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From diagnosis to action: shaping the next phase of pensions reform

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Economic and Social Research Council

Introduction

- The Second Pensions Commission's interim report set out a broad diagnosis of the challenges facing the UK pension system
- Next step: moving from diagnosis to policy action
- Today:
  - Discuss recent IFS research in this context
  - A focus on the trade-offs involved in designing reform

Two key issues for consideration

- How could the Commission approach changing automatic enrolment contributions?

- What are the key priorities for pensions access?

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How could the Commission approach changing automatic enrolment contributions?

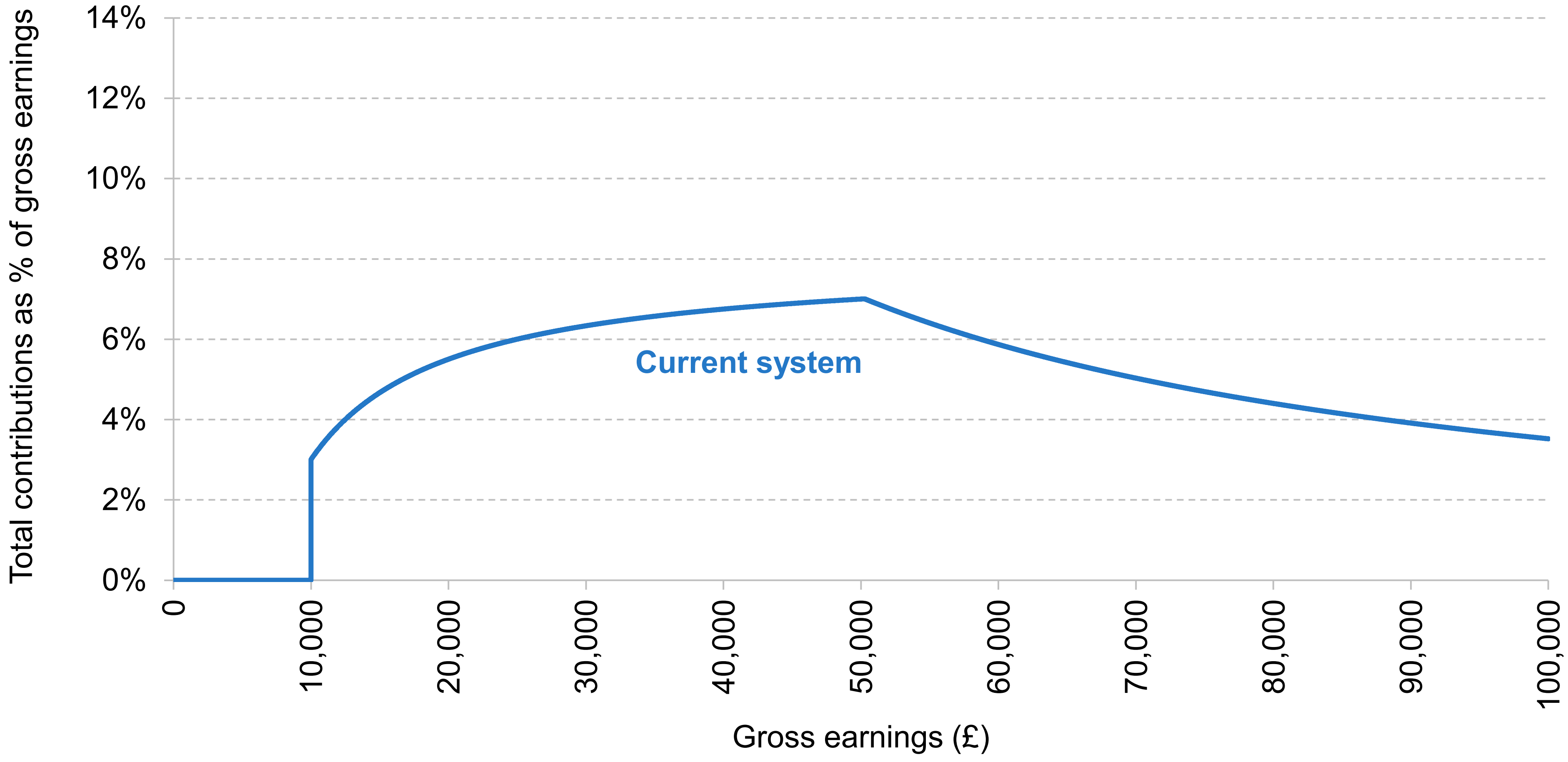
Commission worry about low pension saving

