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Survey of Smaller firms views on Auto-enrolment and NEST

First Report of the ACA's 2010 Smaller Firms Pensions Survey

Conducted by the Association of Consulting Actuaries
In August 2010

PUBLISHED – 27 SEPTEMBER 2010

Summary results: 2010 ACA Smaller Firms Pensions Survey

Auto-enrolment/NEST

Survey background

The survey was conducted by the Association of Consulting Actuaries (ACA) in August 2010 for online completion by 27 August 2010 and was circulated to 12,000 of the UK's smaller firms with 250 or fewer employees, selected on a random basis. Responses were received from 404 firms. This survey report forms part of the ACA's *2010 Smaller Firms Pensions Survey* and focuses on some general trends and, in particular, replies to questions on auto-enrolment and NEST. Most of the questions asked on auto-enrolment and NEST are the same as those asked in the ACA's recent survey¹ of larger employers, conducted earlier in the summer. All respondents received a summary of the auto-enrolment/NEST reforms as they presently stand.

Executive Summary

Smaller firms and pensions

- 78% of firms responding to the survey employ 50 or fewer staff.
- The dominant types of scheme provided by respondents are Group Personal Pensions, Stakeholder and trust based defined contribution schemes. Where final salary schemes are provided, 86% are closed to new entrants and 41% also to future accrual.
- Across most types of schemes, membership participation is slightly below 60% of employees.
- Firms say the principal reasons why employees do not join existing schemes is 'cost' (84%), a 'preference to spend' (72%) and 'disillusionment with pensions' (69%).
- Firms not providing pensions say they do not principally because of 'cost' (96%), 'economic conditions in their sector' (82%) and 'insufficient competitive pressures' (53%).
- 21% of smaller firms are looking to decrease their pension spend, balanced by 14% aiming to increase spend.
- Firms responding to the survey report average combined employer and employee contributions into defined contribution schemes ranging between 7.6% and 9.3% of earnings.

¹ ACA Survey Report on *Auto-enrolment and NEST* in larger organisations, published 31 August 2010 (see: www.aca.org.uk)

Executive Summary continued...

Auto-enrolment and NEST

- 54% of smaller employers support the principle of auto-enrolment into workplace pensions.
- Only 1 in 5 smaller firms has as yet budgeted for the cost of auto-enrolment. However, 53% say the introduction of auto-enrolment and NEST will 'significantly' add to their business costs.
- Over 60% of smaller firms are likely to auto-enrol current 'non joiners' into existing schemes. However, 20% say they will close their existing scheme and auto-enrol all employees into NEST.
- Around a fifth of smaller firms say they will auto-enrol employees into a new firm's scheme, or will restrict entry into an existing scheme placing the balance of employees in NEST, or will use NEST as a foundation scheme.
- Smaller firms expect an employee 'opt-out' rate after auto-enrolment of, on average, 35%.
- 29% of smaller firms are 'likely' or 'highly likely' to consider levelling-down to mitigate the cost of auto-enrolling additional employees.
- Support for NEST is mixed. 43% of smaller employers agree with it, while the remainder are split between those who would prefer commercial provision (11%) and those who disagree with the concept altogether (46%).
- 58% want minimum pension contributions to be a percentage of basic pay rather than of full earnings, although 40% support an earnings basis.
- 66% say that employers with one employee (and 50% with fewer than five employees) should be exempt from auto-enrolment.
- 53% say that the requirement to re-enrol 'opters-out' every three years should be removed.
- 61% say employees with less than 3 months' service should not be auto-enrolled.
- Overall, 53% say the auto-enrolment review should not recommend a delay in its introduction.

Facts and figures: smaller firms' place in the UK economy

The smaller firms sector – firms employing 250 or fewer employees – is the largest part of the UK private sector economy in terms of employment. These smaller firms employ over half of the UK's private sector employees and generate a half of all private sector turnover, amounting to some £1,500 billion per year. These firms make up over 99% of all UK private sector enterprises – there are only just over 6,000 UK private sector enterprises that now employ 250 or more employees.

Whilst figures vary from year to year, there are around 1.2 million organisations that employ at least 1 employee, the majority being companies (755,000), but also including employees of partnerships (177,000) and of sole proprietors (306,000). In a typical year, the number of employing organisations ceasing and forming can be around 30 - 40,000. Only a minority of these employers provide any form of workplace pension.

The major test for the auto-enrolment and NEST regime will be to capture data on these 1.2 million firms (the majority with fewer than 5 employees), whilst also being able to cope with the dynamic changes in business numbers each year, the movements of employees from firm to firm and changes in opt out decisions, and – of course – pension investments and individual employee's changes thereto. This will be an extremely challenging task with an exacting timetable under the staging arrangements published to date.

Figure 1: UK private sector: number of enterprises and employment by size of firms

UK Smaller private sector firms	Number of enterprises	Employees (thousands)	Average number of employees per enterprise
No employees (see note below)	3,545,720	523	-
1 employee only	192,055	192	1
2-4 employees	617,130	1,612	3
5-49 employees	395,645	4,702	12
50-249 employees	26,710	2,651	99
Total: smaller firms (1-249 employees)	1,231,540	9,157	7

(Source: Dept of Business Innovation and Skills, Enterprise Directorate Analytical Unit, 2008 figures, published 14 October 2009)

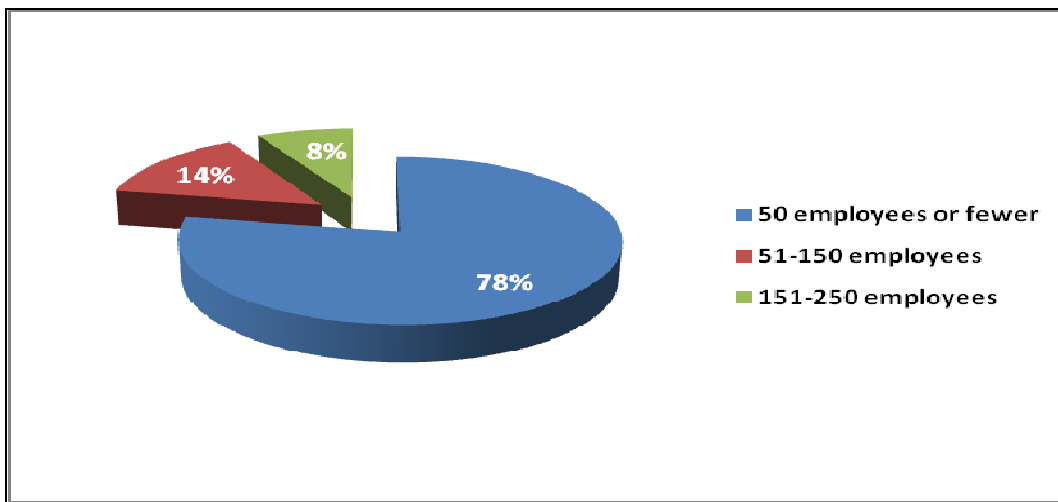
Note: 'No employees' comprises sole proprietorships and partnerships comprising only the self-employed owner-manager and companies comprising only an employee director)

Smaller firms responding to the survey: by employee numbers

Over three-quarters of the smaller firms responding to the survey employ 50 or fewer staff, with the balance of respondents employing between 51 and 250 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 50 or fewer employees².

Equally, with only 12% of respondents indicating they do not run a pension scheme, the sample is not typical of the sector as a whole in that it over represents the proportion of smaller firms offering pension arrangements. Reflecting the impetus behind the Pensions Commission's reports, it remains the case that over 65% of the UK's smaller firms provide no workplace pension provision, albeit it is estimated around a further 5% make contributions into employees' personal pensions only³.

Figure 2: Smaller firms - organisations responding to the survey



² Source: ONS Inter-Departmental Business Register 2009

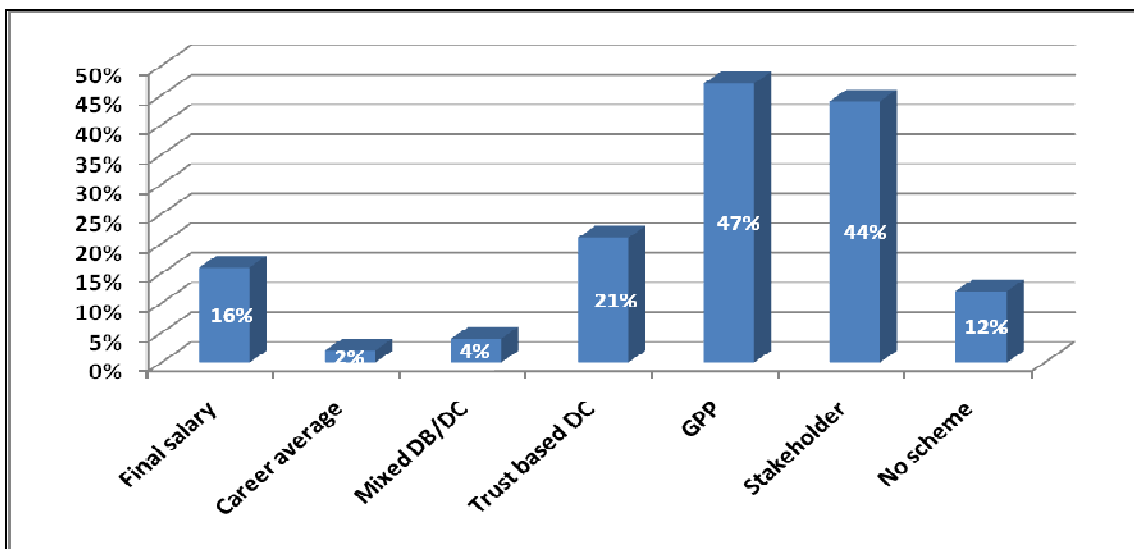
³ Source: DWP Research Report *Employers' attitudes and likely reactions to workplace pension reforms 2009*

Types of schemes run by smaller firms responding to the survey

As this survey is of smaller employers, the dominant types of scheme being run by respondents are defined contribution in nature, with Group Personal Pension Schemes (GPPs) and Stakeholder schemes the most common. Of the final salary schemes offered by these smaller employers, 86% are reported as closed to new entrants and, of these, 41% are now also closed to future accrual by existing employees. The sample includes only a few career average revalued schemes and mixed DB/DC arrangements.

Reflecting the move away from trust based in favour of contract based defined contribution schemes, 11% of trust based schemes are reported as closed to new entrants, with the majority also closed to new contributions from existing employees. The majority of these firms now offer either GPPs or Stakeholder schemes.

