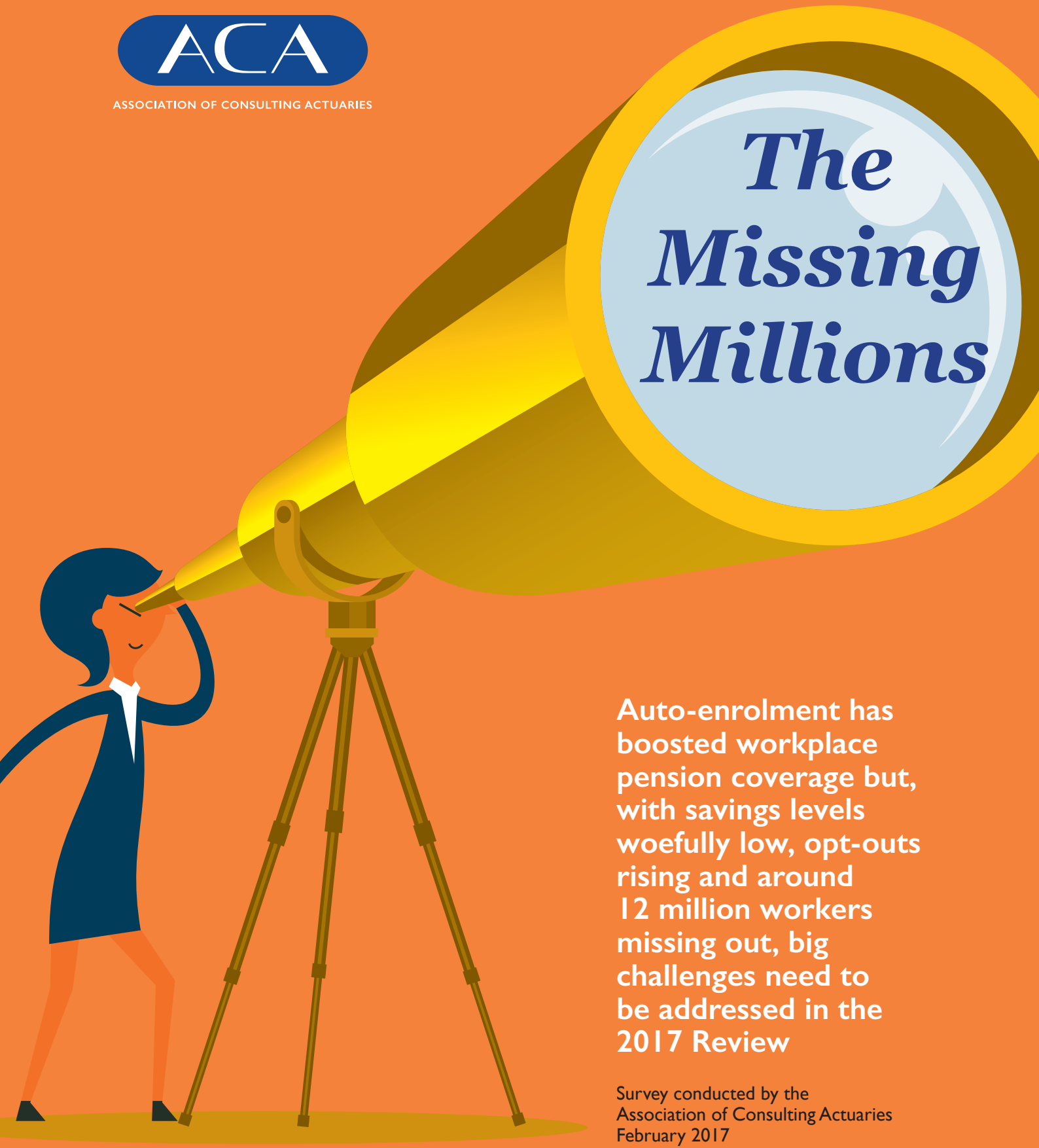
Final Report of 2016/17 ACA
Smaller Firms' Pensions Survey

ACA

ASSOCIATION OF CONSULTING ACTUARIES

The Missing Millions



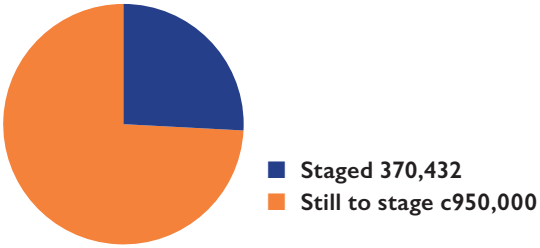
Auto-enrolment has boosted workplace pension coverage but, with savings levels woefully low, opt-outs rising and around 12 million workers missing out, big challenges need to be addressed in the 2017 Review

Survey conducted by the
Association of Consulting Actuaries
February 2017

At a glance survey results

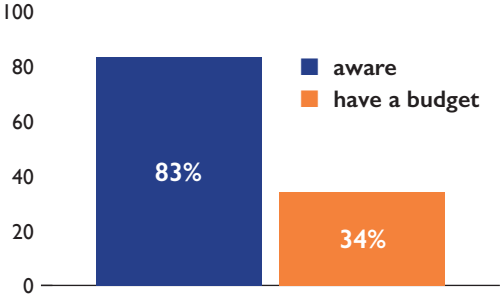
Automatic enrolment in small firms with fewer than 250 employees

Staging



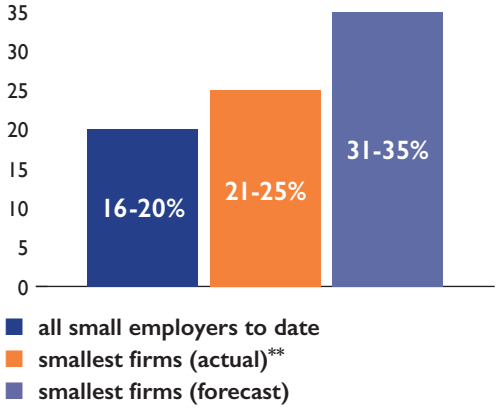
Close to 1 million* ***small employers have to pass their auto-enrolment staging date (as at 31 December 2016). Majority left to stage are micro employers with fewer than 5 workers.***

Awareness



Most of the smallest firms** are aware of staging date, but only a minority have a budget plan.

Opt-outs



Employee opt-outs increasing.

Opt-out reasons

1st Cannot afford

2nd Prefer to spend income

57%

of smallest employers** say auto-enrolment (AE) is 'very complex'.

2–4%

of earnings is the typical AE total pension contributions at small firms.

36–40%

of employees at smallest employers are typically ineligible for AE.

15%

of small firms support increasing minimum contribution rates after 2019.

32%

support lowering the earnings trigger to extend eligibility to join AE.

26%

of the smallest firms say AE will impact on employment.

**Business Population Estimates, 2016.*
***Employing fewer than 10 workers.*

Contents

Chairman's Foreword 5

Key Survey Findings 6

Comment and Ten Policy Recommendations 7

Section 1: Progress of auto-enrolment and pension contributions 10
- Survey respondents
- Complexity hurts the small
- Contributions on the slide
- The new pensions scene: employers that have passed their staging date
- Employers that have not reached their staging date
- Pension contributions – what's the target?
- Steps to 10% and more
- Danger signs
- Support for auto-escalation
- Opt-outs up
- Too many ruled 'ineligible'
- 2017 Auto-enrolment policy review
- Impact of living wage plus auto-enrolment on small firms

Section 2: Summary of findings published in earlier interim reports 17
- Summary of key findings
- Greying workforce
- 2017 Review of State Pension Age
- Moaning about LISA
- What about further pension tax reform?
- Defined benefit schemes: move to CPI with caveats

Footnotes 20

Statistical Appendix: 2016/17 Smaller Firms Pension Survey 21

Auto-enrolment: a quick summary 31

Chairman's Introduction

2016/17 ACA Smaller Firms Pensions Survey

"Sustained contributions at realistic levels are of key importance in delivering an acceptable income in retirement"

We conduct this survey of pension trends in businesses employing 249 or fewer people every second year. In this and our interim reports we have examined how auto-enrolment is progressing as it reaches into the sector and a number of other topical pension issues. At a time of immense change in pensions, we draw conclusions on how in 2017 public policies might need to be adjusted so the improvements in pension coverage over the past five years are built upon and consolidated into the future.

Welcome though auto-enrolment is in extending pension coverage to many more employees, the low level of contributions we again found in this survey from employers and 'new' workplace pension scheme members is a mounting concern. Whilst holding costs down and careful investment is always important, by and large, sustained contributions at realistic levels (we comment later in the report on what this means) are the most important element in delivering an acceptable income in retirement. We have a long way to go if this objective is to be met.

Policy pointers

There are three principal reasons why we believe pension policy needs to be reviewed in 2017 with smaller firms and their employees, who comprise 60% of the UK private sector labour force, particularly in need. The 2017 review of auto-enrolment offers the opportunity to make a start.

First, the income level below which employees are excluded from auto-enrolment is too high. This has meant a large number of employees in all sizes of firms have been excluded from auto-enrolment. In fact, as at 31 December 2016 those ineligible for enrolment broadly are not far short of the numbers that have been added via auto-enrolment. This survey points to those ineligible for auto-enrolment increasing to over 8 million by 2018. When coupled with 4.8 million self-employed, the vast majority with no pension provision, we are looking at over 12 million people outside the auto-enrolment tent.

Second, this problem is compounded by the ONS evidence that employee earnings are on average markedly lower in small firms and notably so where there are fewer than 5 employees. Here over 40% earn below the level entitling them to be auto-enrolled. This means, without a policy change, we could reach the point where the final tranche of ¾ million firms to stage are being chased to register an auto-enrolment scheme and meet compliance rules and costs to deliver up perhaps well under ¾ million employees actually eligible and not 'opting-out'.

Third, the increases in minimum pension contributions in April 2018 and 2019, with probably only modest increases in average earnings over the intervening period, suggest the Government needs to consider whether they must budget for some national insurance or tax concessions to offset these sharp increases in costs. We make suggestions in this report as to how Government might stimulate and protect auto-enrolment by way of using some of the future expected reappraisal of pension tax relief (yes, we still expect further reforms!) to boost the auto-enrolment policy outcome.

In the longer-term, we have advocated for many years that average pension and savings rates must increase so more people enjoy a comfortable income in part or full retirement – and hence we support such initiatives as auto-escalation and the extension of contributions to all earnings up to a ceiling. And, in the near-term, Government may need to be pragmatic and consider simplifying the compliance regime and some targeted financial incentives to help deliver the desired policy outcome of wider and deeper pension coverage in smaller firms. It should at the same time consider how coverage might be extended into the fastest growing sector of the workforce, self-employment, and it is encouraging the 2017 review of auto-enrolment looks set to do this.

Finally, I would like to thank all those firms that responded to the survey questionnaire.

