will be required to auto-enrol their employees into a 'qualifying workplace pension scheme'³ under the Government's pension reforms between late 2012 and early 2016. By October 2017, minimum contributions must be 8% of employee earnings, with a minimum of 3% from the employer plus 4% from the employee and 1% by way of tax relief, albeit employees have an opt-out which also removes the employer's need to contribute.

¹ Employers with 250 or more employees

² Employers with 5,000+ employees

³ A pension scheme that meets or exceeds certain legal standards, including a minimum employer and employee contribution.

Employers said that employees who did not presently join their schemes mainly because of cost (92%) with 61% also not joining because they felt employees were 'disillusioned with pensions'. Almost all (94%) of the mainly smaller employers responding to the survey without a scheme said 'cost' was the main reason they did not provide pensions at present.

Key survey findings include:

Today's pension provision and trends

- Where final salary schemes are provided, 91% are closed to new entrants with 37% of these also now closed to future accrual of benefits (up from 18% two years ago). The predominant types of pensions provided by employers responding to the survey are Group Personal Pensions, Stakeholder and Trust based defined contribution schemes.
- Across most types of schemes, membership participation in workplace pensions varies between 45-70% of employees, with Stakeholder pension participation lowest at, on average, 45% of eligible employees.
- 30% of employers are either presently reviewing their pension arrangements or will do so in the year ahead. However, despite the approach of auto-enrolment, a half of employers have no plans to review their scheme.

Pension spend and contributions

- 47% of employers do not have a target for their pension costs, but 43% are targeting employer pension costs of 4% of payroll or more. However, amongst employers with 49 or fewer employees – where the bulk of private sector firms are found – only just over a quarter (28%) are looking to a pension spend at or above this 4% level.
- Overall, employers responding to the survey report average combined employer and employee contributions into defined contribution schemes ranging between 7½% and 12½% of earnings. Average combined employer and employee contributions into defined benefit schemes remain at over double these levels at 27% of earnings.

Auto-enrolment and NEST

- 73% of employers say they are likely to auto-enrol all employees into their existing workplace pension scheme(s), with 21% saying they are likely to enrol all employees into a new scheme. A fifth may restrict entry into their existing scheme and auto-enrol the balance of employees into NEST.
- At least two-thirds of employers presently offering no pension scheme say they are unlikely to auto-enrol employees into either NEST or an employer's scheme. This suggests many smaller employers have as yet not understood the new legal requirements. Of those that seem to have addressed them, 25% are likely to use NEST and 11% set up an employer's scheme.

Other pension reforms

- In all three areas of investment, longevity and inflation risk, at least half of the employers responding to the survey say that employers should share or take on a majority of these pension risks.
- 56% of employers support the proposal that further increases in State Pension Age should be linked automatically to average increases in life-spans as reported on by an independent body, although the majority of larger employers would prefer that any recommendations be subject to a final decision being made by Government.

- **64% of employers say they want a statutory override that would enable them to adjust their scheme pension age automatically as life-spans extend. The ability to move automatically in line with State Pension Age is the most popular approach (39%).**
- **Upwards of eight out of ten employers support the recommendations made by Lord Hutton that public service pensions should be scaled back (85%), that member contributions should increase (79%) and that the pension age in such schemes should increase to the State Pension Age (91%). Over half (56%) support the continuation of defined benefit provision for public service employees but, of these, only 16% support the continuation of existing benefit levels.**

Commenting on the survey results, **ACA Chairman, Stuart Southall** said:

“The results of our latest *2011 Pension trends survey* are alarming in a number of ways. They point to a rising trend amongst employers of all sizes to review existing pension arrangements and, given the economic climate, for a goodly number to seek ways to reduce their pension costs. It appears the austerity message has been grasped by many private sector employers as they begin to focus on the potential costs of pension reforms around the corner from 2012. This is understandable but, with not much more than a third of private sector employees now in pension arrangements and with many of these set to deliver very modest retirement incomes, the survey findings are disappointing in terms of the need to boost rather than diminish retirement incomes into the future.

“As things stand, there is a clear danger of more ‘levelling-down’ – a trend which our surveys have identified for some years now. With contribution rates into many schemes failing to keep pace with the pension costs of longer life-spans, and with employers expecting, and in some cases relying upon high anticipated levels of pension opting-out for budgetary purposes to keep their auto-enrolment costs down, warning bells are ringing.

“Yes, it is good news that auto-enrolment should widen pension coverage, particularly where no pensions are offered at present. Hopefully, the communications campaign associated with the reforms will mean employees’ general understanding about the need to save much more for a comfortable retirement will be a success, although I am not sure the Government has as yet really grasped the financial pressures falling on the target groups for auto-enrolment over the next few years. Nor, in my view, have they been sufficiently ‘in listening mode’ about ways in which they might encourage more employers to do better than simply the basic. The preparedness of employers to share risks, echoed by the survey results, and the endorsement of this approach by the *Workplace Retirement Income Commission*, to open up new pension designs, needs to be followed up with some urgency.”

The ACA Pensions trends survey report - *Workplace pensions: the alarm bells are ringing* is available at www.aca.org.uk (see: recent publications).

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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 75 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.