Figure 3: Smaller firms - schemes in survey: by type

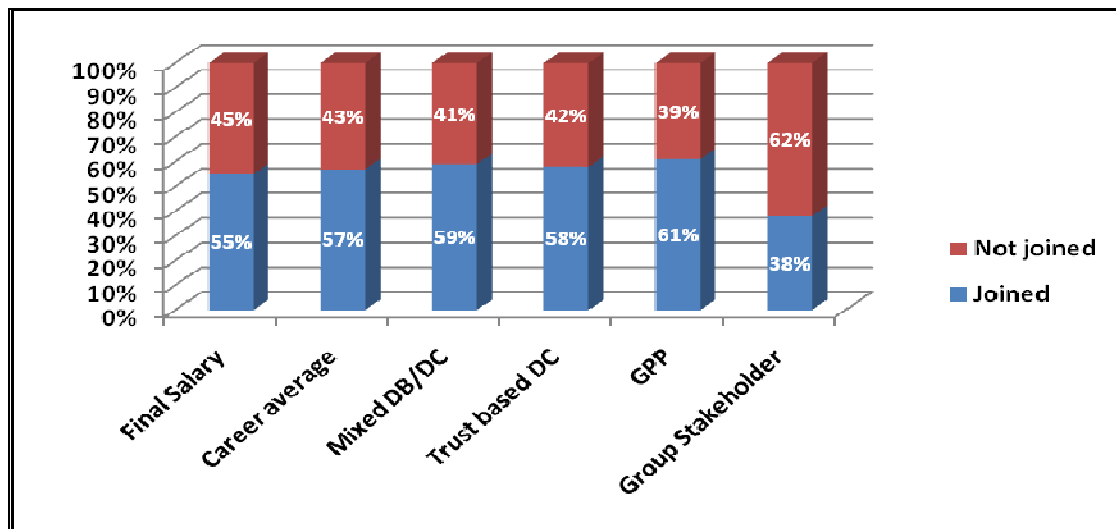


Average scheme membership by eligible employees

Of those eligible to join workplace pension schemes in these smaller firms, average participation rates vary between 38% in Stakeholder schemes with members (27% of Stakeholders reported 'nil' members) through to 61% in Group Personal Pensions (GPPs). Of those firms responding to the survey just 6% already auto-enrol at least some employees into a scheme.

Across this sample, generally over 40% of employees are not in membership of workplace schemes (with this rising to 100% for the 12% of respondents who provide no scheme). There are clear implications in cost terms for these firms when they have to auto-enrol employees into either existing 'qualifying' schemes or into NEST under the Government's current staging and phasing schedule between 2014 and 2016. The degree of cost increases will hinge upon the level of opt-outs and the levels of employer contributions into the future for existing and new members.

Figure 4: Smaller firms - scheme membership



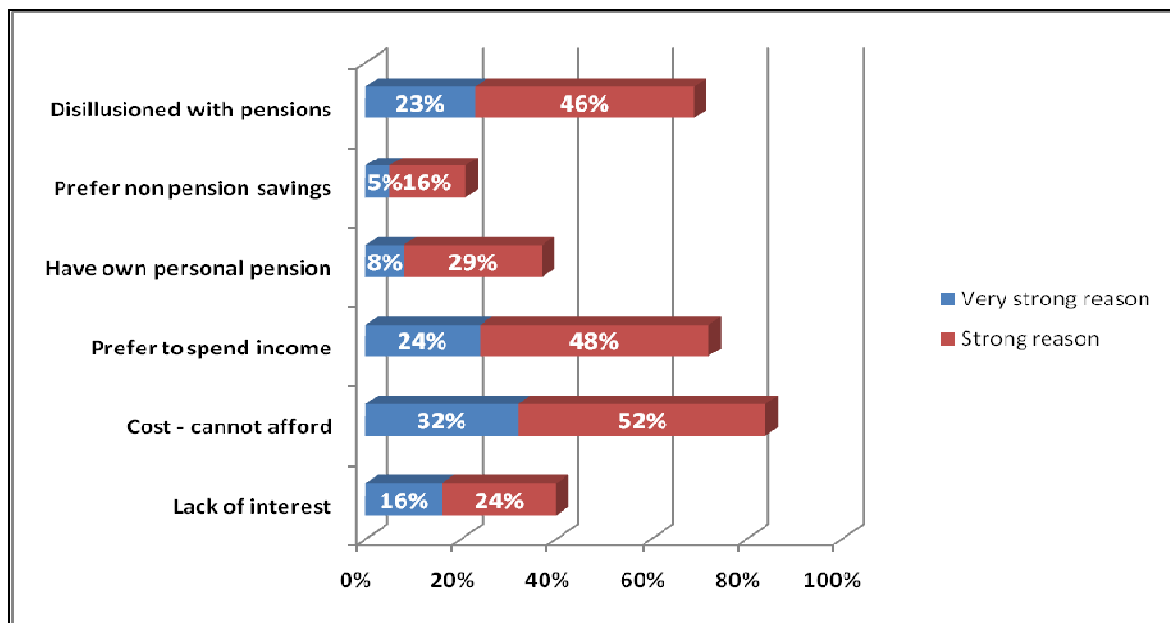
Why are so many employees in smaller firms not in pension schemes?

Respondents are very clear on why they feel so many employees have not joined existing workplace pension schemes. 84% say employees 'cannot afford the cost' (although, 72% also say employees prefer to 'spend their income'). Whilst amongst lower income groups, ONS figures suggest there is little or no room for private savings given current spending patterns and credit commitments, it is less clear this is the case for those around and above average earnings.

A worrying finding is that 69% of firms believe employees are 'disillusioned with pensions', no doubt in the wake of trends over the last decade. Disappointing growth in pension pots as investment returns have reduced, lower annuity rates and, for some, experiences of scheme closures and levelling-down will all have played a part in this situation. The prospect of later retirement ages may also be deterring younger employees from pension saving – other earlier spending priorities appear much more relevant.

These results underscore that whilst auto-enrolment into workplace pension schemes may indeed increase the numbers making pension savings from 2012, there remain huge financial and communication challenges to be addressed if we are not to see the emergence of high opt-out rates. This is particularly the case in this smaller firms sector where pay, benefits and resources for communication tend to be generally lower than in larger private and public sector organisations.

Figure 5: Smaller firms with pension schemes – why do you think employees do not join?



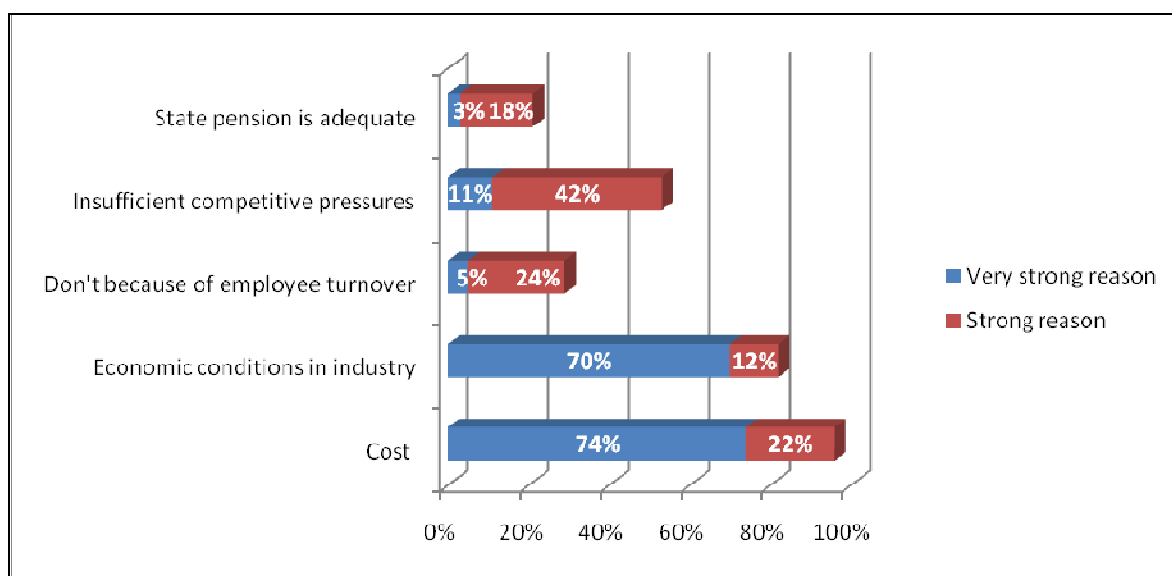
Why do smaller firms not offer pension arrangements?

The reason given by the smaller firms responding to the survey, who do not offer pension schemes, as to 'why not?' is clear cut. Some 96% say this is down to 'cost', a view which they say is buoyed at present by the economic conditions in their respective industries.

Over half say that competitive pressures in their work sectors do not require that they provide pension arrangements, with three in ten saying the high levels of staff turnover they encounter is also providing a further disincentive.

Somewhat surprisingly, one in five firms says that they feel the State pension is 'adequate' to meet the retirement needs of employees. Given the level of State pensions in the UK, this is a difficult response to justify unless respondents believe means-tested State benefits should continue to be a major source of additional income for many in retirement.

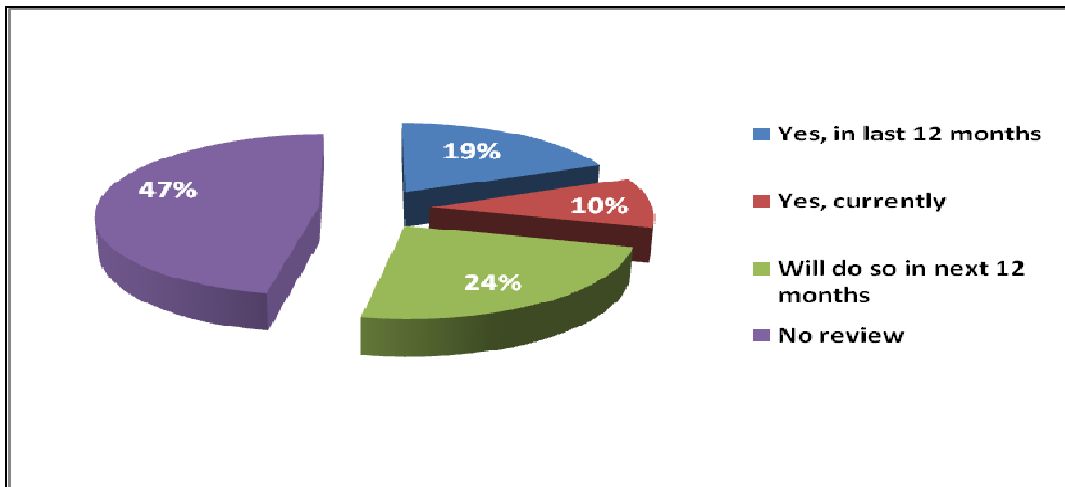
Figure 6: Smaller firms with no pension scheme or employer contribution – why is this?



