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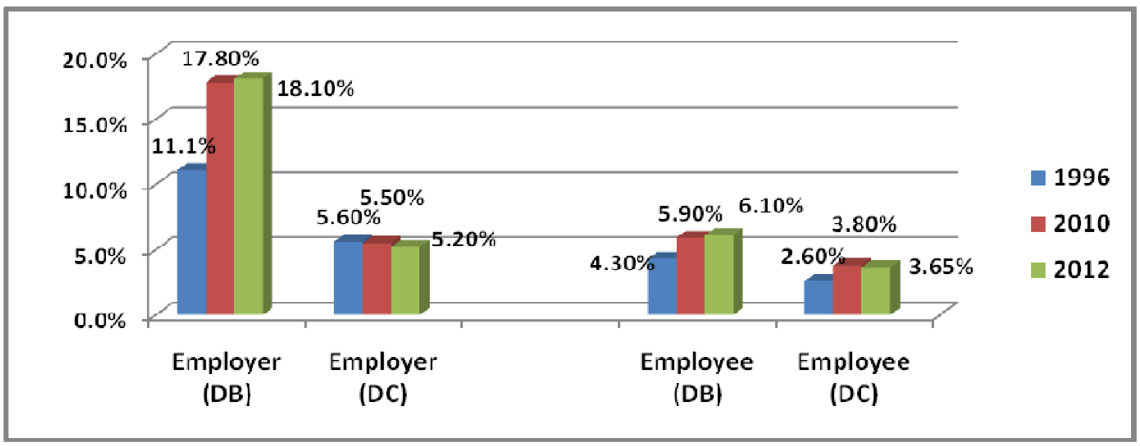
Key to engaging businesses and employees so they contribute more into pensions is financial incentives says ACA survey...

SURVEY FINDS PENSION CONTRIBUTIONS FLATLINING IN SMALLER FIRMS

2 January 2013 – A major survey of pension trends in smaller firms with 250 or fewer employees, to be published this month, has found contributions into smaller firms' pension arrangements – where these are present at all[1] – are flatlining. Average combined pension contributions by employers and employees into defined contribution schemes have remained static since the last survey in 2010 at 9% of earnings into trust-based schemes and just over 7½% into contract-based plans. This trend, given lengthening life spans and generally lower investment returns in recent years, is alarming in terms of the inadequate pension outcomes that will emerge in the years ahead.

Figure 1: Smaller firms – Comparison of trust-based employer and employee contributions (as a percentage of earnings) 1996 – 2010/2012



The final report of the ***ACA 2012 Smaller Firms' Pensions Survey*** conducted by the **Association of Consulting Actuaries (ACA)** has found:

- **Smaller firms believe financial incentives are the key to increasing both employer and employee pension contributions above existing levels. For employers, reduced employer's National Insurance contributions are seen as the most important way of**

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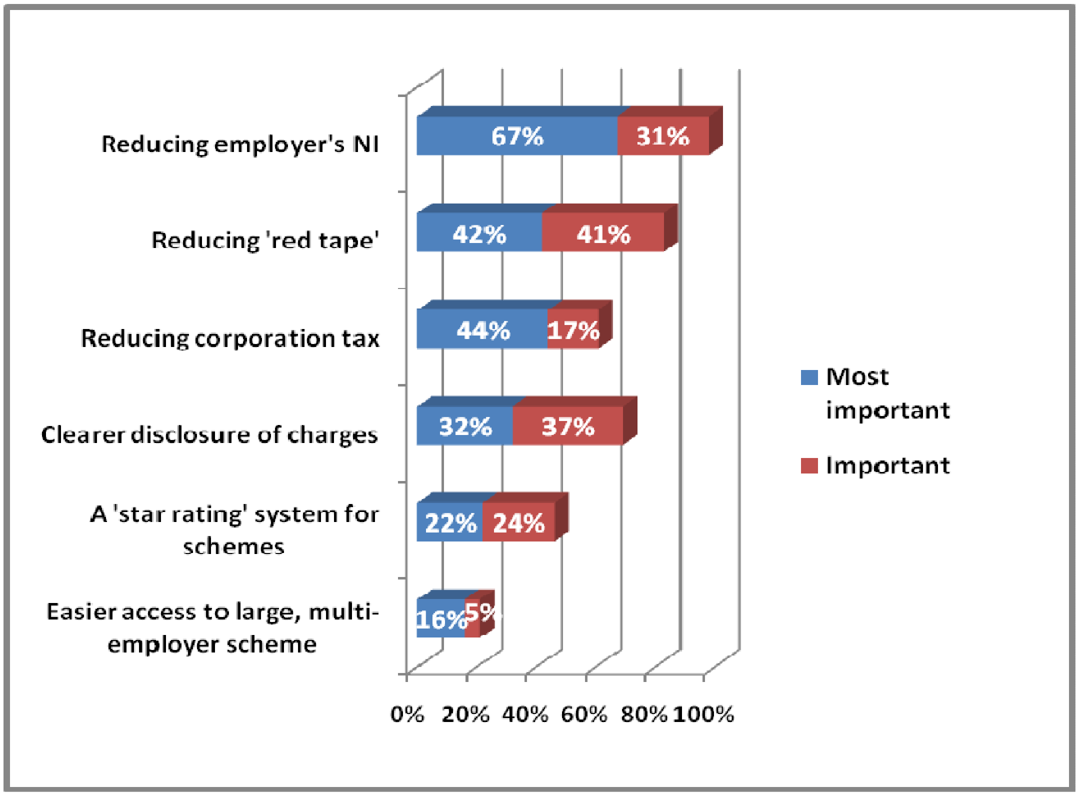
[1] Presently across the UK as a whole, around 75% of smaller firms (rising to 85% of those employing 5 or fewer employees) provide no workplace pension scheme.