Bob Scott
Chairman
Association of Consulting Actuaries

Key survey findings

This biennial survey has been undertaken since 1996 and we conducted this year's in June/July 2016 for online completion by way of a questionnaire broadcast to over 20,000 of the UK's smaller firms with fewer than 250 employees, selected on a random basis. Responses were received from 455 firms. This final report follows on from three interim reports published in the fourth quarter of 2016.

A summary of the other findings reported in the interim reports can be found on pages 17–19, with a full statistical appendix covering the results on pages 21–30.

Throughout the survey report, we refer to firms with 1–4 employees as 'micro employers'. When we refer to the 'smallest firms' this includes firms with 1–9 employees. Figures in brackets in charts are 2014 survey results.

Low pension contributions are a feature of those newly enrolled into workplace pensions

- For those enrolled into new auto-enrolment schemes, the median employer and employee contributions are much the same at respectively between 1–2% of earnings.
- Those previously enrolled into pension schemes ahead of auto-enrolment (a minority in smaller employers) have generally retained median employer contributions of between 3–5% of earnings with employee contributions of between 2–4% of earnings.
- Only 15% of firms support gradually increasing auto-enrolment contributions above 8% of qualifying earnings after 2019.
- A third of firms support lowering the trigger point of qualifying earnings for auto-enrolment (presently £10,000pa), but support for lowering the trigger falls to 22% amongst the smallest firms.
- 26% of the smallest firms say that auto-enrolment will have an impact on their employee numbers. Furthermore, some 37% of the smallest firms and 29% of all the small firms express the concern that the 'living wage' will impact on employee numbers.

Employers who have already auto-enrolled employees into a workplace pension (70% of respondents)

- Over half of the firms with fewer than 50 employees, rising to over three-quarters with fewer than 10 employees, have found setting up an auto-enrolment scheme 'complex' or 'very complex', with the processes in preparing and new administrative systems involved being cited as the next biggest problems.
- Whilst 47% of the employers with pre-existing schemes have kept those arrangements for existing members, generally previous non-joiners and new entrants have been enrolled into multi-employer arrangements, including NEST.
- Across employers of all sizes the median employee opt-out following auto-enrolment is 16–20% with those not eligible for auto-enrolment ranging between 21–40% of employees, depending on the size of firm

Employers who have not yet reached the date when they must auto-enrol (29% of respondents, including 73% of smallest employers)

- The majority of employers who have not yet reached their staging date presently provide no pension arrangements at all. Where schemes are present, contract DC arrangements outnumber trust-based DC arrangements.
- Where employers have made decisions about auto-enrolment many have decided to enrol all eligible jobholders into NEST or another multi-employer scheme. Amongst those employing 10–49 employees, 37% are proposing this route; amongst those with 1–9 employees, the figure reaches 45% (but with 43% still 'undecided').
- Forecast opt-out rates from auto-enrolment range between 11–35% of employees, with the higher rates forecast by the smallest firms with fewer than 10 employees.
- 'Regulatory complexity' and 'new administrative systems' are the principal concerns that pre-staged firms have about auto-enrolment.

Comment and Ten Policy Recommendations

Micro, small and medium-sized (SME) firms, here defined as businesses employing 249 or fewer employees, form the largest part of the UK private sector economy in terms of employment. There are over 1.3 million of these smaller employers and, with the 4.8 million self-employed, they employ around 60% of the UK's private sector workforce – 15.7 million people in all. They generate just short of a half (47%) of all private sector turnover, amounting to some £1.8 trillion per year, and make up over 99.3% of all UK private sector enterprises.

Auto-enrolment presents real challenges to smaller firms

We are presently mid-stream a Government plan, supported by the major political parties, whereby all firms with one employee or more must auto-enrol their eligible employees into a workplace pension scheme with certain minimum standards. To be eligible, employees must earn more than £10,000pa (the 'trigger point' for auto-enrolment) and be aged between 22 and 65. It is striking that ONS figures suggest over 40% of the employees of micro employers are 'ineligible' for auto-enrolment on income grounds alone (see *Figure 1*, below). A further 4.8 million self-employed and many proprietors are also presently outside the auto-enrolment regime.

The major test for those responsible for monitoring compliance with the pensions auto-enrolment regime (the Pensions Regulator) and for those providing qualifying pension arrangements is to capture data on these 1.3 million firms (the majority with fewer than 5 employees), whilst also being able to cope with the dynamic changes in business numbers each year. In the last year alone, 14,000 employing businesses were formed and over 84,000 non-employing (at least initially) businesses.

Figure 1: UK private sector: number of enterprises and employment by size of firms and percentage of employees ineligible for auto-enrolment by earnings

UK Smaller private sector firms	Number of enterprises	Employees (thousands)	Percentage of employees[1] earning below £10,000pa
No employees (see note below)	4,172,185	810[2]	–
1–4 employees	839,785	1,927[2]	42%
5–9 employees	241,640	1,580[2]	24%
10–49 employees	203,550	3,899[2]	14%
50–249 employees	33,310	3,237[2]	9%
Total: smaller firms (1–249 employees)	1,318,285	10,643[2]	19%[3]

(Sources: Department for Business, Energy & Industrial Strategy, Business Population Estimates, 2016, published 13 October 2016 and estimates from ONS Annual Survey of Hours and Earnings 2015. Note: 'No employees' comprises sole proprietorships and partnerships comprising only the self-employed owner-manager and companies comprising only an employee director).

Progress of auto-enrolling employees into pensions and the 2017 review

At the time of writing, some 370,432[4] employers – private and public sector – have staged for auto-enrolment and completed their declaration of compliance, with some 1 million more of the 1.3 million smaller businesses covered by this survey due to stage over the next 2 years.

"So far, those employees ineligible for auto-enrolment on all grounds working in businesses of all sizes that have staged amount to 27% of their employees"

Those larger employers who have staged employ some 23.8 million of the UK's total workforce of around 32 million. Netting off the self-employed (4.8 million), who are not eligible for auto-enrolment, this means those small employers left to stage harbour around 4 million employees.

So far, those employees ineligible for auto-enrolment on all grounds working in businesses of all sizes that have staged amount to 27%[5] of their employees, with the latest tranche of smaller firms reporting 39% ineligible. Based on the opt-out rates reported and forecast by smaller employers responding to this survey (between 11–35%, depending on size) and the lower percentage of employees eligible for auto-enrolment due to the earnings profile of employees engaged by smaller employers, it seems likely that there are only at best around 2 million more employees[6] eligible and likely to be and remain auto-enrolled over the next 2 years. By then, auto-enrolment will have added some 9 million more employees into workplace pensions, probably around 1 million less than current Government forecasts, but certainly a very creditable improvement on the 2012 starting point.

However, the 840,000 micro employers due to auto-enrol their employees may well contribute fewer than one new employee to auto-enrolment per firm.

The self-employed present a further problem. Presently, the self-employed are not obliged to auto-enrol, but it has become increasingly clear that this fast-growing sector is poorly pensioned. Recent studies[7] suggest fewer than ½ million of the near 5 million full and part-time self-employed have a private pension and, additionally, earnings in the sector are generally low. Pressure is mounting to somehow include them in the auto-enrolment process.

The Government is committed to a 2017 review of auto-enrolment to consider progress and to identify policy initiatives for the period ahead.

All footnotes in this Report are featured on page 20.

Comment and Ten Policy Recommendations

We recommend that the 2017 review consider:

Recommendation 1: On grounds of efficiency and cost, it is difficult to justify micro employers being included in the auto-enrolment project especially if the earnings trigger remains at a level excluding over 40 per cent of their employees. It would seem sensible if the upcoming review looks at how for micro employers and the self-employed the auto-enrolment processes and procedures can radically be simplified to ensure the likelihood of greater participation in pension coverage.

Recommendation 2: It may be that earnings growth in the period from now to 2019 will be such that it will in part address the problem of lower earnings in smaller firms. As things stand we recommend a review of the auto-enrolment earnings trigger in the 2017 Government review (or earlier) given the fact that the current level excludes so many employees. It increasingly discriminates against the high percentage of part-time and notably female part-time employees working in the sector.

Pension contributions: 'wait and see' not enough of a plan

This and other surveys conducted by DWP and ONS have highlighted the low level of contributions into new auto-enrolment pension schemes since its launch in 2012 across employers of all sizes. This has markedly reduced average total pension contributions per head, albeit at present over 7 million more employees are contributing into workplace schemes. Whilst in 2013, ONS reported average total contributions into defined contribution schemes were 9.1% of earnings, the latest report shows these are now just 4%[8].

A very challenging period lies ahead when by April 2019 the total auto-enrolment minimum contribution increases to 8% of qualifying earnings, of which at least 3% must come from the employer and 1% will come from the Government in the form of tax relief[9] plus the balance from employees. Our survey findings suggest increases will impact upon a majority of smaller firms, many of which will also be coping at much the same time with the progression in cost increases driven by the 'living wage' dictated by Government. It would seem likely that unless the Government makes advance plans to mitigate the cost increases involved, there will be an increase in opt-out levels and possibly an employment shake-out, particularly if the economy hits the difficulties forecast by many pundits.

The sharp cost increases falling on both employers and employees who stage late in the process in 2017/18 is a particular worry, as these will be the smallest firms including many new businesses set up since 2012.

All footnotes in this Report are featured on page 20.

We therefore recommend:

Recommendation 3: When and if the Government is considering incentives to encourage enterprise by way of lower taxation and national insurance it should consider whether a share in tax reductions might be earmarked to increasing both or either employer and employee pension contributions. Further increases in the Employment Allowance are a particularly good way of helping smaller firms, part of which could be earmarked for meeting higher pension contributions.

Recommendation 4: The Government, as part of its 2017 review, should consider a means whereby employers staging in 2017/18 are able to phase in their minimum auto-enrolment contributions over perhaps a 3-year period. New businesses should also be considered for such a phasing-in period.

Recommendation 5: As part of its 2017 review, the Government needs to set out a pathway from 2019 as to how increases in minimum auto-enrolment contributions are to be planned over probably a decade ahead. That review should seek to identify a consensus on reforms across the political parties so employers and employees are convinced of the plan's durability. It should identify what support the Government is prepared to commit to adjusting tax and national insurance contributions over the period to support employers and employees alongside what other initiatives, including support for auto-escalation and advisory/educational services, are to be promoted. The ability for both employers and employees to reduce contributions when difficulties arise needs also to be considered so the inflexibilities introduced by legislation and regulation into the defined benefit regime are not repeated in the auto-enrolment regime.

Other recommendations arising from the Survey's interim reports

Our earlier interim reports on the survey identified the rationale for five further recommendations:

Recommendation 6: Whilst we have some sympathy with the view that the Lifetime ISA ought to have been delayed pending the outcome of the 2017 auto-enrolment review to consider its impact on auto-enrolment, matters have moved on. However, we do believe that how LISAs sit alongside auto-enrolment needs to be considered by the review.

Recommendation 7: Pension tax relief should be retained as a valuable encouragement for pension saving, but with more help targeted on lower income groups. As part of a much needed and 'real' simplification process, the Lifetime Allowance should be abolished in the Spring or Autumn 2017 Budgets, as this is set at an unrealistically low level and is causing huge administrative and financial challenges to employers and affected employees.