Scheme reviews

Given the uncertainties of how the 2012 pension reforms may pan out post the current Government's reviews, it is perhaps surprising that a majority of these smaller employers will have reviewed their pension arrangements over a 2 year window. It maybe that this reflects the stream of regulatory measures impacting on existing arrangements in recent years. However, given the numbers looking to undertake reviews in the next 12 months (24%), it may be a sign that the 2012 reforms are beginning to be noticed, with early actions now being considered. Although smaller firms have more time to consider how they should react to the reforms, it may well be that the staging and phasing message has not been fully appreciated, with many of these smaller businesses registering the '2012' date as one they must act by.

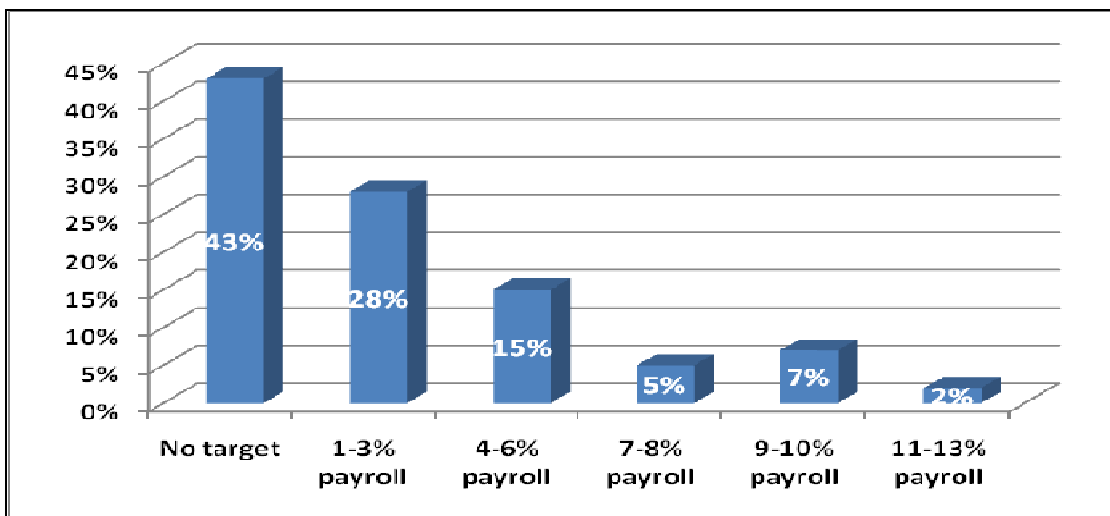
Figure 7: Smaller firms: have you or are you about to review your pension arrangements?



Targets for pension costs

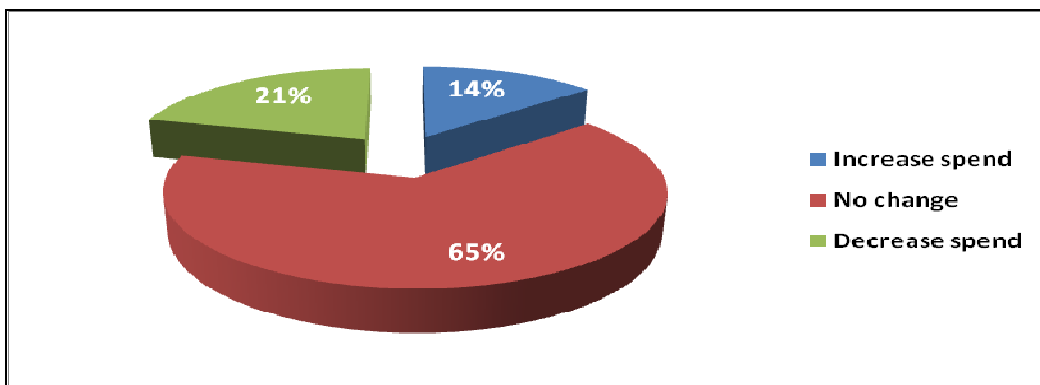
Whilst four out of ten smaller firms say they have no target as to what their pension costs are or should be, it is encouraging that three in ten are targeting employer pension costs of 4% of payroll or more (i.e. broadly in excess of the minimum employer contribution levels that will come into full force from October 2017 for employees in membership of 'qualifying' company schemes or NEST). The concern is that those saying 'no target' is made up of those firms who presently make no workplace provision (12%) or where employer contributions are presently around the minimum of 3% of earnings (but where the earnings definition may be somewhat narrower than presently envisaged by the auto-enrolment/NEST regulations).

Figure 8: Smaller firms: do you have a target as to what your business will spend on pensions as a percentage of payroll?



However, given the difficult economic times many businesses are experiencing, it is relatively ‘good news’ that those looking to reduce pension spend only modestly outnumber those looking to increase spend, with the majority holding to their current spend on pensions. Whether the October 2010 Spending Review may cause more businesses to ‘think twice’ about their budgets, including pension costs, remains to be seen.

Figure 9: Smaller firms: overall, is your business trying to increase or decrease its spend on pensions?



Pension contribution levels

Employer contributions into defined contribution schemes across these smaller employers are averaging between 4 to 7% of earnings, with employee contributions hovering between 3% and 4% of earnings. Contribution levels reflect both the type of arrangement provided and the size of employer. In the main, trust based defined contribution schemes are attracting higher levels of contributions than both GPPs and Stakeholder schemes. Also, both employer and employee contributions in firms with over 150 employees tend to be higher than in firms with fewer employees.

What these figures indicate, however, is that as auto-enrolment (and NEST) press ahead, there is limited scope for levelling-down existing pension contributions to mitigate the potential cost of enrolling additional employees into schemes. As we reported in our earlier survey of larger organisations, levelling-down is much more likely to be a feature in larger organisations where current employer contribution levels tend to be much higher. That said, there is scope in the average contribution rates reported for levelling-down in a swathe of smaller firms to defray the cost of additional employees joining ‘qualifying’ schemes from 2014.

Whether this occurs is likely to depend on estimates of how many employees will opt-out (estimates, at present, are much higher amongst these smaller firms than has been reported by larger employers, see page 17). What may also hold down costs is if current ‘non members’ are enrolled into schemes where employer contributions are lower than existing members. Such a two-tier approach to provision may seem to have negative HR implications and may prove difficult to deliver in practice, but the DWP’s 2009 research seems to suggest this is an approach being considered by some employers⁴. Certainly, the upcoming

⁴ Source: DWP Research Report *Employers’ attitudes and likely reactions to workplace pension reforms 2009*

reforms may well accelerate the closure of those remaining open defined benefit schemes in the sector (where average employer contributions are presently 17% of earnings), with both new and existing employees being moved into lower cost DC schemes.

Figure 10: Smaller firms: 2010 defined contribution levels broken down by firms' sizes

Average employer contributions	1-50 employees	51-150 employees	151-250 employees	All
Trust based defined contribution	4.8%	5.5%	6.6%	5.5%
Group Personal Pension	3.7%	4.9%	5.5%	4.2%
Stakeholder scheme	4.1%*	4.8%*	5.2%*	4.3%*

Average employee contributions	1-50 employees	51-150 employees	151-250 employees	All
Trust based contribution	3.1%	4.2%	4.6%	3.8%
Group Personal Pension	3.2%	3.6%	4.1%	3.4%
Stakeholder scheme	3.6%	3.8%	4.3%	3.7%

Average combined contributions	1-50 employees	51-150 employees	151-250 employees	All
Trust based contribution	7.9%	9.7%	11.2%	9.3%
Group Personal Pension	6.9%	8.5%	9.6%	7.6%
Stakeholder scheme	7.7%*	8.6%*	9.5%*	8.0%*

Note: Stakeholder figures exclude 27% of schemes with 'nil' employer contributions

Key findings: auto-enrolment

Throughout this section of the report, the results are compared with the ACA's survey report on auto-enrolment and NEST conducted amongst larger private and public sector employers, which was published in August 2010⁵.

Do you broadly agree with there being a new employer duty to auto-enrol most employees into a workplace pension scheme with certain minimum standards?

A majority of smaller firms (54%) say they support the new employer duty to auto-enrol into a qualifying scheme. This is somewhat lower than we reported amongst larger firms (75%) and, perhaps, is higher than might be expected given the extra costs involved in auto-enrolment in a sector where current pension scheme participation rates are relatively low. However, as we note elsewhere in the report, this response may to some degree reflect a generally pessimistic view by firms in terms of how many employees will continue in scheme membership following auto-enrolment.

Figure 11: Smaller firms - support for auto-enrolment

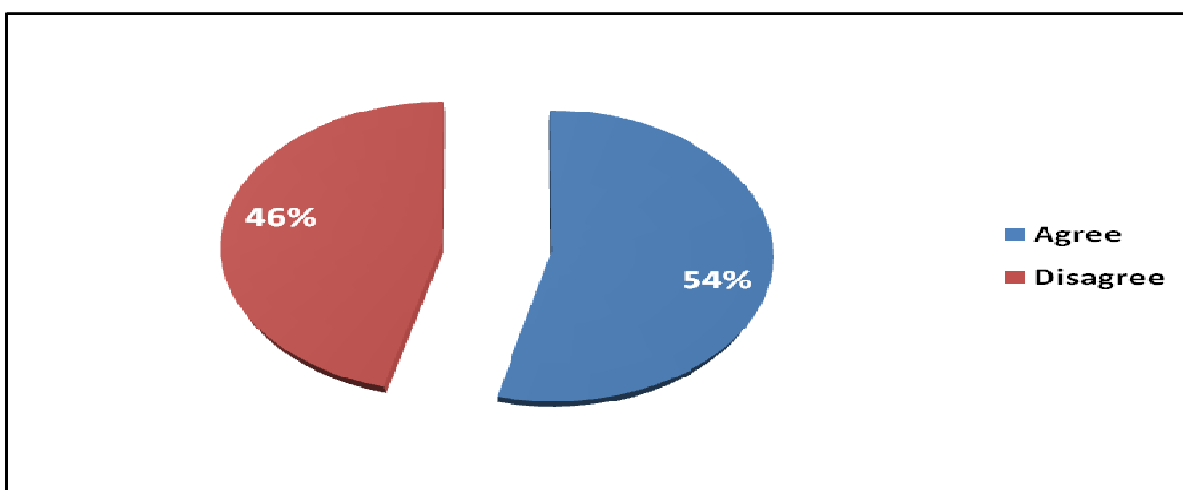
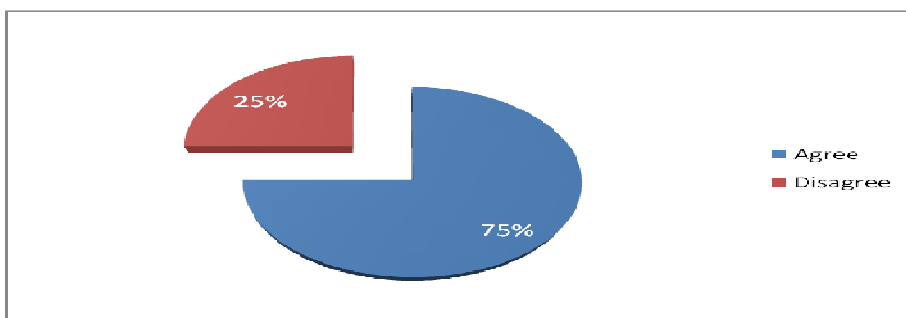


Figure 11B: Larger firms - support for auto-enrolment



⁵ ACA Survey Report on *Auto-enrolment and NEST* in larger organisations, published 31 August 2010 (see: www.aca.org.uk). The survey covered 210 employers with pension scheme assets of £161bn. Three-quarters of the respondents employed in excess of 1,000 employees, including a quarter employing in excess of 10,000.