enabling them to boost pension contributions, followed by less 'red tape', reduced corporation tax and a clearer disclosure of pension charges.

Figure 2: Smaller firms – What actions by Government (and others) would most encourage firms to increase their EMPLOYER contribution to any scheme offered now or in the future?

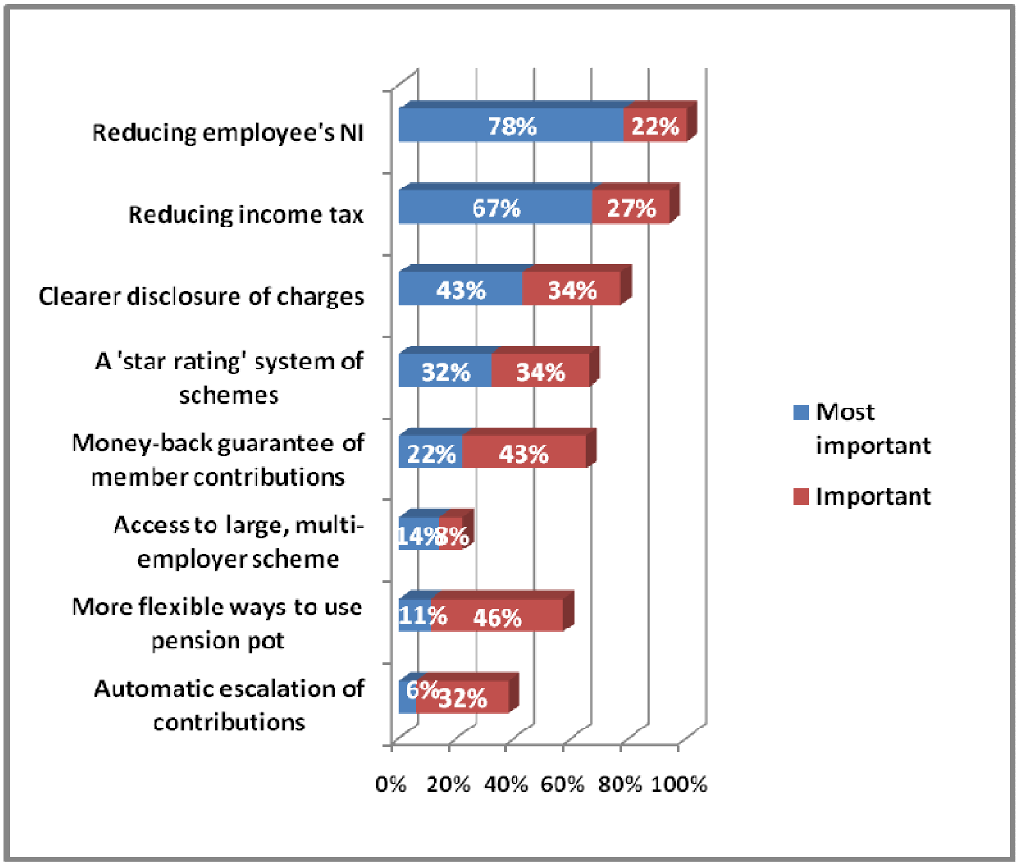


- **For employees to contribute more into their pensions, firms again felt reduced National Insurance and Income tax were key, followed by a clearer disclosure of charges. They also felt that a 'star rating' system for pension schemes covering charges, governance and transparency and a 'money-back guarantee' of members' contributions on retirement or death would help boost scheme membership, both initiatives championed recently by the Pensions Minister, Steve Webb (see *Figure 3*, next page).**