Recommendation 8: Future changes to the State Pension Age should retain a Universal State Pension, but with measures to allow people greater flexibility over when they can take their State pension below State Pension Age.

Recommendation 9: The Government should amend legislation so the trustees of private sector defined benefit pension schemes can move to CPI indexation of pension benefits by way of a statutory override to scheme rules, as applies to public sector schemes. Reforms should also allow employers to convert historical benefit scales to a single simplified benefit structure on the basis of fair value.

Recommendation 10: Although not directly a finding of the survey, the overall results we believe support the establishment of a standing independent pension commission, which would periodically advise Government on promoting the active extension and betterment of private retirement income provision and making recommendations on the future of State and public sector retirement provision.

All footnotes in this Report are featured on page 20.

Section 1

Progress of auto-enrolment and pension contributions

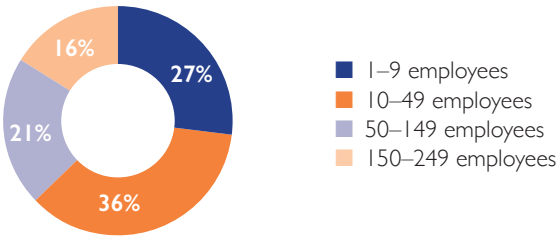
Survey respondents

Just over six out of ten of the firms responding to the survey employ 49 or fewer staff, with the balance of respondents employing between 50 and 249 employees. This sample does not represent a 'mirror image' of the UK's smaller firms sector. If it did, around 98% of the sample would be drawn from firms with 49 or fewer employees[10]. Nevertheless, the sample provides a good cross-section of small firms of all sizes.

Ahead of auto-enrolment, it was estimated around 75% of the UK's smaller firms provided no workplace pension scheme albeit around a further 7% made contributions into employees' personal pensions[11] and notably only 15% of employers with fewer than 5 employees (over ¾ million employers) offered a pension. Auto-enrolment is changing this picture but with much still to be done to bring hundreds of thousands of smaller firms' employees into workplace pension coverage over the next 2 years.

Throughout the survey report, we refer to firms with 1–4 employees as 'micro employers'. When we refer to the 'smallest firms' this includes firms with 1–9 employees. Numbers in (brackets) in Figures are 2014 survey findings.

Figure 2: Smaller firms – employers responding to the survey



(Source: 2016/17 Smaller Firms Pension Survey, see Table 1, page 21).

Of those employers responding to the survey, 70% have passed their staging date for auto-enrolling employees into pensions, with the balance yet to reach their date (see *Table 2, page 21*).

Complexity hurts the small

For those who have completed staging:

The biggest problems found with auto-enrolment were the preparatory stages, the new administrative systems needed to cope with the compliance regime and the ongoing monitoring of earnings, contributions levels and/or eligibility.

For employers yet to stage:

The complexity of the regulatory regime, despite all the efforts put into easing understanding by TPR and providers, is seen as the main problem, again followed by the new administrative systems that small firms are having to consider to comply *(see Figure 3).*

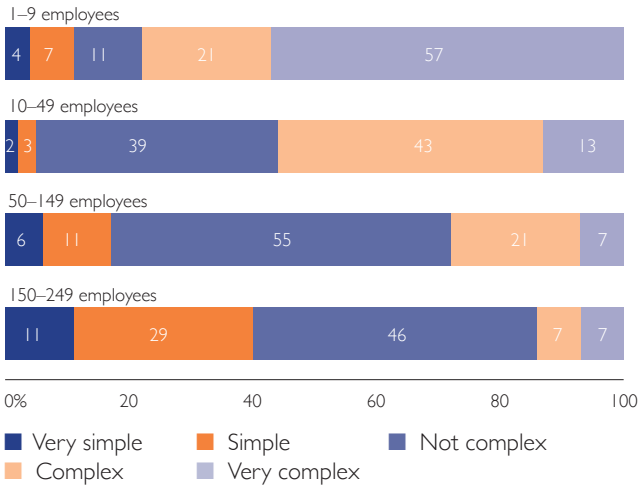
Unsurprisingly, **the smallest firms employing fewer than 10 employees are particularly concerned about the complexity of auto-enrolment with close to six out of ten regarding it as 'very complex'** *(see Figure 4).*

Figure 3: When preparing for auto-enrolment what caused the biggest problem to employers (compared to employers that have not yet reached their staging date)? (in ranked order)

	Employers who have passed staging date	Employers yet to reach staging date
Processes in preparing for change	1	3
Regulatory complexity	3	1
Assessment of options available	4	5
Uncertainty over cost	6	4
Communications	5	6
New administrative systems	2	2

(Source: 2016/17 Smaller Firms Pension Survey, see Tables 3 and 12, pages 21 and 24).

Figure 4: Employers beyond staging date – complexity of auto-enrolment felt hardest by smallest employers



(Source: 2016/17 Smaller Firms Pension Survey, see Table 4, page 22).

All footnotes in this Report are featured on page 20.

Contributions on the slide

The results of this year's survey underscore that DC contributions into schemes established prior to auto-enrolment have stalled with clear indications that the contributions being made into arrangements for previous non-joiners and non-members are at much lower levels, with these new members largely being joined up to NEST or other multi-employer schemes.

"Contributions into auto-enrolment schemes set up for previous non-joiners and new members generally are at a much lower level than for existing scheme members"

The two tables alongside highlight the pension contribution levels being made by both employers and members into pension arrangements where employers have reached their staging date for auto-enrolment (see *Figure 5*) and where auto-enrolment has still to come (see *Figure 6*).

Whilst the total contributions into firms' trust-based and contract-based schemes remain similar to the figures we collected in 2014, supporting DWP feedback that employers have generally not levelled-down contributions to scheme members who pre-dated auto-enrolment, average contributions have inevitably fallen away with so many previous non-joiners and new entrants being enrolled into NEST and other multi-employer schemes at minimum auto-enrolment contribution levels or just above.

Employer and employee contributions into these newer schemes are both ranging between 1–2% of earnings compared to employer contributions of between 3–5% of earnings and employee contributions of between 2–4% for employees previously enrolled in smaller firms' pensions ahead of auto-enrolment *(see Figure 5).*

This evidence supports ONS reports[12] that DC contributions have on average reduced over the last few years because of the reasons stated above. The two charts over the page (see *Figures 7 and 8*) summarise the scale of change in the types of pension arrangements offered by employers that have reached their staging date and the marked trend towards different arrangements being run by these employers for previous non-joiners and new entrants (with these largely attracting lower pension contributions).

Figure 5: Employers beyond staging date – as a percentage of total earnings, median EMPLOYER and median EMPLOYEE contribution into pension scheme(s).

	Employer			
	1–9	10–49	50–149	150–249
Contract DC	3%	3%	3% (4%)	4% (4%)
Firm's Trust DC	3%	3%	3% (5%)	5% (5%)
NEST	<1%	1–2%	1–2% (1–2%)	1–2% (1–2%)
Other multi-employer scheme	1–2%	1–2%	2% (3%)	3% (3%)
Defined Benefit	–	–	16–20% (16–20%)	21–25% (16–20%)
	Employee			
	1–9	10–49	50–149	150–249
Contract DC	2%	2%	2% (3%)	3% (3%)
Firm's Trust DC	2%	3%	4% (4%)	4% (4%)
NEST	<1%	<1%	1–2% (1%)	1–2% (1%)
Other multi-employer scheme	1–2%	1–2%	1–2% (2%)	1–2% (1%)
Defined Benefit	–	–	6% (5%)	6% (6%)

(Source: 2016/17 Smaller Firms Pension Survey, see Table 5, page 22).

Figure 6: Employers yet to reach staging date – if employers already offer a pension scheme, as a percentage of total earnings, median EMPLOYER and median EMPLOYEE contribution into pension scheme(s).

	Employer		**Employee**	
	1–9	10–49	1–9	10–49
Contract DC	3% (4%)	3% (4%)	2% (4%)	3% (4%)
Firm's Trust DC	3% (4%)	4% (5%)	2% (3%)	3% (4%)
NEST	<1%* (1%*)	<1% (–)	<1%* (1%*)	<1% (–)
Other multi-employer scheme	1–2%* (4%*)	1–2% (3%)	1%* (3%*)	1% (4%*)

(Source: 2016/17 Smaller Firms Pension Survey, see Table 16, page 26. Note: Restricted sample).*

The new pension scene: employers that have passed their staging date for auto-enrolment

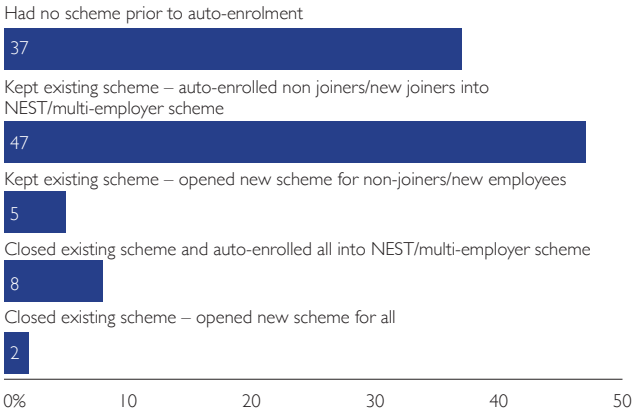
The post auto-enrolment pension scene across smaller employers is beginning to emerge in the results of the survey. Whilst the sample of respondents includes more employers who had pre-existing pension arrangements than the sector as a whole, the pattern emerging is quite striking.

As we have noted, the big change is the major inroads made by NEST and other multi-employer arrangements in covering particularly previous non-joiners and new entrants and, of course, all employees where no workplace pension arrangements existed prior to auto-enrolment.

Whilst 47% of the employers with pre-existing pension schemes say they have kept those arrangements for existing members, they have enrolled previous non-joiners and new entrants into multi-employer arrangements, including NEST.

10% of employers have closed existing schemes, with the majority enrolling all of their eligible employees into NEST or another multi-employer scheme *(see Figure 7).*

Figure 7: Employers beyond staging date – how their workplace pension arrangements have changed as a result of auto-enrolment

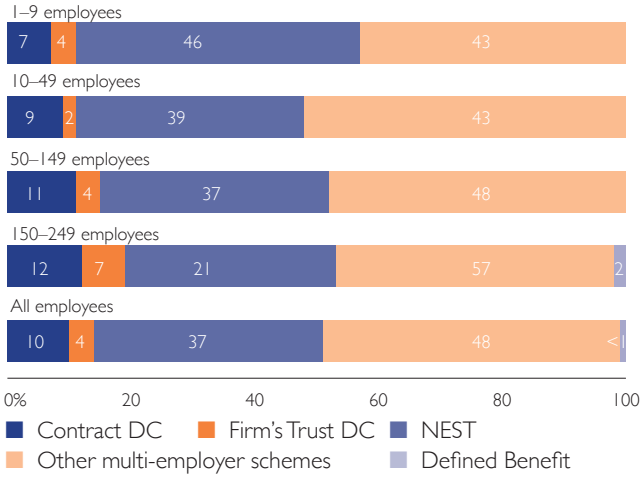


(Source: 2016/17 Smaller Firms Pension Survey, see Table 6, page 22).