Do you broadly agree with there being a new national scheme (NEST) set up that employers must auto-enrol most employees into if they do not offer access to a workplace pension scheme of a minimum standard?

A sizeable minority (43%) of these smaller firms are supportive of NEST (the National Employment Savings Trust) as a fall back arrangement where employers fail to offer their own 'qualifying' workplace pension scheme with certain minimum standards into which employees are auto-enrolled.

Of those that are opposed to NEST, 46% disagree with the concept – in the main these are those who also oppose the auto-enrolment approach. A further 11% oppose NEST on the basis that they feel existing commercial providers should be able to meet the market's needs, presumably on the basis that this would avoid the need to establish a costly new centrally organised administration at a time when the Government's financial resources are already over-stretched (and given the impact that these costs are having on charges to members over the foreseeable future). The difficulty with this view is that commercial providers have shown little enthusiasm for such an approach. It would probably only be viable in cost and organisational terms if the number of employers being required to auto-enrol employees is radically reduced (over 1.2 million enterprises employ one or more employees) or if the requirement to auto-enrol is relaxed so organisations have a longer period to comply, perhaps initially making this voluntary at the micro-employer level.

Figure 12: Smaller firms - attitudes towards NEST

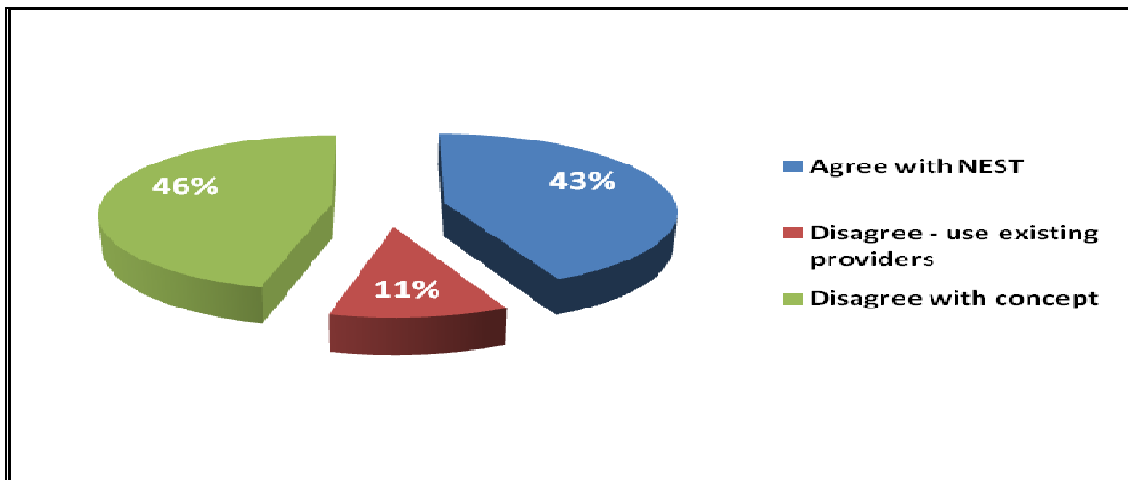
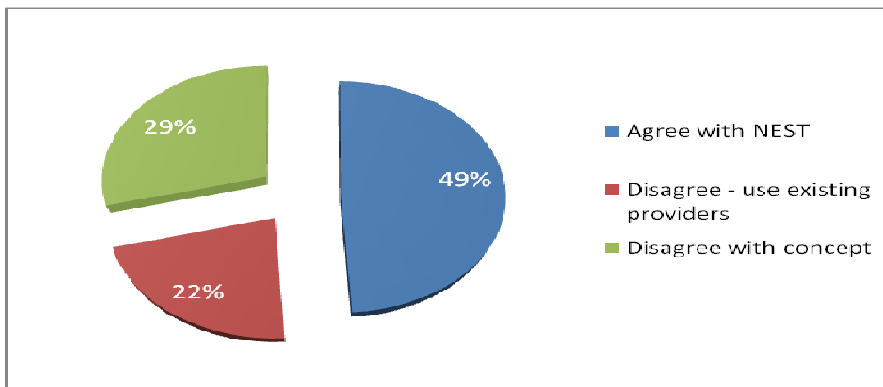


Figure 12B: Larger firms - attitudes towards NEST



Under current policy, depending on the number of employees in your firm, you will be required to auto-enrol all ‘eligible jobholders’ into a ‘qualifying workplace pension scheme’ (QWPS) - a firm’s scheme or NEST - between 2012 and 2016. Are you aware of the date when your firm must auto-enrol ‘eligible jobholders’ into a qualifying scheme?

Perhaps surprisingly, 54% of these smaller firms say they are aware of the date between March 2014 and February 2016 when they must auto-enrol eligible jobholders into either a ‘qualifying’ existing or new firm’s scheme or NEST.

In October 2012, the largest employers begin auto-enrolment. In fact, the vast majority of firms responding to this survey will have to auto-enrol from March 2014 (by which time all employers with over 90 employees will have had to comply) onwards through to 2016. Those remaining firms offering auto-enrolment into an open defined benefit or hybrid scheme will however not have to auto-enrol until October 2016.

If there is no change to the process as a result of the current review, the challenging period for those running and monitoring auto-enrolment will be in the period from April 2014. Over a 4-month period, some 27,000 enterprises with between 50 and 249 employees will be expected to begin auto-enrolment (unless they already do so). And then, the even bigger task – in the next 18 months, some 1.2 million enterprises with fewer than 50 employees will be required to introduce auto-enrolment. These are challenging numbers and given the inevitable restrictions on spending to implement this policy at a time when the economic position remains very uncertain, serious questions need to be asked by the reviewers and Government as to whether the timetable is at all realistic. The recent difficulties encountered by a well-established body (HMRC), in administering correctly the records of millions of taxpayers, hardly bodes well for the auto-enrolment ‘enforcers’ (NEST, its contractors and TPR), who with far fewer resources will be expected to cope with millions of individual employee records and an entirely new compliance regime.

Elsewhere in the survey, respondents are supportive of changes in policy that would remove micro-employers from the requirement to auto-enrol and, certainly, the ACA recommendation to the reviewers is that it may be wise to delay any extension of auto-enrolment to this group until there is a clearer picture of how successfully it has been implemented across larger organisations.

Figure 13: Smaller firms - awareness of auto-enrolment date for organisation

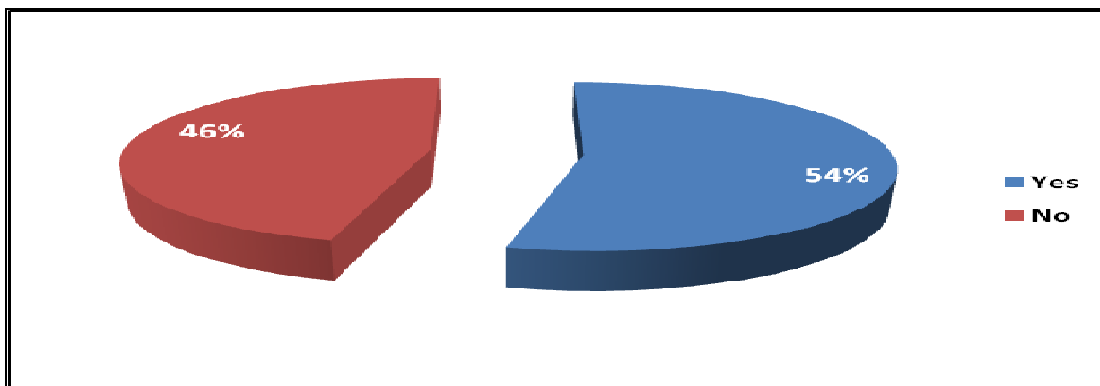
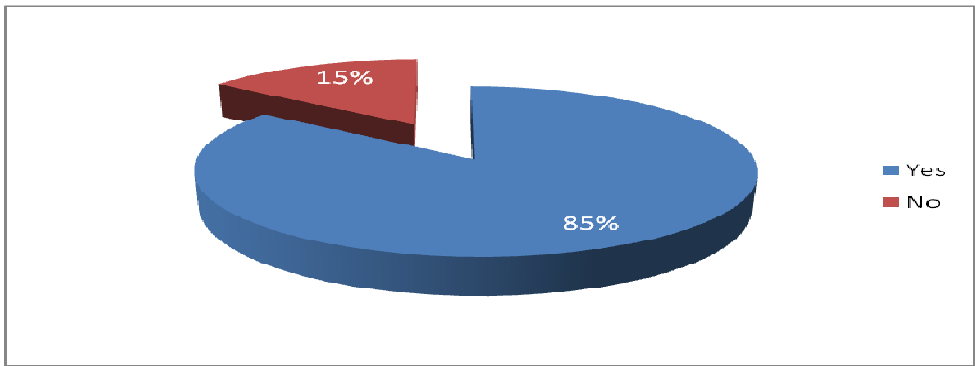


Figure 13B: Larger firms - awareness of auto-enrolment date for organisation



Have you budgeted for the likely increase in costs that could arise from higher scheme membership as a result of auto-enrolment?

A minority of respondents (21%) of these smaller firms have at present budgeted for the likely increase in costs arising from auto-enrolment. Given the generally low level of scheme participation in open defined contribution pension arrangements reported here (see *Figure 4*), this is troubling, albeit it is three to four years before the first compulsory requirement to auto-enrol in smaller firms. It may mean many more employers over the next two to three years or so will wake up to the potential costs involved and take mitigating actions, leading to an increase in scheme reviews (this may already be evident, see *Figure 7*). There is also the potential for some levelling-down of contributions, or other cost reductions that may impact on pay levels or employment numbers.