- **Where defined benefit schemes remain – 91% in the sector are closed to new entrants (43% of these to future accrual)[2] – this survey found the average ongoing funding level, expressed as a percentage of liabilities is 77% (as opposed to 82% two years ago). However, the survey – as in 2010 – found a general lengthening in estimated recovery periods, with two-thirds looking to ten years or more (compared to a third, two years ago), with an increasing number looking to recovery periods stretching beyond 20 years.**

[2] See *A million challenges ahead*, 2012 ACA Smaller Firms' Pension Survey, Report 1, 15 October 2012 at www.aca.org.uk (see 'Research' page)

Figure 3: Smaller firms – What actions by Government (and others) do firms think would encourage EMPLOYEES to increase their pension contributions?



The ACA says that the public are understandably unclear about the level of pension saving needed to achieve anything like a comfortable retirement income given the changes in the economy, particularly since 2008. Someone earning around current average earnings (£26,500 per annum) aged 30, expecting to retire at age 67 on two-thirds of their pre-retirement income (as recommended by the Pensions Commission) needs to save around 20% of 'band earnings'[3] or 16% of total earnings (inclusive of employer and employee contributions and tax relief) to hit this target income, also assuming a flat rate State pension of £140 per week, £7,280 per annum. If savings remain at 8% of band earnings, then retirement incomes could be closer to 45% of pre-retirement earnings (all figures expressed in today's terms)[4].

[3] Under the new auto-enrolment rules, from their staging date, employers and employees must pay pension contributions on 'band earnings' above £5,564pa up to £42,475pa provided the eligible jobholder earns above £8,105pa and decides not to opt-out (2012/2013 figures). By 1 October 2018, total minimum pension contributions will be 8% of band earnings (4% employee, 3% employer, 1% tax relief).

[4] **Please note:** The assumptions used are a male starting a pension at age 30 and retiring at age 67, no spouse's pension, estimated annual investment growth of 5%, annual management charge of 0.5%, assumed inflation of 2.5% pa compound throughout the investment period, 3% increase in pension per annum and a 5 year guarantee. No lump-sum taken. A single tier State Pension of £7,280 per annum (£140 per week) is also assumed. All values expressed in today's terms. All figures are a guide only. Pension funds and annuities purchased will depend on factors such as actual future pension fund returns, taxation, charges, inflation, annuity options chosen and annuity rates at retirement, all of which are subject to change and cannot be guaranteed.

The ACA survey has gathered responses from 344 smaller employers with 250 or fewer employees. There are over 1.2 million of these smaller firms which employ over half of the UK's private sector employees (59%) and generate a half of all private sector turnover (49%), amounting to £1,500 billion per year. They make up 99% of all private sector enterprises.

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

"At present, three-quarters of the UK's smaller firms offer no pension scheme at all, but by 2018 there should have been a 'sea change' in this situation, with all employers auto-enrolling their staff by then. Clearly, our economic path over the next 5 years will govern how many employees opt-out of pensions, but ahead of 2018 we need to be firmly addressing how we can get more people to save much more so they have a sufficient income in retirement.

"We hope the higher single-tier State pension reform will go ahead and provide a sustainable 'core' income in the years ahead, but on top of this we need to save much more than 8% of 'band earnings' for a comfortable retirement with less reliance on State support.

"I would like to see the Government and Opposition pledge to raise minimum pension contributions on band earnings to 10% by 2015 and 12% by 2020, but with pledges to cut national insurance, ear-marking reductions so they support extra private pension savings. If we do not increase these minimum contributions, then Government ambitions to hold down State welfare costs are unlikely to materialise – indeed, the pressure will be in the other direction."

The final report of the ACA *2012 Smaller Firms' Pensions Survey* final report will be published shortly. For a copy of the initial survey report see *A million challenges ahead*, published on 15 October 2012 go to www.aca.org.uk (see 'Research' page)

For further details:	Andrew Vaughan – general comment	020 7776 2200
	Steve Leake – general comment	01483 540 300
	David Robertson – survey results	020 3207 9380 (M: 07919 911380)

About the Association of Consulting Actuaries (ACA)

The **Association of Consulting Actuaries (ACA)** is the representative body for consulting actuaries, whilst the Institute and Faculty of Actuaries is the professional body. The ACA has 1,750 members working in around 75 firms. ACA Members are all qualified actuaries and all actuarial advice given by members is subject to the Actuaries' Code. The ACA forms the largest national grouping of consulting actuaries in the world.