Whilst a number of firms' contract DC and trust-based DC schemes are now closed to new members and a larger number also closed to new contributions, such schemes still remain widespread, particularly amongst firms with 50 or more employees that have auto-enrolled to date, but with NEST and other multi-employer schemes beginning to capture a significant share of those 'new' to pensions (see *Table 7*, page 23).

It will be interesting to see in future surveys whether the structure of schemes will change as the minimum contribution levels are increased in April 2018 and 2019 and, in particular, whether there will be a rationalisation in the number and spread of schemes being run by these employers *(see Figure 8).*

Figure 8: Pension arrangements used for auto-enrolment by employers for who have passed their staging date



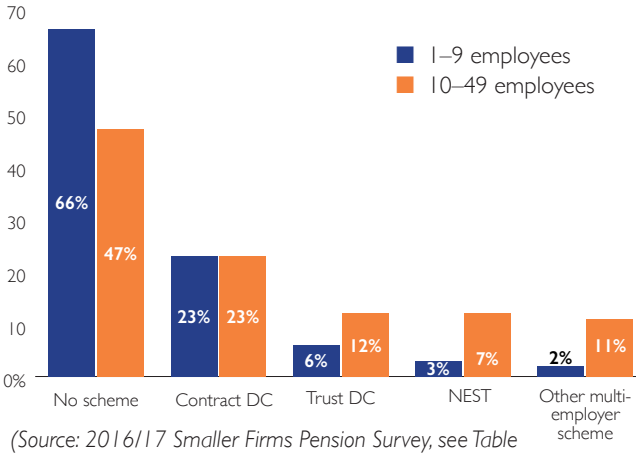
(Source: 2016/17 Smaller Firms Pension Survey, see Table 8, page 23).

Employers that have not reached their auto-enrolment staging date

The picture of pension provision for those employers who have not staged is very different from that described above.

Whilst there is some evidence of multi-employer arrangements being established ahead of staging dates, the majority of these smaller employers presently provide no pension arrangements at all. Where there are existing schemes, contract DC arrangements outnumber trust-based DC arrangements *(see Figure 9)*.

Figure 9: Pension arrangements of employers that have not yet reached their auto-enrolment staging date



(Source: 2016/17 Smaller Firms Pension Survey, see Table 13, page 25).

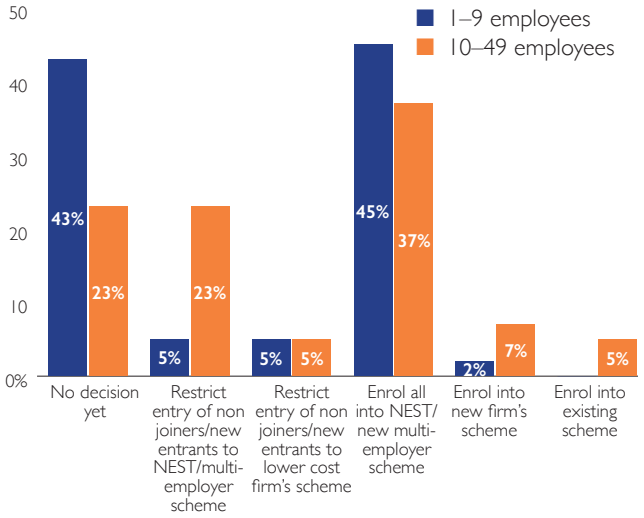
Of the employers that have yet to reach their staging date none auto-enrol all of their employees into a pension arrangement, although 9% auto-enrol some employees into an existing scheme *(See Table 14, page 25).*

All footnotes in this Report are featured on page 20.

Where small and micro employers have made decisions (and 43% of micro employers have not) by far the largest number have decided to enrol all eligible jobholders into NEST or another multi-employer scheme. Amongst those employing 10–49 employees, 37% are proposing this route; amongst those with 1–9 employees, the figure reaches 45% (but with 43% still 'undecided' *(see Figure 10)*).

To a degree the final destination of those to be auto-enrolled, particularly in the micro sector, will depend on which providers are prepared to offer arrangements. With a statutory requirement to offer a scheme to all comers, our expectation is that NEST will take an increasing share of enrolments as staging reaches more of the smallest entities, with many other providers considering this market to be uneconomic, although since 2012 a few other large providers have adapted their offerings to encompass very small firms.

Figure 10: Employers yet to reach staging date – employers' likely decisions in setting up/changing their workforce pension scheme when they are required to auto-enrol employees into a scheme



(Source: 2016/17 Smaller Firms Pension Survey, see Table 15, page 25).

Pension contributions – what's the target?

The survey results suggest the overall slide in average DC contributions across employers will continue over the next 18 months as more small and micro employers auto-enrol employees at near minimum statutory contribution levels ahead of the planned hike in minimum contributions from April 2018 and then a year later.

In this section of the report we explore what pension outcomes might be expected in years to come if both employers and employees sustain pension contributions at the auto-enrolment rates which will be prevalent from April 2019 and whether these are likely to deliver outcomes that people are going to consider adequate. And if this level of saving is judged to be inadequate, we look at what might be done to increase levels of contributions.

Over a decade ago, Lord Turner's Pensions Commission[13] explored the target replacement level of income that different individuals might look to, based on their pre-retirement incomes, to match their pre-retirement living standards. *Figure 11* replicates that Report's proposals, with income bands updated to 2012 levels.

"Present and upcoming minimum contribution levels into auto-enrolment schemes are unlikely to deliver comfortable incomes in retirement for very many people, even with the new State pension. This message is only slowly getting across to the public"

Figure 11: Analysis by the Pensions Commission on the target level of income people are likely to expect in retirement, expressed as a replacement rate by income band

Income bands (gross earnings) and replacement rate targets		
Original 2004 income band	Income band in 2012 earnings terms	Target replacement rate
Up to £9,500	Up to £12,000	80%
£9,500 – £17,500	£12,000 – £22,100	70%
£17,500 – £25,000	£22,100 – £31,600	67%
£25,000 – £40,000	£31,600 – £50,000	60%
Over £40,000	Over £50,000	50%

(Source: DWP Paper, Reinvigorating workplace pensions, November 2012, page 7).

Whilst these targets would not suit every individual they provided the groundwork for setting the auto-enrolment contribution rates that will apply from April 2019, namely 8% of an individual's qualifying earnings between £5,876pa and £45,000 (2017/18 rates), subject to earnings exceeding a trigger point, which is presently £10,000pa. However, to achieve the target replacement levels, particularly at lower incomes there was also a need to introduce a higher level basic State Pension than existed in 2004 and, here again, Government has acted by introducing the higher single-tier State Pension from April 2016 to underpin private pension saving.

Steps to 10% and more

But is this enough? A detailed Pensions Policy Institute paper[14] has explored the range of variables at play and identified the difficulty in achieving replacement income targets. Their modelling found the target replacement income of 67% of pre-retirement earnings was only reached in half of the cases they looked at. More worrying still, saving at 8% of qualifying earnings, in 25% of the scenarios delivered less than three-quarters of the target replacement income sought. The report noted that outcomes would also be heavily influenced by the indexation method used for the new State Pension – adequacy will be much harder to achieve if the linkage is to average earnings rather than the current 'triple lock'[15]. And, unsurprisingly, contribution rates needed to achieve an adequate retirement income will be sensitive to consistency of contributions, investment approaches and charges.

In short, the PPI noted the total contribution required to reach a two-thirds chance of achieving their target replacement income would range from 10% of qualifying earnings in a low charging scheme (0.5% AMC) with a triple locked State pension and up to 17% in a higher charging scheme (1% AMC) and an earnings-linked State pension.

These findings are not dissimilar to those we produced in 2010[16] when, in order for an individual on average earnings to target a 40% replacement income (excluding the State pension), we suggested a contribution rate of the order of 10% of total earnings was needed rising to 16% if a partner's pension and 25% tax free lump sum was wanted in addition to the replacement income target, with savings starting at age 30 through to age 68.

The Pensions Minister, Richard Harrington, has admitted that "in terms of quantum, the contributions are not enough…everyone knows that they will need to save more to have 60–65% of salary in retirement that they say they want."[17]

From the findings of this survey, it has to be expected that modest progress in increasing contribution levels from a very much lower base found at hundreds of thousands of small firms who presently offer no workplace scheme is very unlikely ahead of 2019.

Danger signs

Previous Pensions Ministers[18] have also spoken of the need to increase pension contributions and have been supporters of auto-escalation (see next column). However, there must be some real concern that for the vast majority of smaller firms covered by this survey – over 90% of firms in the country – there is, first, a major step for them to take on board auto-enrolling eligible employees at initially 2% of qualifying earnings (with many not doing so until 2017/18), and, second, then raising combined contributions to 5% and then 8% of qualifying earnings over just two years – in 2018 and 2019 – set against a back-cloth of an uncertain economic climate.

We do wonder, without some development in policy, whether such sizeable jumps in contribution levels from employers and employees in this smaller firms sector can be afforded over such a short period if earnings growth remains modest and economic activity uncertain.

"Without some policy shift, we fear there may be a steep rise in opt-outs in small firms in the years ahead and a real danger of policy failure in a sector where better pension coverage is vital if the nation's retirement outcomes are to improve"

One possibility could be that if the political parties are intent on further reforms to pension tax relief then they could consider as part of any reforms raising the NIC threshold or increasing the current Employment Allowance[19]. If this was increased it could help meet or largely offset the increase in costs from auto-enrolment for micro and the smallest employers, protecting the boost to employment from this sector in recent years. Raising the NIC threshold would also reduce employees' costs and would be more effective for many employees in smaller firms than increasing the personal tax allowance because of lower average pay levels in the sector[20].

Support for auto-escalation

There are other ways that some smaller employers could build on initiatives like The Pension Quality Mark[21] by fostering a trend towards higher member pension contributions or by adopting auto-escalation as a feature of their approach to pensions.

"Once signed up, an individual no longer has to take active decisions to increase their contributions – that happens automatically"

Auto-escalation encourages people to commit to increasing their pension contributions at a future date, often in line with wage increases. The idea is one that the DWP has said is worthy of further examination[22] as, much like auto-enrolment, it plays on people's inertia.

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 wages, 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.

Whilst the concept has been taken up by the majority of large companies using defined contribution in the USA, the idea has not taken off in the UK. A clear economic pre-condition is, however, that earnings are generally increasing year by year. It may be that the UK economy has entered a phase where year on year wage increases will begin to re-emerge enabling auto-escalation to take hold.

Realistically, the expectation must be that auto-escalation will be taken up by employers of some size and hence probably only the larger employers in the smaller firms sector will be prepared to move in this direction.