Of those organisations that have budgeted for extra costs, the average opt-out rate assumed by these smaller firms is 35% (much higher than for larger firms, where our recent survey found an average anticipated opt-out rate of just 15%). For many open schemes, this suggests auto-enrolment in smaller firms might lead to modest increases in membership as low as 5% (where membership is already around 60% of eligible employees) through to +25%, where membership levels are low – potentially increasing employer pension contribution costs by similar (and often higher) percentage amounts. Where no scheme is presently in place at all, the costs falling on these smaller employers, phased in over the period 2014 to 2017, will be greatest.

Figure 14: Smaller Firms - have you budgeted for auto-enrolment?

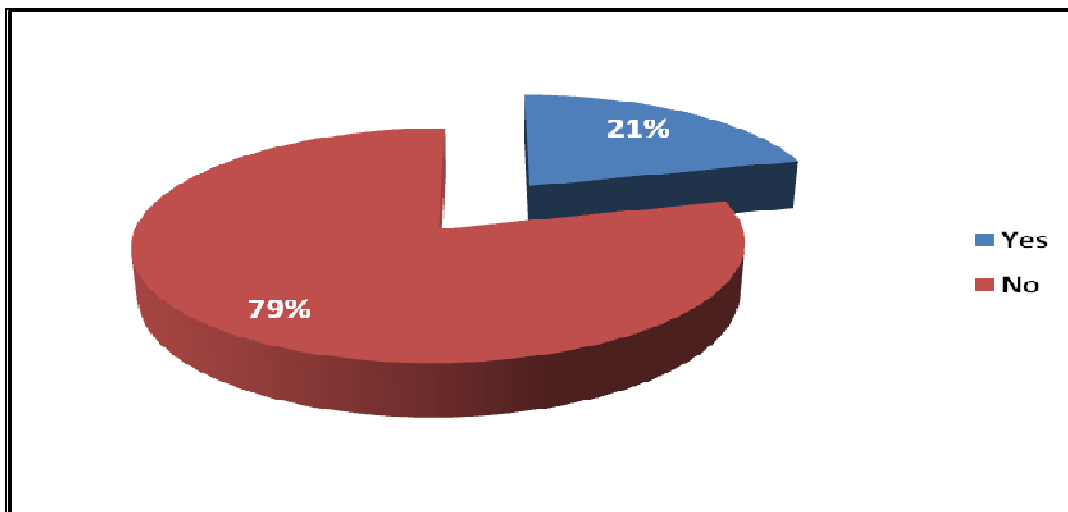
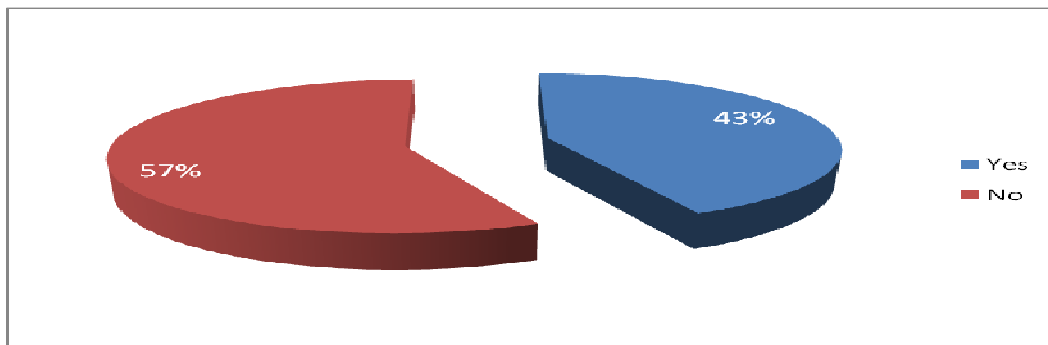


Figure 14B: Larger firms - have you budgeted for auto-enrolment?



What in your view will be the most likely response of your firm to auto-enrolment and NEST?

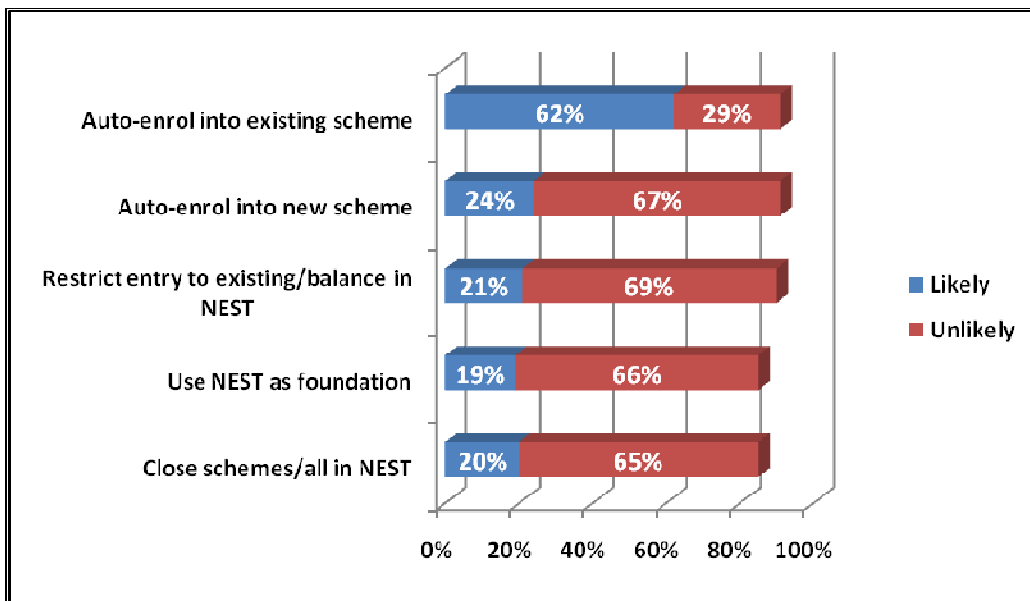
The survey found that most of these smaller firms are likely to auto-enrol present 'non joiners' into their existing pension scheme(s) – in the main into GPPs, Stakeholder and trust based DC schemes. There may be some levelling-down in contributions to mitigate costs (see *Figure 16*), where current employer contributions exceed the minimum to apply from 2017 (presently, 3% of band earnings).

The results also suggest over a fifth of organisations will consider auto-enrolling into a new domestic scheme, suggesting either the closure of existing schemes, both defined benefit and defined contribution, or the possibility that present 'non joiners' will be enrolled into new schemes, possibly attracting lower employer contributions⁶. A further fifth say they will restrict entry into their existing schemes, auto-enrolling the balance of employees into NEST and another fifth may use NEST as a foundation scheme, running a firm's top-up scheme above this.

A further fifth are likely to close their existing arrangements, largely made up of firms where Stakeholder schemes have not taken off, where employer contribution levels are close to the 3% of earnings level or where present participation rates are low.

Of those firms presently not running workplace schemes, the majority are as yet undecided as to what they will do, with the remainder split between opening a firm's scheme, or using NEST.

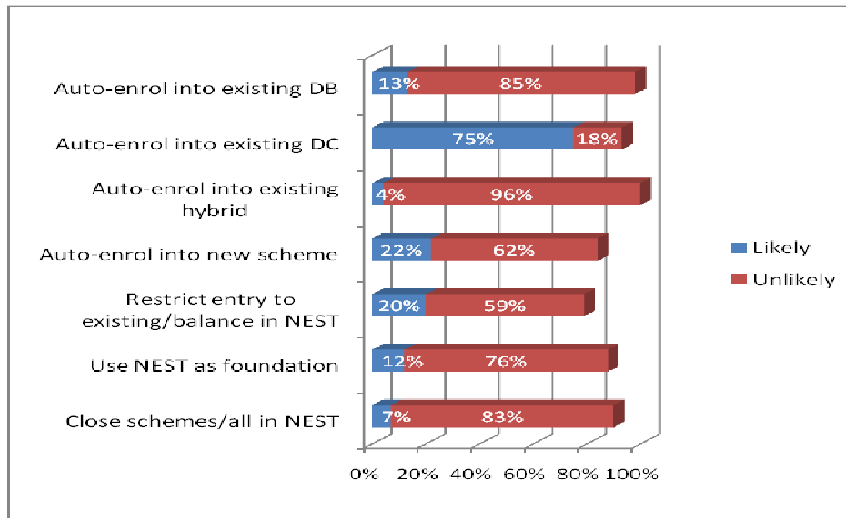
Figure 15: Smaller firms - organisation responses to auto-enrolment and NEST



Note: Where totals are below 100%, the balance of respondents said 'not sure'.

⁶ This is supported by the findings in DWP Research Report *Employers' attitudes and likely reactions to workplace pension reforms 2009*

Figure 15B: Larger firms - organisation responses to auto-enrolment and NEST



Note: Where totals are below 100%, the balance of respondents said 'not sure'.

Will you review existing scheme(s) benefits to mitigate the cost of higher scheme membership from auto-enrolment?

Three out of ten firms (29%) are likely to review existing scheme benefits/contributions to mitigate the cost of higher scheme membership from auto-enrolment. Given the numbers that have so far budgeted for the costs of auto-enrolment (21% - see *Figure 14*), this may be a number that climbs as more organisations identify potential cost increases over the next few years. Given current participation rates in schemes (see *Figure 4*), and the anticipated increases in membership expected from auto-enrolment suggested by this survey (increases in membership of 5-25% of employees), there must be the expectation of some modest levelling-down of contributions, where these are presently higher than the proposed minimum levels applying from 2017. There may also be adjustments to pay and employment levels, or lower pension contribution rates for 'non joiners' and new entrants. Much is likely to hinge on the economic situation over the next few years and how this impacts on business performance and costs.

