Auto-enrolment is set to celebrate its 5th anniversary in the UK in 2017. Patrick Heath-Lay and Ruston Smith from The People’s Pension talk to us about the policy and structural challenges ahead, as the industry looks to build on the success of auto-enrolment over the next five years.
Auto-enrolment has been one of the most successful government policies of the last two decades. Designed to reverse the decline in the UK’s occupational pension coverage, it has brought seven million new members into defined contribution schemes.

Harnessing inertia — members have to opt-out rather than opting-in — has been the key to the success of the policy. National opt-out rates remain at around 10%. However, although the policy has been successful at dramatically increasing the number of people with a workplace pension, there are still significant challenges.

Aiming Higher

While it’s admirable that there has been an increase in the number of people with an occupational pension, contribution levels are generally far too low.

Current legislation calls for contribution levels to rise to 3% from employers and 4% from employees by April 2019. But there is a danger these increases in contribution levels will be derailed. Patrick Heath-Lay, chief executive officer of The People’s Pension, says: “These could be open to political interference as they will happen shortly before a general election.”

Even if the increases remain on track, they are not sufficient. Most pension consultants suggest that contribution levels need to be closer to 10% or 15% to ensure a comfortable retirement.

Educate or Escalate?

There is a hope that members will become more engaged in their pensions and will take active decisions to ensure they can have a comfortable retirement.

But it would be unrealistic to expect this engagement to happen in the near term. Heath-Lay comments: “There would need to be serious investment in financial education before we could see the benefits.”

In addition, pensions are considered to be too difficult and complicated for most people. And thinking about long-term financial plans runs counter to human behaviour — we prefer short-term goals.

Heath-Lay states: “The onus for ensuring that contribution levels are increased lies with the government.” Like auto-enrolment, this process should harness member inertia and automatically escalate payments over time.

Thinking about long-term financial plans runs counter to human behaviour — we prefer short-term goals.

CONTRIBUTION LEVELS NEED TO BE CLOSER TO 10–15% to ensure a comfortable retirement

Source: SSGA

3 Source: SSGA.
**Widening the Net**

While auto-enrolment has introduced millions to an occupational scheme, there are significant groups who lack pension provision — the self-employed and those with multiple jobs below the current earnings threshold.

Developing an effective auto-enrolment policy for the self-employed is tricky. Heath-Lay says: “The difficulty is figuring out how to incentivise self-employed people to save when there is no employer to match contribution levels.”

The government cannot afford to shirk its responsibilities to the self-employed or those with multiple jobs. And it needs to address the issue of inadequate contribution levels. Heath-Lay says: “If the government wants to ensure people can fund their retirement without relying too heavily on the state, it needs to address these issues.”

Whether the government will find the time to address these policy issues as it navigates the tricky waters of Brexit, however, is doubtful. In the meantime, the retirement industry can play its part to improve the savings landscape.

**Consolidate**

A key issue the industry could tackle without the involvement of the government is the proliferation of small pots — each time an employee moves jobs, they could potentially be auto-enrolled in a new scheme.

Providing pensions to people with multiple jobs is perhaps an easier conundrum to solve.

Heath-Lay says: “As each job is considered individually, people with multiple jobs are not auto-enrolled even though their total pay might be considerably more than £10,000.” The earnings threshold for auto-enrolment is £10,000. Making auto-enrolment mandatory would be the simplest way to solve this conundrum.

Having multiple pension pots is an exceptionally inefficient way to look after a pension as there is no consistent investment strategy and administration costs balloon. Heath-Lay says: “This is a huge issue which needs addressing.”

It presents a number of different challenges. Ruston Smith, Trustee at The People’s Pension, comments: “Each time a member changes a job there is a chance they could decide to opt-out of their pension as there will be a new auto-enrolment process.”

The industry cannot afford to become too complacent about low opt-out rates. Smith states: “There’s a danger the industry could think its job done, but auto-enrolment and individuals’ choice to rejoin or not will continue throughout the working life of a member.”

Smith says: “This trend is only going to accelerate as people are expected to have many more employers than previous generations.”

Heath-Lay comments: “It should be much easier for a member to simply keep paying into the same pension pot, irrespective of where they are working.” Adding, “Opting for a master-trust, like The People’s Pension, would provide a good solution as it can be used irrespective of the employer.”

Smith adds: “The increased scale of the largest master trusts means that if a member changes employers, they may not necessarily change provider. Standards and services of master trusts are continuing to improve and innovate — benefiting members.”

Having multiple pension pots is an exceptionally inefficient way to look after a pension as there is no consistent investment strategy and administration costs balloon.
The Pensions Dashboard

The creation of a pensions’ dashboard would help to reduce the number of pension pots as it would allow easier comparison of different pension policies. But this is a complex exercise. Heath-Lay says: “There are number of difficult technical stages which have to be completed, however, before this can be achieved.”

To create a dashboard, there has to be a central, trusted source of data — this is a huge project involving high volumes of data from hundreds of pension providers. But if this can be achieved, it would revolutionise the industry, argues Heath-Lay. “This project would result in the industry agreeing on the pension data standards, which aligns all the providers.”

Once this can be agreed, this standardisation will make it much easier for people to consolidate their pots with one provider or retain their current provider through multiple employments via an additional centralised clearing service.

Heath-Lay says: “This will cut down on unnecessary replication in the system and lower the cost of administration as it will be much easier to trace individual members.” The cost of establishing the pensions’ dashboard could be easily recouped from the costs of trying to find members at retirement, he adds.

5 YEARS ON – 5 KEY PRIORITIES

1. Automate – More people are saving, but rates remain insufficient. Auto-escalation will help harness inertia and nudge to stronger savings behaviours

2. Reinforce – Opt-out rates are low, but it’s no time for complacency. Particularly for those with multiple jobs

3. Consolidate – Multiple pots mean multiple costs. Complex to address, but the need is set to intensify

4. Embrace – Bringing the benefits of DC to the self-employed and those with multiple jobs below the current earnings threshold

5. Engage – Communications and guidance to promote strong savings behaviours and facilitating choice at retirement

The People’s Pension

The People’s Pension, provided by B&CE, is a flexible and portable workplace pension. It is a multi-employer scheme with independent trustees and operates on a not-for-profit basis. It is the largest private sector pension scheme in the UK with over two million people auto-enrolled.

Our thanks to:

Ruston Smith, Trustee, The People’s Pension

Patrick Heath-Lay, Chief Executive Officer, The People’s Pension

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