Education

The survey results underscore the difficulties in achieving the higher pension contributions that are essential if more people are to experience a comfortable retirement. The State pension is unlikely to meet most people's income needs alone without supplements by way of private savings or reliance on uncertain State benefits. Whilst Government taxation strategies and initiatives like auto-enrolment can help, and there always will be a

All footnotes in this Report are featured on page 20.

group that remains reliant on State benefits in retirement, for many others there is a need to persuade them somehow to choose less consumption today in favour of greater security tomorrow, not just for income in later life, but for the inevitable and earlier 'rainy day'.

Opt-outs up

One of the achievements to date of auto-enrolment has been the much lower opt-out rate than was expected by Government. Average opt-out rates of around 10% have been reported in surveys of larger employers and by providers such as NEST as opposed to earlier DWP estimates of opt-outs ranging between 20–35%. However, more recent data has indicated that amongst smaller employers, opt-out rates have risen to 17%[24].

"More recent data has indicated that amongst smaller employers, opt-out rates have risen to 17%"

Previous ACA surveys have pointed to quite different opt-out expectations across employers of different sizes. Our *2011 ACA Pension trends survey*[25] reported, on average, that larger employers were budgeting for an opt-out rate of 12%. It was feedback from mid-sized, small and micro employers (many of which have not yet hit staging dates) which pushed the average opt-out rate up to around 25%.

Whilst the low opt-out rate reported from the outset of auto-enrolment might have caused many smaller employers to budget conservatively for opt-out rates of between 1–10% of eligible employers, in fact the actual median opt-out level reported to this year's survey of staged employers is in the 16–20% band across the 'staged' sample *(see Table 9, page 23).*

This is on a firm by firm basis and clearly given the much lower opt-out rates prevalent in larger businesses, the actual overall opt-out rate of employees, as a whole, is still likely to be towards the lower end reported to date. However, the results of this survey would seem to suggest that opt-out rates amongst these smaller employers are not as positive as one might hope, especially when account is also taken of the numbers ineligible to be auto-enrolled (see page 7).

Amongst employers yet to stage, whilst those with 10–49 employees are estimating low opt-out rates of 11–15%, the 'smallest employers' with 1–9 employees are expecting much higher opt-out rates of between 31–35% of employees (although actual reported rates from those that have staged are lower) *(see Table 17, page 26).*

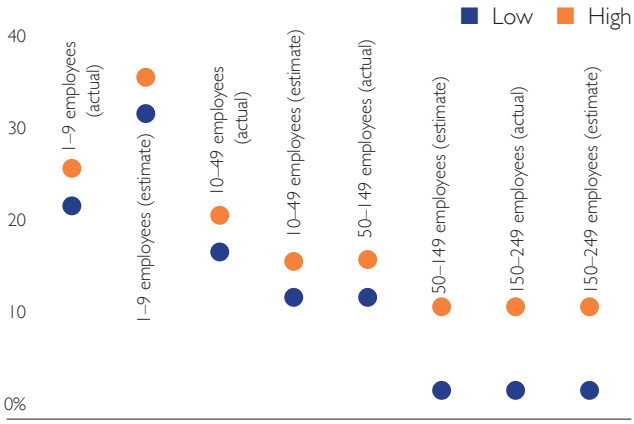
As we report later, only a minority of these latter employers have as yet budgeted for auto-enrolment, so these figures may change over time, but the forecasts may also reflect the fact that for micro employers just one or two employees opting-out may represent over 25% or 50% of their employee numbers.

With their recent experience of auto-enrolment, it is interesting to assess why employers felt employees are opting-out of the pension arrangements provided.

Across all sizes of employers, the prime reason given was 'cost – cannot afford', with this running ahead of employees' 'preference to spend income'.

This is a reversal of the principal reasons given by firms two years' ago and may reflect a greater experience of feedback over the period during which there has been poor earnings growth (see *Figure 13*).

Figure 12: Employers beyond staging date – range of median opt-out rates estimated ahead of auto-enrolment and range of median actual opt-out rates



(Source: 2016/17 Smaller Firms Pension Survey, see Table 9, page 23).

Figure 13: Employers beyond staging date – employers' view on the main reasons why employees 'opt-out' of pension arrangements (in ranked order)

Cost – cannot afford	1 (2)
Prefer to spend income	2 (1)
Lack of interest	3 (6)
Prefer non pension savings	4 (5)
Disillusioned with pensions	5 (3)
Have own personal pension	6 (4)

(Source: 2016/17 Smaller Firms Pension Survey, see Table 10, page 24).

Too many ruled 'ineligible'

Of employers that have staged, depending on the size of firms, between 21–40% of employees were reported as 'not eligible' for auto-enrolment *(see Table 11, page 24).*

There are a range of reasons for this – employees under age 22 and those over State pension age and, of course, those earning below the £10,000pa trigger point for auto-enrolment. However, if amongst the smallest employers there is a combination of between 36–40% 'ineligible' and 31–35% 'opting-out', the numbers being and staying auto-enrolled at this size of employer could be very modest indeed – perhaps just 1 in 4 employees.

The median 'opt-in' rate for those ineligible for auto-enrolment is in the band of 1–5% of employees.

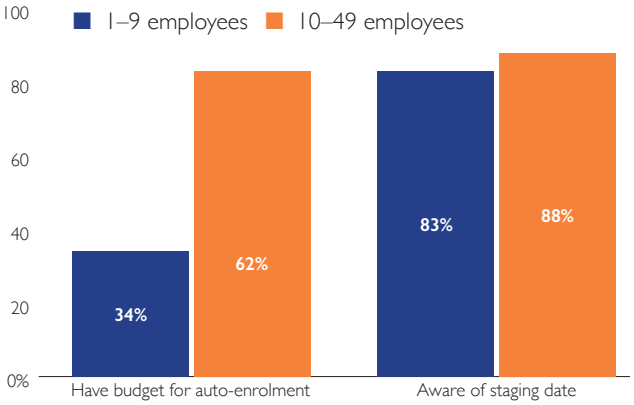
Those making such a request are likely to be those under age 22 and those earning above £5,824, but below £10,000pa.

As might be expected, the larger firms yet to enrol have a slightly greater awareness of their upcoming staging date and have a budget for auto-enrolment. Surveys by the Regulator[26] and other organisations generally point to lower levels of awareness of staging (and auto-enrolment understanding) amongst small and micro employers, so it is encouraging that progress appears to be being made as staging dates approach.

That said, amongst the 'smallest employers' – over ¾ million employers with fewer than 10 employees – while awareness of staging dates is now quite high (83% of firms are aware) budgeting for auto-enrolment (34% are doing so) is still low *(see Figure 14).*

The ability of the Regulator to monitor whether this is a compliance problem at the micro employer level is challenging given the sheer scale of numbers now staging.

Figure 14: Employers yet to reach staging date – awareness of date when employers must auto-enrol eligible jobholders by and budget readiness



(Source: 2016/17 Smaller Firms Pension Survey, see Tables 17 and 18, page 26).

"Only 15% of firms support gradually increasing auto-enrolment contributions above 8% of qualifying earnings after 2019"

2017 Auto-enrolment policy review

The Pensions Minister has announced the broad scope of the 2017 review of auto-enrolment with a consultation due early in 2017. In the survey (conducted ahead of the announcement) we tested firms' views on a number of reforms, some of which have already been recommended to DWP by the House of Commons Work and Pensions Select Committee[27]. Some of these have been picked up by the Minister in his scoping Statement of 12 December 2016.

Close to 9 out of 10 firms support legislation making clear that employers should not be held liable if an auto-enrolment scheme they have selected performs badly.

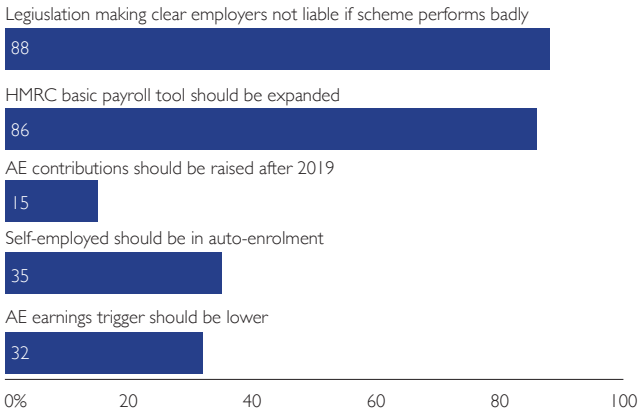
The concern here is that some lawyers have said that there may be a liability if employers cannot demonstrate due diligence in the choice of the scheme.

A similar number support the HMRC basic payroll tool being expanded to support small businesses in meeting auto-enrolment obligations, which it does not presently do.

Indicating the challenge in raising minimum contributions, only 15% of firms support gradually increasing auto-enrolment contributions above 8% of qualifying earnings after 2019.

And only just over a third of firms support lowering the trigger point of qualifying earnings for auto-enrolment (presently £10,000pa), with support for lowering the trigger falling to 22% amongst the smallest firms *(see Figure 15).*

Figure 15: What support is there from employers for some suggested changes to be addressed in the 2017 review of auto-enrolment?



(Source: 2016/17 Smaller Firms Pension Survey, see Table 19, page 27).

Impact of living wage plus auto-enrolment on small firms

Whilst small firms are generally supportive of 'the idea of' the living wage and half support the eventual 8% minimum contribution level achieved in April 2019, support is much lower for both amongst the smallest employers.

26% of the smallest firms also say that auto-enrolment (and 37% that the 'living wage') will have an impact on their employee numbers. Indeed, some 29% of all the small firms express the concern that the 'living wage' will impact on employee numbers *(see Table 20, page 27).*

All footnotes in this Report are featured on page 20.

Section 2

Summary of earlier findings of 2016 Smaller Firms' interim survey reports

Published October – December 2016

Three interim reports were published in the third quarter of 2016 following the findings of the survey.

Summary of other key findings in interim reports

Retirement ages set to out-pace increases in State Pension Age

- Whereas two years ago, just 4% of firms expected typical retirement ages to rise to above age 67 by 2020 (by when SPA increases to age 66), five times as many – 20% of firms – now expect typical retirement ages to rise to above age 67 by then. And, looking further ahead, when SPA rises by 2028 to age 67, some 36% expect typical retirement ages to be a pace ahead at age 68 or above.
- In the 2017 review of State Pension Age, more than half of the survey's respondents supported a change to allow for a flexible State Pension Age from age 66.

Moaning about LISA and pension tax reform

- The ACA survey found that 72% of firms are confused by the launch of the Lifetime ISA (LISA) next year given the Government's parallel initiative of requiring all small firms with 1 or more employees to also auto-enrol employees into separate qualifying pension arrangements.
- 60% of firms say they want the current system of pension tax retained but with more help targeted on lower income groups, which – inevitably – if costs are to be constrained means further reductions in relief at the top income levels with more relief at lower incomes.

Support for statutory override to apply CPI indexation

- Over 90% of firms support legal reforms that would allow defined benefit schemes to move to CPI indexation of benefits (as opposed to RPI or any other higher indexation provision in scheme rules).