Figure 16: Smaller firms: auto-enrolment: will your organisation mitigate the cost of higher scheme membership

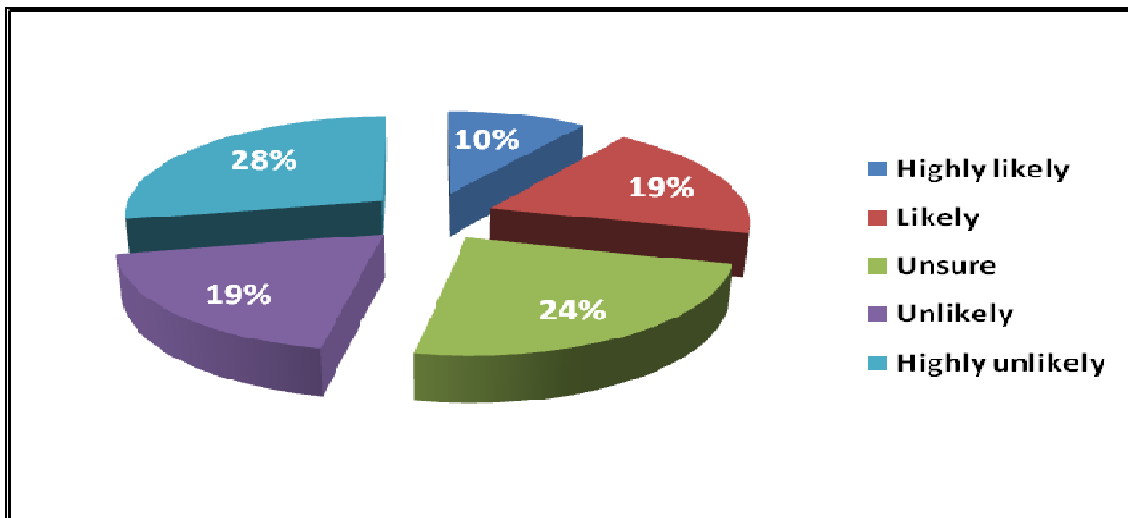
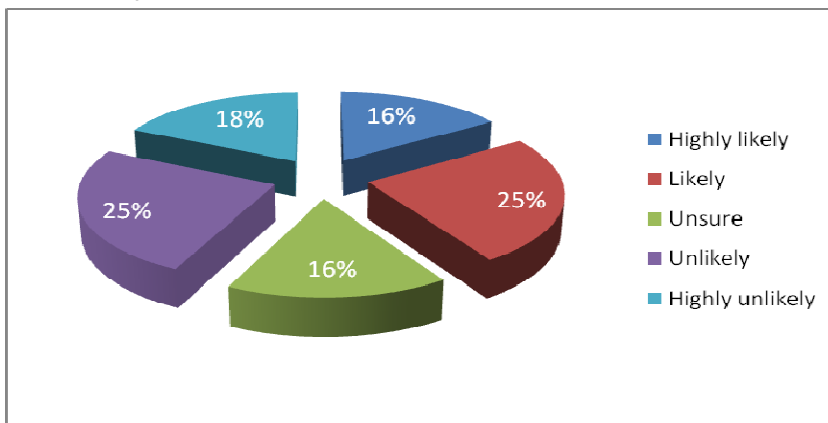


Figure 16B: Larger firms: auto-enrolment: will your organisation mitigate the cost of higher scheme membership



Should the review of auto-enrolment consider any change to the presently planned minimum contribution of 8% of band earnings (4% from employee, 3% from employer, 1% tax relief), which will apply in full from October 2017?

A majority of respondents favour 'no change' in the planned minimum contribution of 8% of band earnings (4% employee, 3% employer and 1% tax relief) to apply in full from October 2017. Around a quarter favour an increase in the contribution rates, with only a minority calling for reductions in contribution levels.

Figure 17: Smaller firms - should minimum contribution rates be changed?

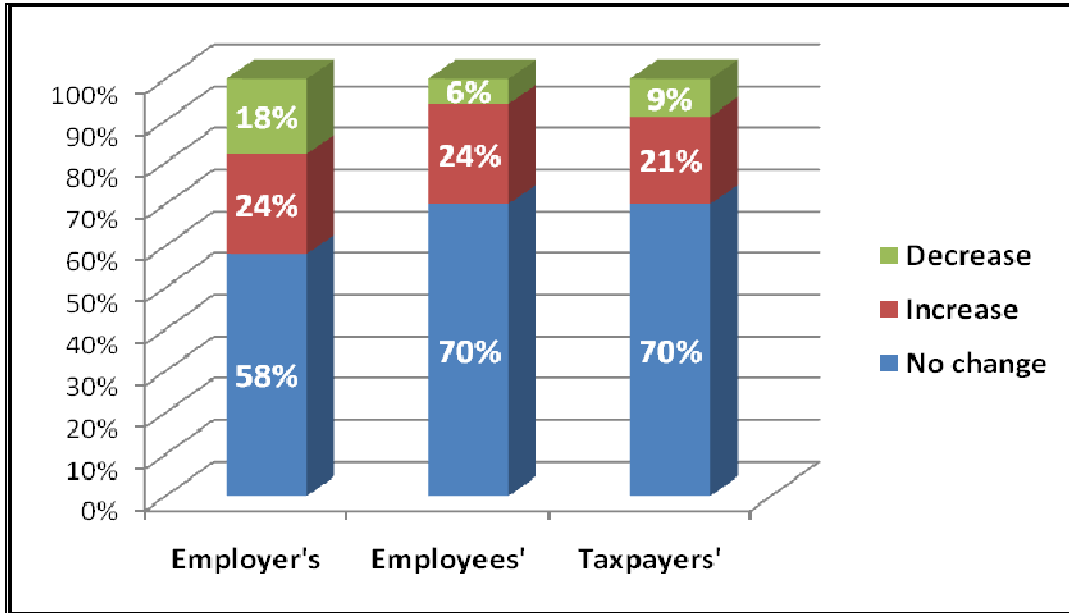
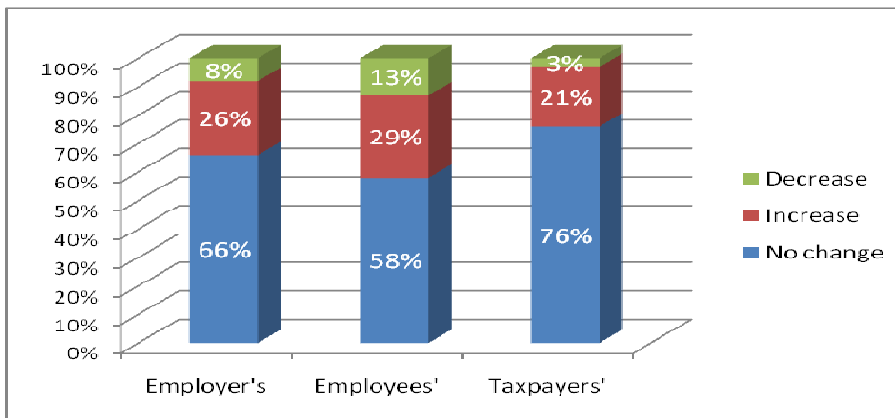


Figure 17B: Larger firms - should minimum contribution rates be changed?



Under current rules, minimum pension contributions are to be based on a percentage of earnings (including salary, wages, overtime, bonuses and commission) rather than a percentage of basic pay. Do you agree with this?

There has been much debate during the genesis of the auto-enrolment/NEST about how best and most simply to determine minimum contribution rates. As matters stand, contribution rates are to be based on a percentage of earnings (including salary, wages, overtime, bonuses and commissions) rather than a simple percentage of basic pay.

Our survey found four out of ten smaller firms support an earnings basis – a much higher percentage than we found amongst larger firms in our earlier survey. This different viewpoint may reflect differences in the general make-up of pay between larger and smaller firms. The ACA has made a number of recommendations to the reviewers as to how the ‘earnings issue’ might be resolved.

Figure 18: Smaller firms - contributions: link to earnings or basic pay?

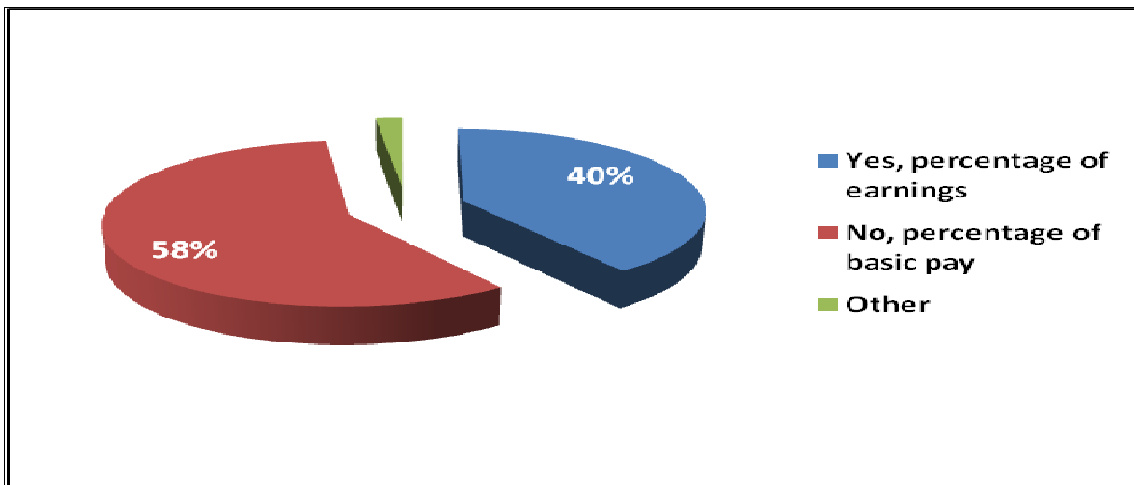
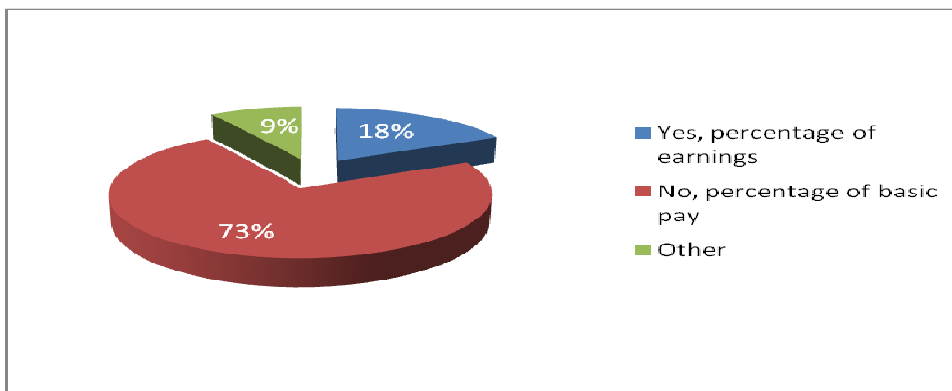


Figure 18B: Larger firms - contributions: link to earnings or basic pay?



Do you think auto-enrolment should be delayed or removed in respect of certain requirements?

The survey investigated a number of current requirements in respect of auto-enrolment and whether any should be delayed or removed.