Greying workforce

Recent surveys have shown that the number of those staying on at work past the State Pension Age (SPA) has been climbing at some pace. Indeed, a DWP paper[28] found as many as 1 in 10 of those aged between 70 and 74 are now in work. This extension in post-pension age work has been explained largely by the financial pressures on those approaching retirement, not least because of much reduced income from private savings and annuities in a low-interest rate environment.

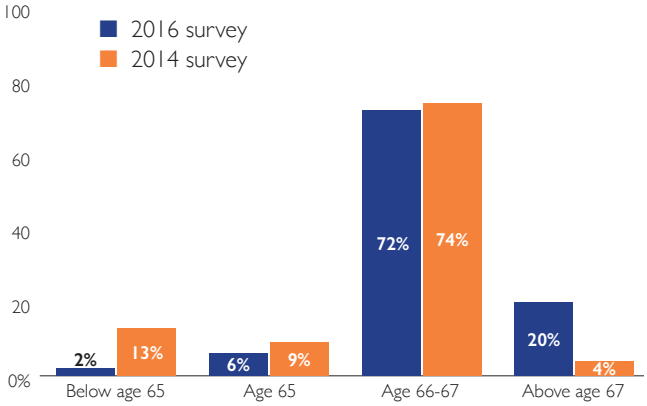
This year's survey found a significant shift in the percentage of firms where employees are typically retiring at age 66 or above – 35% as opposed to just 8% two years ago *(see Table 21, page 28)*, **with the change most marked amongst firms employing fewer than 50 employees.**

Looking ahead, there has also been a big shift over the last two years in firms' forecasts of typical retirement ages in their businesses as SPA increases over the next decade or so. The changes suggest many employers expect that typical retirement ages in the smaller firms' sector will out-pace the increases in SPA.

Whereas two years ago, just 4% of firms expected typical retirement ages to rise to above age 67 by 2020 (by when SPA increases to age 66), five times as many – 20% of firms – now expect typical retirement ages to rise to above age 67 by then (see Figure 16). And, looking further ahead, when SPA rises in 2028 to age 67, some 36% expect typical retirement ages to be a pace ahead at age 68 or above.

Again, it is employers with fewer than 50 employees who expect the biggest leaps in typical retirement ages. This is likely to be related to the lower earnings prevalent in smaller firms – where, as we note earlier, over 40% of employees in micro employers (1–4 employees) earn less than £10,000pa.

Figure 16: Typical age at which employees retire at present and employers' forecast as to how this will change by 2020 (by when SPA increases to age 66). Results compared with 2014 survey.



(Source: 2016/17 Smaller Firms Pension Survey, see Table 22, page 28).

These findings suggest that small firms are expecting more employees to want to work on beyond current retirement ages with the pace of change in 'working-on' moving more quickly than the increases in SPA. This should mean an increasing number of older employees will be receiving both a wage and/or salary whilst also being in receipt of their State pension (unless they defer). Whilst this could mean more of this group have a comfortable financial position than those in the same age group today, continued low annuity and savings rates may offset this hope. Whilst some studies have disputed the impact, a sharp and persistent rise in older employees continuing to work must at some stage have an impact on employment and career opportunities for younger people (where, for example, despite average levels falling below 5%, currently over 11% of those aged 18–24 are unemployed).

The 2017 Review of State Pension Age

The Government has begun to consider future moves in the State Pension Age (SPA) and is seeking views at present on possible options with a view to making an announcement by May 2017 on the path ahead. The review will not only encompass projections of life-span changes over the period ahead, but also wider social considerations as evidenced by the interim report of the Cridland review.

This year's survey explored some of the changes that should be considered in the review.

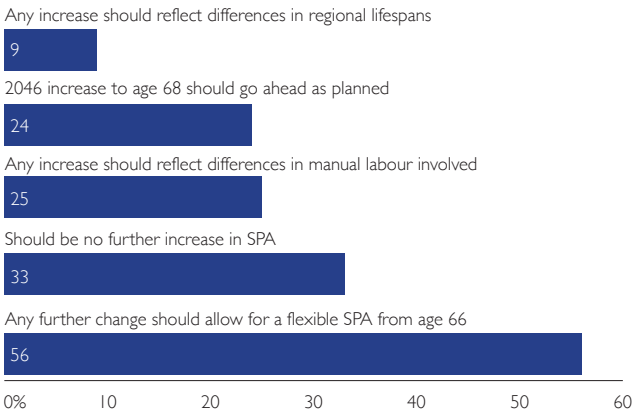
By far the most popular call was for any further change to allow for a flexible SPA from age 66, which is supported by more than half of the survey's respondents. This was clearly judged to be a more acceptable proposal than outcomes where the SPA might be lower for those in manual occupations or a solution that in some way reflects regional disparities in life-spans *(see Figure 17).*

That said, despite extending life-spans, a third of firms wanted the review to result in no further increases in SPA and a quarter felt an increase to age 68 should not take place until the planned date of 2046.

An option for individuals to have some flexibility to draw their State Pension from an earlier age than State Pension Age, as life-spans extend, would help those who feel less able to continue to work beyond that age for a range of reasons. It would seem a sensible compromise and overcome the unfathomable ways that might have to be dreamt up to test who might qualify for a lower SPA as a 'manual' employee or by way of regional deprivation (would this apply to all post codes in a region – rich or poor – and how would the government prevent people gaming the system by switching to occupations/addresses that provided an entitlement to a lower SPA?).

"By far the most popular call was for any further change to allow for a flexible SPA from age 66, which is supported by more than half of the survey's respondents"

Figure 17: The Government has set up a review to examine whether further increases in the State Pension Age (SPA) should be brought forward due to advances in life-spans and hence the increasing cost to the taxpayer. What are employers' views on further increases in the State Pension Age?



(Source: 2016/17 Smaller Firms Pension Survey, see Table 23, page 28).

Moaning about LISA

Following a consultation exercise, many expected the then Chancellor would announce a widespread reform of pension tax relief in his April 2016 Budget, but in the end he did not go ahead with such a radical change and instead announced the launch from next April of a Lifetime ISA (LISA) targeted at the 'young' aged between 18 and 40.

Savings into a LISA would be from after-tax income up to a maximum of £4,000 per year with a 25% bonus on savings made before age 50. However, after age 60 all savings can be taken tax-free. A Government message, amongst others, is (to quote) 'use it to save for retirement'.

The survey found that 72% of firms are confused by the launch of the Lifetime ISA (LISA) next year given the Government's parallel initiative of requiring all small firms with one or more employees to also auto-enrol employees into separate qualifying pension arrangements *(see Table 24, page 29).*

All footnotes in this Report are featured on page 20.

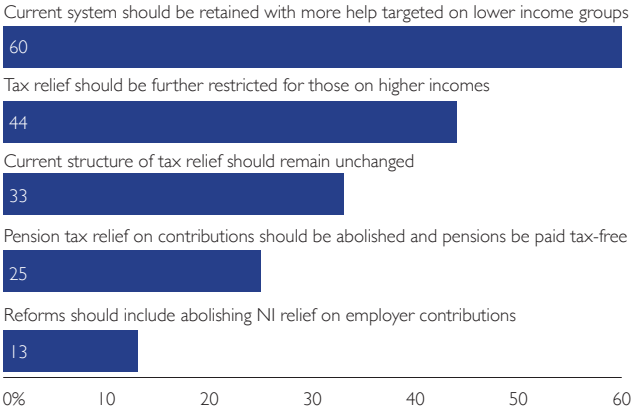
What about further pension tax reform?

The wider pension tax reform many expected last year was not forthcoming, but certainly more changes were not totally ruled out. Might the Spring or Autumn 2017 Budgets take this up again? To date, there have been few pointers from the new Chancellor, Philip Hammond[29], but if he is tempted to make further changes, our survey points to the measure that would be most popular amongst smaller employers.

60% of firms say they want the current system of tax retained but with more help targeted on lower income groups, which – inevitably – if costs are to be constrained means further reductions in relief at the top income levels with more relief at lower incomes, perhaps a flat rate relief up to a capped annual amount.

Whilst 25% of firms support a pension ISA-type model, where savings are taxed with the pension paid tax-free, just 13% would support a change whereby NI relief on employer pension contributions is abolished (see *Figure 18*).

Figure 18: Level of support from employers on suggestions from some organisations that pension tax relief should be reduced or targeted in a different way



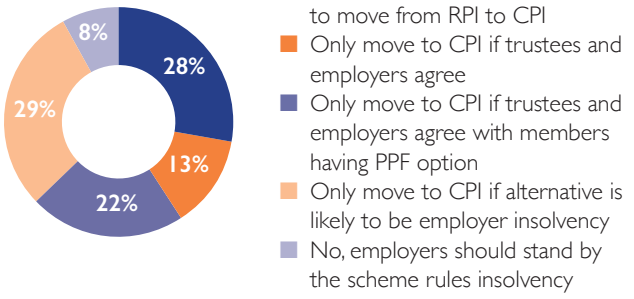
(Source: 2016/17 Smaller Firms Pension Survey, see Table 25, page 29).

Defined benefit schemes: move to CPI with caveats

The survey covers firms with fewer than 250 employees and many of the larger firms in this sample once offered defined benefit pensions to some or all employees. Today, over 84% of the defined benefit schemes run by these employers are closed to new members and a further 57% are also closed to future accrual. However, the compulsory indexation of benefits – required by law from the late 1990s – adds considerably to ongoing pension costs, often reducing monies available for funding defined contribution pensions for many existing employees. Whilst some schemes have moved from RPI to CPI indexation of benefits, many have found their scheme rules too complex to progress such a change or the process too costly to enact, especially for a smaller firm.

The survey found 92% favoured a change in the law to allow the move to CPI, albeit many wanted this to be subject to the agreement of trustees or, only if otherwise, the employer was likely to declare its insolvency *(see Figure 19).*

Figure 19: Should the Government change the law so that pension schemes can reduce pension increases if continuing to provide increases at the level in scheme rules will severely and adversely affect the employer?



(Source: 2016/17 Smaller Firms Pension Survey, see Table 26, page 30).

Footnotes

[1] Workers aged between 22 and SPA.

[2] Excluding working proprietors not working under a contract of employment in return for a wage or salary.

[3] Weighted average.

[4] *Declaration of compliance report to 31 December 2016*, published by the Pensions Regulator.

[5] *Automatic Enrolment Commentary and Analysis, April 2015-March 2016*, published by the Pensions Regulator, page 26.

[6] See Figure 1, on page 7.

[7] *The self-employed and pensions*, published by the Resolution Foundation, May 2015.

[8] ONS, *Occupational Pension Schemes Surveys*, 1993 and 1995.

[9] There are provisions for schemes that structure their contributions in different ways to be certificated as qualifying schemes.

[10] **Source**: BEIS Business Population Estimates 2016.

[11] **Source**: DWP Research Report *Employers' Pension Provision Survey 2011*.