In fact, respondents said none of the requirements listed should be delayed, but a majority say the following:

- 61% say those with under 3 months' service should not be auto-enrolled
- 66% say firms with 1 employee (and 50% say firms with fewer than 5 employees) should be removed from the auto-enrolment requirements
- 53% say the requirement to auto-enrol every 3 years should be removed

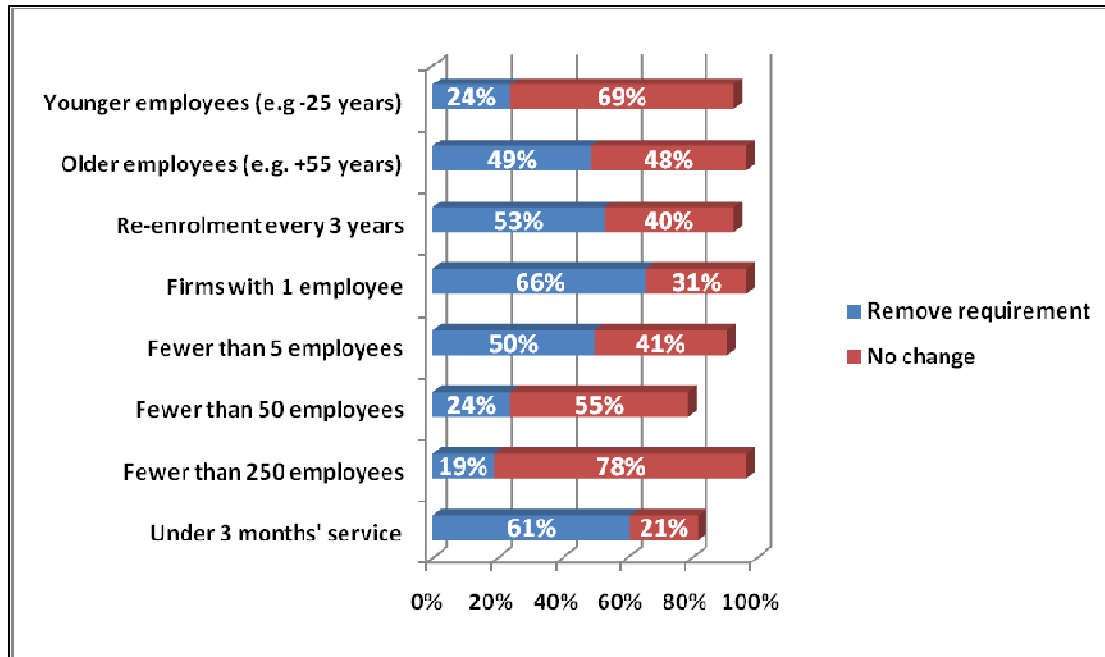
Encouragingly and giving support to the auto-enrolment project, these smaller firms opposed decisively the exclusion of firms with 5 or more employees from the requirement to auto-enrol. If the auto-enrolment policy was reviewed to exclude firms with just 1 employee, then this would reduce the number of firms that the auto-enrolment regime would need to manage by some 200,000. More significantly, excluding firms with fewer than 5 employees would reduce the number of firms subject to auto-enrolment by a further 600,000. Such a decision would greatly ease the administrative challenge faced by the auto-enrolment regime, whilst only reducing the numbers eligible for auto-enrolment by around 2 million (leaving 8-9 million still covered by the policy)⁷. Excluding these micro-employers need not be a permanent decision. Once the regime has been established and been seen to work efficiently, smaller firms could be gradually eased into coverage.

Firms were split down the middle as to whether auto-enrolment should be removed for older employees joining a scheme/NEST (say those aged 55 or over), where some argue there is a danger of a mis-sale as the amounts that might be saved until retirement may only produce sufficient income to disentitle retirees from State benefits. Set against this, there is the view that excluding older employees might stop those working on past today's retirement age from generating worthwhile funds, particularly if they work on towards 70 or beyond.

A clear majority oppose the requirement for younger employees (between age 22 and, say, age 25) to be excluded on the basis they may move employments more rapidly and have other spending priorities in their early 20s.

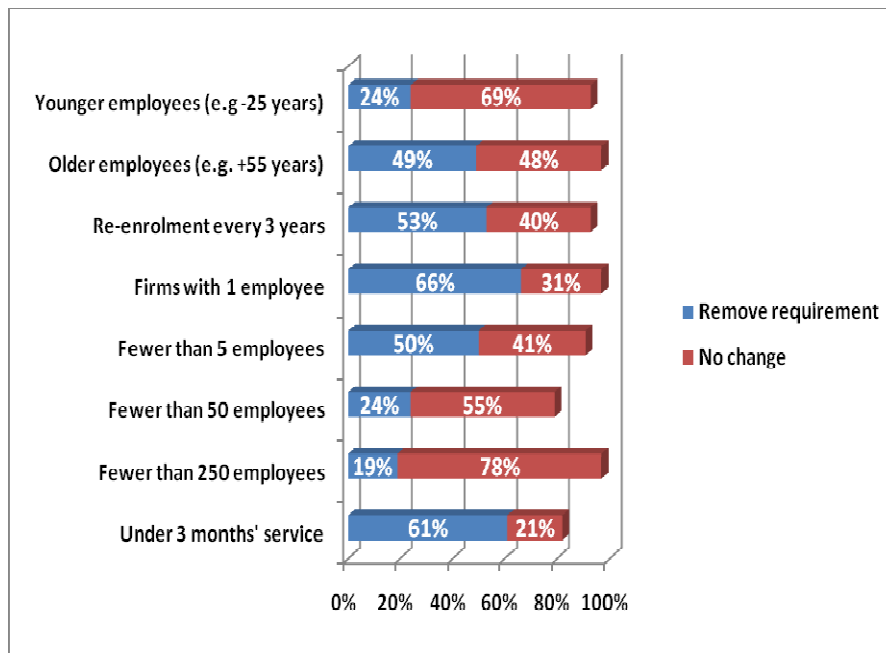
⁷ See *Hansard*, Column 1152W, 27 July 2010: Steve Webb MP replying to a written Parliamentary Question by Angela Eagle MP.

Figure 19: Smaller firms: should auto-enrolment be removed as a requirement for:



Note: where totals fall short of 100%, the balance of respondents said 'delay'

Figure 19B: Larger firms: should auto-enrolment be removed as a requirement for:



Note: where totals fall short of 100%, the balance of respondents said 'delay'

Do you think auto-enrolment should be delayed as a requirement until the Government passes legislation to allow employers greater freedom to offer more flexible pension designs than at present?

Currently, many would argue that there are too many complexities in UK legislation, so employers find it difficult to design pension arrangements that are cost effective and flexible enough. In particular, the defined benefit regime is too prescriptive and, as a result, the number of open schemes has reduced rapidly in recent years. Whereas in 1996 our *Smaller Firms Pension Survey* found 82% of such schemes were open to new entrants, just 14 years later we found a similar number now closed. If there were to be greater freedom and flexibility in design, it is doubtful in this sector that the appetite for DB 'lite' or a risk sharing approach would re-kindle defined benefit provision, other than at the margins by the larger firms. However, what is relevant is that firms' trust based defined contribution schemes are also in decline due to the more onerous regulatory requirements that apply to them as against contract based arrangements. It is important that the regulatory regimes covering such schemes are both proportionate and offer a level playing field.

If the existing pension regimes are not eased ahead of the introduction of auto-enrolment, then it seems likely that the process of employers levelling-down existing provision (both what remains of DB and firms' trust based DC) will continue. This may raise questions as to whether the governance of new defined contribution arrangements is as robust as it needs to be given the increasing number of employees covered by such arrangements.

Figure 20: Smaller firms: auto-enrolment to await Government legislation to allow greater freedom of pension design

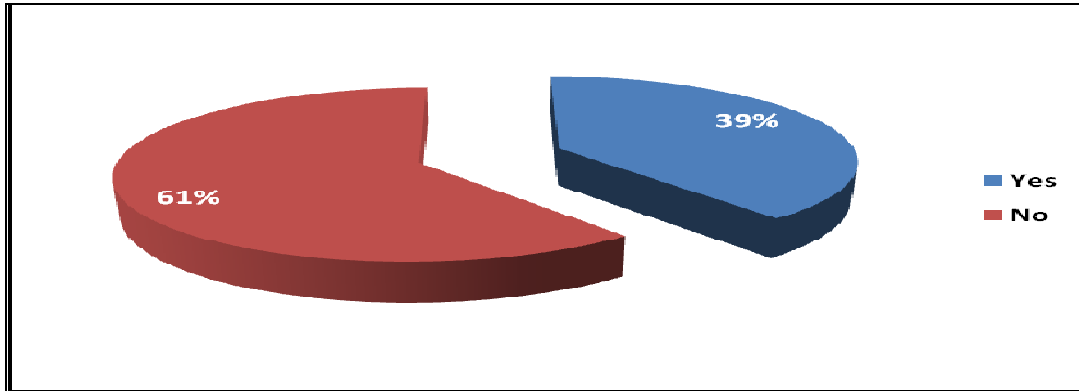
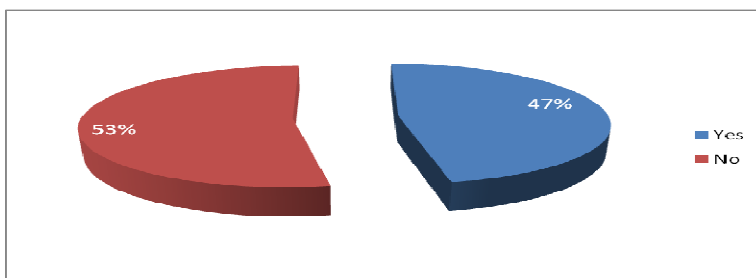


Figure 20B: Larger firms: auto-enrolment to await Government legislation to allow greater freedom of pension design



Overall, do you think the Government's review of auto-enrolment should recommend delay in its introduction?

Smaller firms are almost equally divided on whether the current review of auto-enrolment should delay its introduction, but with a small majority saying 'no' (a reverse of the majority position amongst larger firms). The process to date could hardly be described as rapid – from the Pensions Commissions reports, first recommending auto-enrolment, to full implementation will have exceeded a decade. Those opposing delay might argue that there will never be an ideal time to launch auto-enrolment, that staging and the phasing in of contributions should ease the pain for both employers and employees, and the importance of encouraging wider coverage of pension savings simply cannot be delayed any longer.

Set against this, those favouring delay may base this on the failure to date of Government to ease the legislation covering existing schemes and the concerns of levelling-down that remain. They may also feel the immediate period ahead of economic uncertainty is a bad time to place further costs on employees and business. As a result, auto-enrolment may get off to a bad start with high levels of opt-outs with many employees hard pressed financially and, rightly, concentrating on debt repayment.