[12] ONS reports *Occupational Pension Schemes Surveys 2013 and 2015*, which report average total defined contribution rates have fallen from 9.1% to 4% of earnings over the period.

[13] Pensions Commission Report, published 2004.

[14] *What level of pension contribution is needed to obtain an adequate retirement income?* Published by the Pensions Policy Institute, October 2013.

[15] The so-called 'triple-lock' system means that State pensions will rise by whichever of annual earnings growth, inflation or a 2.5% baseline is highest.

[16] *ACA Biennial Review*, published 29 April 2010 (www.aca.org.uk see 'publications').

[17] Interview featured in *Pensions World*, December 2016, pages 12–13.

[18] Namely, both Sir Steve Webb and Baroness Altmann.

[19] Most private sector employers paying Class 1 NI can at present get up to £3,000pa off their NI bill by way of the Employment Allowance. This particularly helps small businesses with their employment costs.

[20] See Figure 1, page 7 of this report.

[21] Schemes can be awarded The Pension Quality Mark (PQM) where total pension contributions equal at least 10% of employees' pensionable salary (with a minimum of 6% from the employer) or PQM PLUS where total contributions equal at least 15%, with minimum employer contributions of 10%.

[22] *DWP paper, Reinvigorating workplace pensions*, November 2012, Cmnd 8476, pages 19–20.

[23] *Automatic enrolment opt-out rates: findings from research with large employers*, published by DWP (2013).

[24] *DWP paper, Employers' Pension Provision survey 2015*, published March 2016, page 52.

[25] *2011 ACA Pension trends survey*, published 3 January 2012, page 27 at www.aca.org.uk (Research and Surveys page).

[26] *Automatic Enrolment Commentary and Analysis: April 2015-March 2016, published by the Pensions Regulator*, July 2016.

[27] *Automatic enrolment*, Eleventh Report of Session 2015-16, HC 579, published 15 May 2016.

[28] DWP paper, *Employment statistics for workers aged 50 and over*, published November 2015.

[29] However, the November HM Treasury consultation following the 2016 Autumn Statement, *Reducing the money purchase annual allowance*, notes that two thirds of pension tax relief goes to higher and additional rate taxpayers and comments, 'the government is committed to enabling individuals to save more so that they have security in retirement, but it is important that resources focus where there is most need'.

Statistical Appendix

2016/17 ACA Smaller Firms Pension Survey

The 2016/17 biennial survey was conducted in June/July 2016 for online completion and was broadcast to over 20,000 of the UK's smaller firms with fewer than 250 employees, selected on a random basis. Responses were received from 455 firms.

(Figures in brackets are 2014 survey findings.)

Survey Sample

Table 1: Breakdown of employers responding to survey (by employee numbers).

1–9 employees	10–49 employees	50–149 employees	150–249 employees
27% (34%)	36% (21%)	21% (24%)	16% (21%)

Table 2: Depending on their employee numbers, between 2014 and 2018 employers will be (or will have been) required by law to auto-enrol all 'eligible jobholders' into an auto-enrolment pension scheme. Percentage of employers responding to the survey who have passed or not reached their 'staging date' (i.e. the date by which they must observe this legislation and auto-enrol all eligible jobholders into a pension scheme).

	1–9 employees	10–49 employees	50–149 employees	150–249 employees	All employers
Staging date passed	23% (1%)	74% (–)	100% (90%)	100%	70% (43%)
Staging date not reached	73% (92%)	26% (94%)	– (10%)	–	29% (53%)
Don't know	4% (7%)	– (6%)	–	–	1% (4%)

Firms Where Auto-Enrolment Staging Date Has Passed

Table 3: Employers beyond staging date – when preparing for auto-enrolment, what caused the biggest problems to your business? Ranked in order with 1 as biggest problem.

	1–9 employees	10–49 employees	50–14 employees	150–249 employees	All employers
Assessment of options available	5	2	4 (3)	3 (3)	4 (3)
Uncertainty over financial cost	4	5	5= (4)	6 (5)	6 (4=)
Processes in preparing for change	2	3	1 (1)	1 (1)	1 (1)
Regulatory complexity	3	4	3 (2)	4 (2)	3 (2)
New administrative systems	1	1	2 (6)	5 (6)	2 (6)
Communications	6	6	5= (5)	2 (4)	5 (4=)

Table 4: Employers beyond staging date – overall, did you find setting up an auto-enrolment scheme relatively simple or complex?

	1–9 employees	10–49 employees	50–14 employees	150–249 employees	All employers
Very simple	4%	2%	6%	11%	6%
Simple	7%	3%	11%	29%	11%
Not administratively cumbersome	11%	39%	55%	46%	43%
Complex	21%	43%	21%	7%	26%
Very complex	57%	13%	7%	7%	14%

Table 5: Employers beyond staging date – as a percentage of total earnings, median EMPLOYER and median EMPLOYEE contribution into pension scheme(s). Answers are median.

	Employer				Employee			
	1–9	10–49	50–149	150–249	1–9	10–49	50–149	150–249
Contract DC	3%	3%	3% (4%)	4% (4%)	2%	2%	2% (3%)	3% (3%)
Firm's Trust DC	3%	3%	3% (5%)	5% (5%)	2%	3%	4% (4%)	4% (4%)
NEST	<1%	1–2%	1–2% (1–2%)	1–2% (1–2%)	<1%	<1%	1–2% (1%)	1–2% (1%)
Other multi-employer scheme	1–2%	1–2%	2% (3%)	3% (3%)	1–2%	1–2%	1–2% (2%)	1–2% (1%)
Defined Benefit	–	–	16–20% (16–20%)	21–25% (16–20%)	–	–	6% (5%)	6% (6%)

Table 6: Employers beyond staging date – how did these employers change their workplace pension arrangements as a result of the requirement to auto-enrol all eligible jobholders into an auto-enrolment scheme from their staging date.

	1–9 employees	10–49 employees	50–14 employees	150–249 employees	All employers
Closed existing scheme – opened new firm's scheme for all	–	–	4%	9%	3%
Closed existing scheme and auto-enrolled all into NEST/other multi-employer scheme	7%	5%	11%	8%	8%
Kept existing scheme(s) – opened new firm's scheme for non-joiners/new employees	–	3%	9%	6%	5%
Kept existing scheme and auto-enrolled non-joiners/new employees into NEST/ other multi-employer scheme	18%	59%	42%	46%	47%
Had no scheme prior to auto-enrolment	75%	33%	34%	31%	37%

Table 7: Employers beyond staging date – pension arrangements and their status.

	Employers with scheme type				Of these schemes % closed to new members?				Of these Schemes % closed to new members and future accrual/contributions?			
Employees	1–9	10–49	50–149	150–249	1–9	10–49	50–149	150–249	1–9	10–49	50–149	150–249
Contract DC	20%	38%	43%	41%	–	–	5%	7%	17%	4%	20%	13%
Firm's Trust DC	6%	14%	18%	24%	–	–	6%	12%	50%	24%	18%	22%
NEST	47%	37%	37%	34%	–	–	–	–	–	–	–	–
Other multi	40%	52%	47%	46%	–		–	–	–	–	–	3%
DB	–	–	12%	59%	–	–	27%	27%	–	–	55%	58%

Table 8: Employers beyond staging date – Schemes used for auto-enrolment.

	1–9 employees	10–49 employees	50–14 employees	150–249 employees	All employers
Contract DC	7%	9%	11%	12%	10%
Firm's Trust DC	4%	2%	4%	7%	4%
NEST	46%	37%	37%	34%	37%
Other multi-employer schemes	43%	52%	48%	45%	48%
Defined Benefit	–	–	–	2%	< 1%

Table 9: Employers beyond staging date – when preparing for auto-enrolment what member 'opt-out' did employers assume and how did this compare with the actual 'opt-out' rate and increase in payroll costs? Answers are median and median bands.

'Opt-out' rate assumed ahead of staging date				Expected increase in payroll costs			
1–9	10–49	50–149	150–249	1–9	10–49	50–149	150–249
31–35%	11–15%	1–10%	1–10%	5%	3%	2%	1%
11–15% (1–10%)*				3% (2%)*			

***In 2014, responses only covered firms with 50 employees or more**

Actual 'opt-out' rate following auto-enrolment				Actual increase in payroll costs			
1–9	10–49	50–149	150–249	1–9	10–49	50–149	150–249
21–25%	16–20%	11–15%	1–10%	3%	3%	2%	1%
16–20% (11–15%)*				3% (2%)*			

***In 2014, responses only covered firms with 50 employees or more**

Table 10: Employers beyond staging date – what do employers see as the main reasons why employees 'opt-out' of pension arrangements? Ranked in order of importance with 1 as most important reason.

	1–9 employees	10–49 employees	50–14 employees	150–249 employees	All employees
Lack of interest	3	3	6 (6)	4 (6)	3 (6)
Cost – cannot afford	1	1	1 (2)	2 (2)	1 (2)
Prefer to spend income	2	2	2 (1)	1 (1)	2 (1)
Have own personal pension	6	6	4 (4)	6 (4)	6 (4)
Prefer non-pension savings	5	4	3 (5)	5 (5)	4 (5)
Disillusioned with pensions	4	5	5 (3)	3 (3)	5 (3)

Table 11: Employers beyond staging date - percentage of employees NOT ELIGIBLE for auto-enrolment (for example because their earnings are generally too low or because of age) and percentage of ineligible employees wanting to 'opt in' to auto-enrolment scheme. Answers are median bands.

Percentage of employees NOT ELIGIBLE for auto-enrolment				Percentage of employees NOT ELIGIBLE for auto-enrolment requesting to 'opt in' to scheme			
Employers with:				Employers with:			
1–9 employees	10–49 employees	50–149 employees	150–249 employees	1–9 employees	10–49 employees	50–149 employees	150–249 employees
36-40%	31-35%	21-25% (16-20%)	21-25% (16-20%)	1-5%	11-15%	1-5% (1-3%)	1-5% (1-3%)

Firms Where Staging Date for Auto-Enrolment Not Yet Reached

Table 12: Employers have already started preparing for auto-enrolment, what is causing the biggest problems? Ranked in order with 1 as biggest problem.

	1–9 employees	10–49 employees	All employers
Assessment of options available	4 (1)	5 (1)	5 (1)
Uncertainty over financial cost	2 (3=)	4 (4)	4 (4)
Processes in preparing for change	3 (3=)	1 (3)	3 (3)
Regulatory complexity	1 (2)	2 (2)	1 (2)
New administrative systems	2 (5)	3 (5)	2 (5)
Communications	6 (6)	6 (6)	6 (6)

Table 13: Employers yet to reach staging date – pension arrangements (if any) offered by employers at present, their status and which may be used for auto-enrolment.

	Employers with scheme type		Of these schemes % closed to new members?		Of these schemes % closed to new members and future accrual/ contributions?		Scheme to be used for auto-enrolment	
	1–9 employees	10–49 employees	1–9 employees	10–49 employees	1–9 employees	10–49 employees	1–9 employees	10–49 employees
No scheme	66%	47%						
Contract DC	23%	23%	25%	20%	15%	20%	5%	9%
Firm's Trust DC	6%	12%	60%	20%	20%	40%	2%	3%
NEST	3%	7%	–	–	–	–	36%	34%
Other multi-employer scheme	2%	11%	–	–	–	–	14%	40%
No decision							43%	14%

Table 14: Employers yet to reach staging date – percentage of employers who at present voluntarily auto-enrol all or some employees into any workplace pension scheme(s).

	1–9 employees	10–49 employees	All employers
Yes, all	–	–	–
Yes, some	7%	13%	9%
No	93%	87%	91%

Table 15: Employers yet to reach staging date – employers likely decision in setting up/ changing their workplace pension scheme when they are required to auto-enrol employees into a scheme.

	1–9 employees	10–49 employees	All employers
Enrol all eligible jobholders into an existing firm's scheme	–	5%	2%
Enrol all eligible jobholders into a new firm's scheme	2%	7%	4%
Enrol all eligible jobholders into NEST/new multi-employer scheme	45%	37%	42%
Restrict entry of pre auto-enrolment non joiners and new employees to lower-cost (than existing) firm's scheme	5%	5%	5%
Restrict entry of pre auto-enrolment non joiners and new employees to NEST or other new multi-employer scheme	5%	23%	10%
No decision as yet	43%	23%	37%

Table 16: Employers yet to reach staging date – if employers already offer a pension scheme, as a percentage of total earnings, median EMPLOYER and median EMPLOYEE contribution into pension scheme(s). Answers are median.

	Employer		Employee	
	1–9 employees	10–49 employees	1–9 employees	10–49 employees
Contract DC	3% (4%)	3% (4%)	2% (4%)	3% (4%)
Firm's Trust DC	3% (4%)	4% (5%)	2% (3%)	3% (4%)
NEST	<1%* (1%*)	<1% (–)	<1%* (1%*)	<1% (–)
Other multi-employer scheme	1–2%* (4%*)	1–2% (3%)	1%* (3%*)	1% (4%*)

(* Restricted sample)

Table 17: Employers yet to reach staging date – have employers budgeted for the cost of auto-enrolment and, if so, what member 'opt-out' rate are they assuming? What approximate increase in payroll costs are they expecting (if any)? Answers are median and median bands.

Percentage of firms that have budgeted for cost of auto-enrolment?		Anticipated 'opt-out' rate on auto-enrolment		Expected increase in payroll costs	
1–9 employees	10–49 employees	1–9 employees	10–49 employees	1–9 employees	10–49 employees
34% (29%)	62% (43%)	31–35% (16–20%)	11–15% (1–10%)	5% (4%)	2% (3%)

Table 18: Employers yet to reach staging date – are employers aware of the date when they must auto-enrol 'eligible jobholders' into a qualifying scheme?

	1–9 employees	10–49 employees	All employers
Yes, aware of date	83% (46%)	88% (62%)	84%
Yes, started planning	90%	95%	91%
Months away from staging date:			
- Up to 3 months	2%	25%	10%
- 4–6 months	10%	54%	24%
- 7–12 months	25%	14%	22%
- Over 12 months	63%	7%	44%

Table 19: A number of suggestions have been made to Government that should be addressed in the 2017 review of how auto-enrolment works. What support from employers is there for the following proposals?

	1–9 employees	10–49 employees	50–14 employees	150–249 employees	All employers
Support lowering the trigger points on qualifying earnings so more are eligible for auto-enrolment (AE)	22%	34%	36%	40%	32%
Support changes so self-employed are auto-enrolled	24%	33%	44%	46%	35%
Support gradually increasing AE contributions above 8% after 2019	11%	13%	20%	21%	15%
Support for HMRC expanding basic PAYE tools to support smaller businesses in meeting AE obligations	91%	93%	85%	64%	86%
Support legislation making it absolutely clear employers are not liable if AE scheme performs badly or fails	92%	89%	88%	81%	88%

Table 20: As well as the cost of auto-enrolment, the Government has decided to increase the minimum wage for those aged over 25 so it becomes what they term a 'National Living Wage' of a minimum rising to around £9 per hour by 2020. What are employers' views on the following?

	1–9 employees	10–49 employees	50–14 employees	150–249 employees	All employers
The living wage is a bigger cost issue for your firm than auto-enrolment (AE)	39%	30%	12%	25%	28%
AE has/will have an impact on firms' employee numbers	26%	5%	6%	8%	11%
The living wage will have an impact on firms' employee numbers	37%	29%	20%	29%	29%
Support for the idea of a minimum living wage at the level proposed	52%	61%	73%	70%	62%
Support for the eventual level of minimum AE contributions into pensions of 8% of qualifying earnings	38%	42%	76%	78%	51%

Interim Report Findings

Greying Workforce

Table 21: By employer size – percentage of current employees who are over the current State Pension Age (age 65).

Employees over State Pension Age	1–9 employees	10–49 employees	50–14 employees	150–249 employees	All employers
None	36%	40%	36%	40%	38%
Up to 5%	45%	42%	50%	45%	45%
6–10%	9%	9%	12%	15%	10%
11–15%	6%	6%	2%	–	5%
Over 15%	4%	3%	–	–	2%

Table 22: Typical age at which employees retire from employers at present and employer forecasts on how this will change by 2020 and 2028.

	1–9 employees			10–49 employees			50–14 employees			150–249 employees			All employers		
	Now	2020	2028	Now	2020	2028	Now	2020	2028	Now	2020	2028	Now	2020	2028
Below 65	15%	<1%	–	19%	<1%	–	31%	2%	–	34%	6%	3%	23% (39%)	2% (13%)	1% (3%)
Age 6	36%	3%	3%	35%	1%	1%	42%	9%	5%	54%	17%	7%	42% (53%)	6% (9%)	3% (2%)
66–67	30%	67%	52%	25%	72%	53%	26%	76%	72%	10%	73%	74%	22% (7%)	72% (74%)	60% (63%)
68–69	14%	25%	27%	16%	21%	25%	1%	12%	15%	2%	4%	10%	10% (1%)	17% (3%)	21% (26%)
70 or more	5%	5%	18%	5%	5%	21%	–	1%	8%	–	–	6%	3% (–)	3% (1%)	15% (6%)

Table 23: The Government has set up a review to examine whether further increases in the State Pension Age (SPA) should be brought forward due to advances in life-spans and hence the increasing cost to the taxpayer. What are employers' views on further increases in the State Pension Age?

	1–9 employees	10–49 employees	50–14 employees	150–249 employees	All employers
Next increase to age 68 should take place by 2046 as planned	38%	22%	15%	17%	24%
Should be no further increase in the State Pension Age	40%	33%	27%	29%	33%
Any further change should allow for a flexible SPA from age 66	59%	54%	52%	60%	56%
Any increase should reflect differences in manual labour involved	31%	34%	10%	14%	25%
Any increase should reflect differences in regional life-spans	11%	6%	8%	13%	9%

(More than one answer given by some firms)

Lifetime ISA

Table 24: In the last Budget, the then Chancellor announced that from April 2017 individuals aged between 18 and 40 will be able to save up to £4,000 each year in a new Lifetime ISA and receive a 25% bonus of up to £1,000 a year from the Government. Savers will be able to use some or all of the money to buy a first home or keep it until age 60, when it could be taken tax-free. What do employers think of this new savings idea?

	1–9 employees	10–49 employees	50–14 employees	150–249 employees	All employers
It should be supported and will be popular with younger employees	55%	51%	47%	45%	50%
It is likely to discourage younger people from saving into workplace pensions	58%	54%	46%	48%	52%
It will have no impact on workplace pension saving	20%	24%	34%	60%	31%
Younger people should be encouraged to auto-enrol into a LISA rather than into a workplace pension scheme	23%	26%	21%	18%	23%
I find its launch confusing when workplace pensions are also being promoted	69%	73%	74%	70%	72%

Pension tax reform

Table 25: Pension tax relief (net of tax on pensions in payment) currently costs around £21 billion per annum. Some organisations are suggesting that tax relief should be reduced? Or targeted in a different way. What are employers' views?

	1–9 employees	10–49 employees	50–14 employees	150–249 employees	All employers
Current system should be retained with more help targeted on lower income groups	71%	65%	47%	48%	60%
Tax relief should be further restricted for those on higher incomes	54%	46%	38%	32%	44%
Current structure of tax relief should remain unchanged	32%	28%	38%	40%	33%
Pension tax relief on contributions should be abolished and pensions be paid tax-free	40%	23%	18%	16%	25%
Reforms should include abolishing NI relief on employer contributions	23%	14%	7%	3%	13%

Defined benefit schemes: move to CPI indexation

Table 26: Should the Government change the law so that pension schemes can reduce pension increases if continuing to provide increases at the level in scheme rules will severely and adversely affect the employer?

	Yes
All schemes should have the option, just as public service schemes changed from RPI to CPI in 2010	28%
So long as the trustees and employer agree	13%
So long as trustees and employer agree and members are given the chance to opt to go into the PPF instead	22%
Only if it can be shown that the alternative is likely to be insolvency of the employer with the scheme ending up in the PPF	29%
Employers should stand by the scheme rule	8%

Auto-enrolment: a quick summary

The reforms require employers to automatically enrol 'eligible' workers into a qualifying workplace pension scheme. The enrolment duties have been staged in between October 2012 and February 2018 by size of employer, starting with the largest and finishing with new businesses established during staging.

Employees are eligible for auto-enrolment provided they are aged at least 22 and under State Pension age, and earn over £10,000pa in 2016/17 terms. Initially, until April 2018, contributions have been set at a minimum of 1% employer contribution as part of a total minimum contribution of 2% on qualifying earnings (earnings between £5,824 and £43,000pa) in 2016/17 terms (and between £5,876 and £45,000 in 2017/18). By April 2019, once fully phased in, the total minimum contribution will be 8% of qualifying earnings, of which at least 3% must come from the employer and 1% will come from the Government in the form of tax relief. There are provisions for schemes that structure their contributions in different ways to be certificated as qualifying schemes.

Those presently earning less than £10,000pa can ask to take part in auto-enrolment and, if they earn more than £5,824pa, their employer will be obliged to make the minimum contribution too. Those aged under 22 or over State Pension age and still working can also opt-in in the same way. All employees have the right to opt-out.

Auto-enrolment is expected to reverse the trend of falling private pension income over time. Without it, median private pension income was expected to fall from around £3,900 a year in 2020 to around £2,200 in 2050. It is expected auto-enrolment will reverse this trend so median private pension income is around £3,600 by 2050.

Once fully implemented, automatic enrolment aims to transform the culture of saving, increasing the number of individuals newly saving or saving more in a workplace pension by around 9–10 million and increasing the amount that is being saved in workplace pensions by around £17–19 billion a year by 2019/20.

The Association of Consulting Actuaries (ACA) is the representative body for UK consulting actuaries and is the largest national grouping of consulting actuaries in the world. The ACA is a full member of the International Actuarial Association.

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