Figure 21: Smaller firms - overall, should auto-enrolment be delayed?

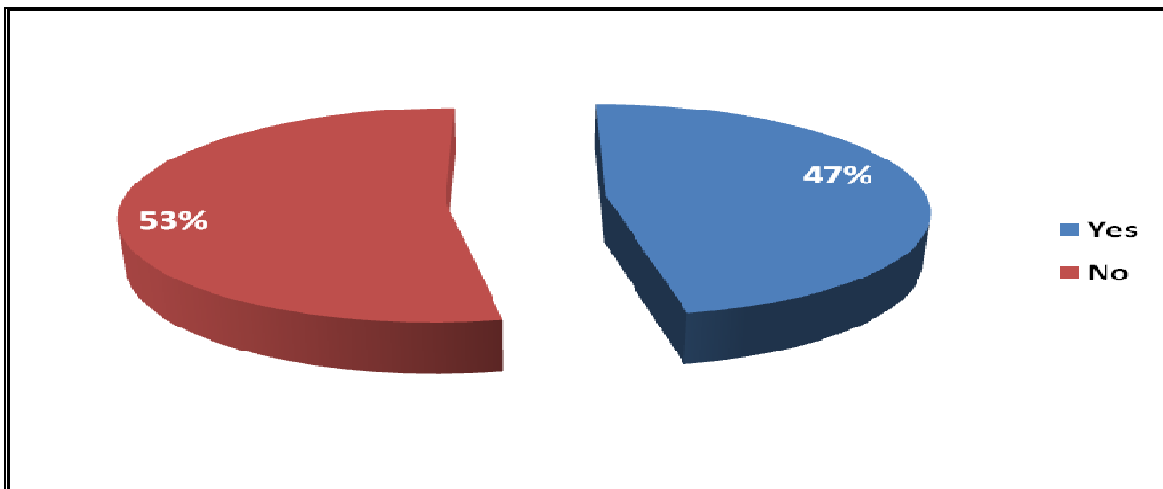
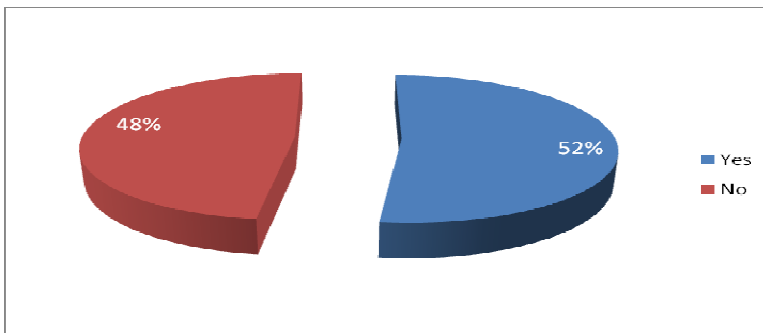


Figure 21B: Larger firms - overall, should auto-enrolment be delayed?

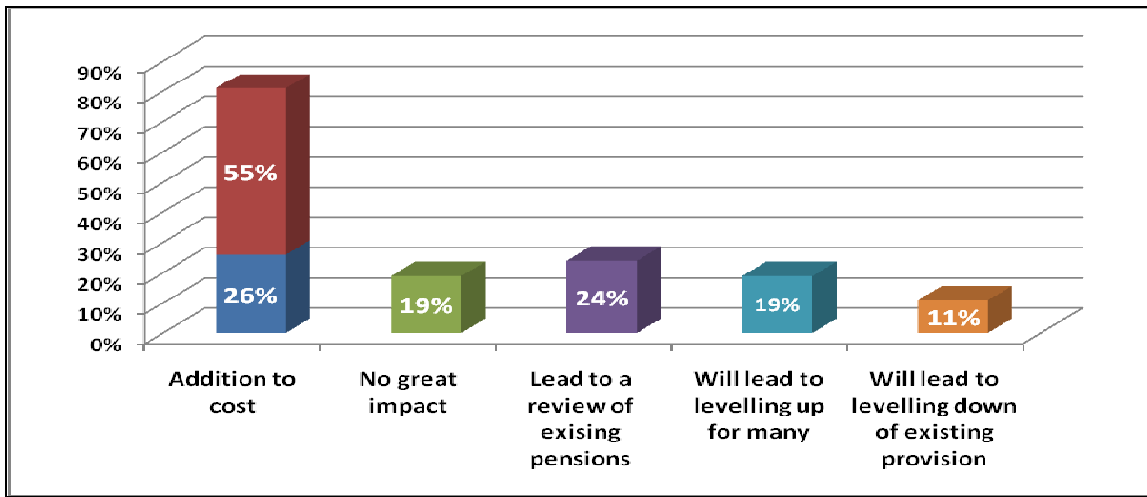


Overall, how do you think the introduction of auto-enrolment and NEST will affect your firm and workplace pension provision?

A quarter of smaller firms expect the introduction of auto-enrolment and NEST to lead onto a review of existing pension arrangements, with one in ten expecting levelling-down as a consequence. A fifth expect levelling up for many, which is perhaps surprisingly low as expectations seem to be that many more will be covered by pensions than previously, albeit this survey also forecasts opt-out rates of around 35%.

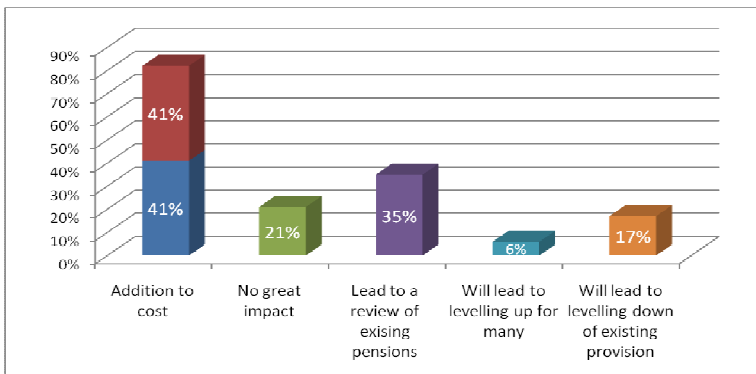
The most serious concern must be that 55% expect a 'significant' addition to business costs and 26% a 'marginal' one. Aside from the administrative costs involved in ensuring observance of the auto-enrolment regime as presently conceived, those smaller firms covered by this survey facing significant increases in costs will be those with nil or low existing levels of scheme participation, and where employee opt-out rates ultimately fall short of expectations and budgets.

Figure 22: Smaller firms: overall, how will auto-enrolment impact on your organisation?



Note: 'Addition to cost' - 26% say 'marginal' additional cost and 55% say 'significant' increase in cost.

Figure 22B: Larger firms: overall, how will auto-enrolment impact on your organisation?



Note: 'Addition to cost' - 41% say 'marginal' additional cost and 41% say 'significant' increase in cost.

Other survey findings

- 79% of smaller firms support the increase in State Pension Age to age 66 sooner than 2026.
- If the SPA is moved to age 66 in 2016, respondents then favour age 67 being implemented between 2020 and 2026 and age 68 between 2026 and 2036.
- 88% say the removal of the default retirement age will not lead to employers offering better pension schemes as a means to encourage employees to retire.

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For a copy of the Association's response to the review of auto-enrolment visit:
www.aca.org.uk (publications page – 13 August 2010)

Summary of new employer duties under Auto-enrolment and NEST

The Pensions Commission Reports in 2005 and 2006 pointed to significant under-saving for retirement, notably amongst low-to-moderate earners, with millions heavily reliant on inadequate State pensions. The then Government responded by flagging its intention to restore the indexation of State Pension to earnings growth alongside a number of other improvements (but with the State Pension Age gradually increasing in stages to 68 between 2024 and 2046). Additionally, to boost pension coverage and to take in up to 10 million new pension savers, the Government accepted the need for both a low-cost national scheme (now called NEST) for employees not offered access to an employer's scheme meeting certain minimum requirements and auto-enrolment into either NEST or an employer's scheme. The new Coalition Government has established a review of auto-enrolment, with the reviewers asked to report back to the Pensions Minister by 30 September 2010.

As things stand:

- a new employer duty is due to come into force from October 2012. From then, **auto-enrolment of all 'eligible jobholders'** (those aged 22 and below State Pension Age), with qualifying annual earnings between £5,034pa and £33,540pa, **into a 'qualifying workplace pension scheme' (QWPS) will begin as a statutory requirement** for the largest employers. These earnings figures will be up-dated for 2012, bringing the possible earnings band closer to between £6,000pa and £40,000pa.
- Medium sized and small employers will be required to auto-enrol their 'eligible jobholders' into a QWPS on a staged basis geared to PAYE references, such that all employers, including single employee firms, will be integrated by September 2016.
- 'Jobholders' aged over 16 and under 22 or over State Pension Age up to age 75 will be able to ask to be auto-enrolled into a QWPS if they fall within the updated earnings band above (and the employer must comply and pay the employer's contribution). If they have no qualifying annual earnings, they can enrol, but no employer contribution is required.
- All jobholders will have the right to 'opt out' (but eligible jobholders must be auto-enrolled first) and all eligible jobholders will be re-enrolled on a set date every 3 years, with a view to increasing scheme coverage over time.
- During the staging period up to September 2016 the total minimum pension contributions will be 2% of employee earnings, with a minimum of 1% from the employer. From October 2016 this will rise to 5% of employee earnings, with a minimum of 2% from the employer. From October 2017 contributions will be 8% of employee earnings, with a minimum of 3% coming from the employer (plus 4% from the employee and 1% by way of tax relief). Earnings include salary, wages, overtime, bonuses and commission, as well as statutory sick and maternity pay.
- Defined benefit and hybrid schemes will be exempt from staging – the duty to auto-enrol will instead be delayed until October 2016.
- Employers will be able to auto-enrol eligible jobholders into a firm's own existing (or new) QWPS, when this is certified as such by the Pensions Regulator, or otherwise must enrol them in the new National Employment Savings Trust (NEST), previously known as the 'personal accounts' scheme. A firm's own scheme will only be certified as a qualifying scheme if it reaches requirements that are at least equal to or better than NEST.
- NEST has been developed as a trust-based, defined contribution, portable, low-cost scheme (0.3% annual management charge plus 2% charge on each contribution until NEST set up costs are met), designed for the needs of low-to-moderate earners. Its investment approach will reflect the needs of these groups.
- NEST will only accept transfers in and out of the scheme in very limited circumstances.

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. Members of the ACA provide advice to thousands of pension schemes, including most of the country's largest schemes. Members are all qualified actuaries and all actuarial advice given is subject to the Actuaries' Code.

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September 2010