- Key focus for Commissions interim report: DWP project 43% of working-age population are on course for inadequate income in retirement
- A third of eligible employees saving at the minimum default contribution rates
- Almost half of working-age people are not saving into a pension
  - About of half of those not saving are in paid work – either opted out or not eligible (including the self-employed)
- → We want consider policies to increase saving rates among these groups, focusing on changes to automatic enrolment parameters

Modelled scenarios

	Age range	Earnings trigger	Qualifying earnings range	Employer contribution rate	Total contribution rate
Current system	22 to SPA	£10,000	£6,240 to £50,270	3%	8%

Minimum total contribution rate as percentage of total earnings



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Scenario C: Increase contributions to 12%	18 to SPA	£10,000	£6,240 to £65,000	6%	12%

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Scenario C: Increase contributions to 12%	18 to SPA	£10,000	£6,240 to £65,000	6%	12%
Scenario D: Increase contributions from first pound	18 to SPA	£4,000	£0 to £65,000	6%	12%

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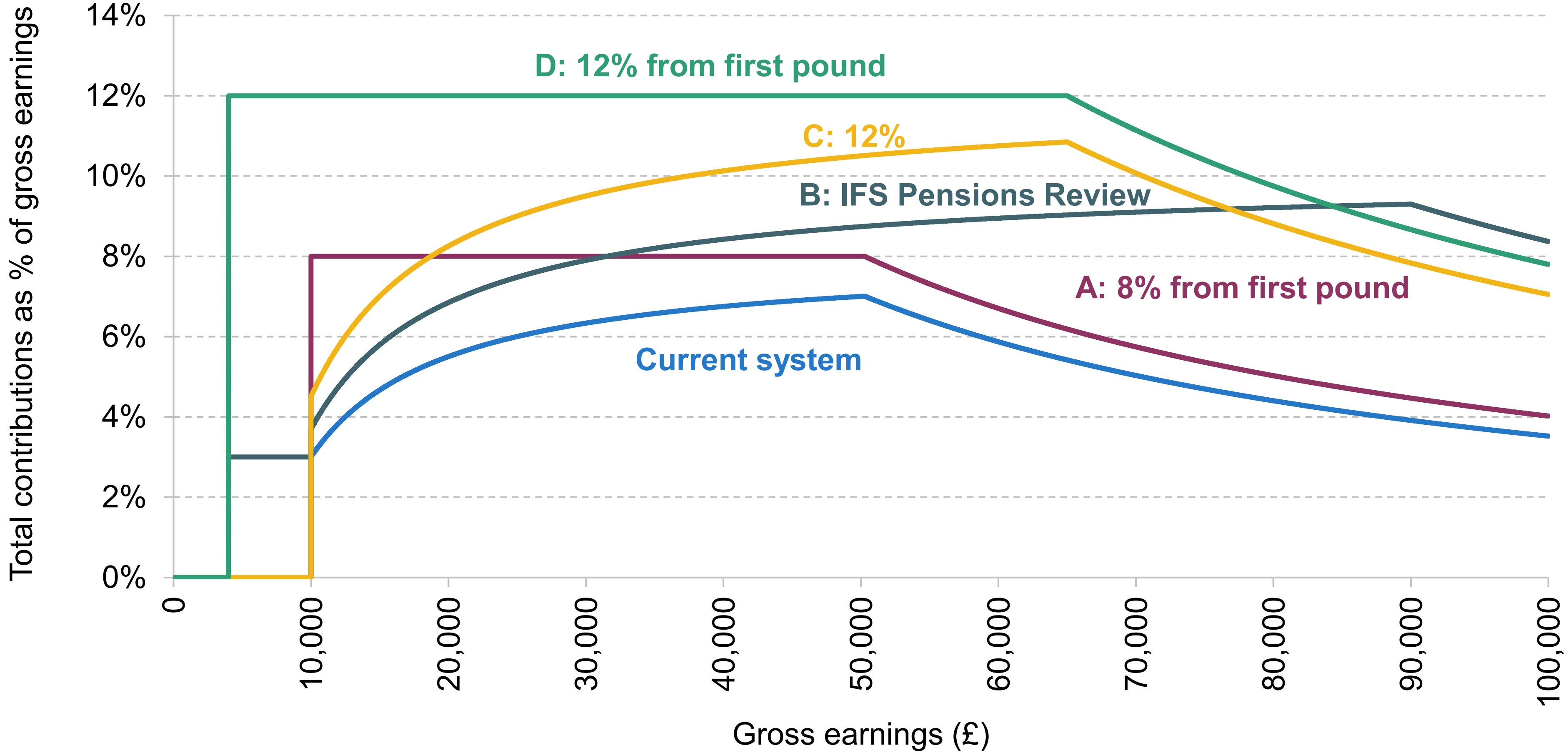
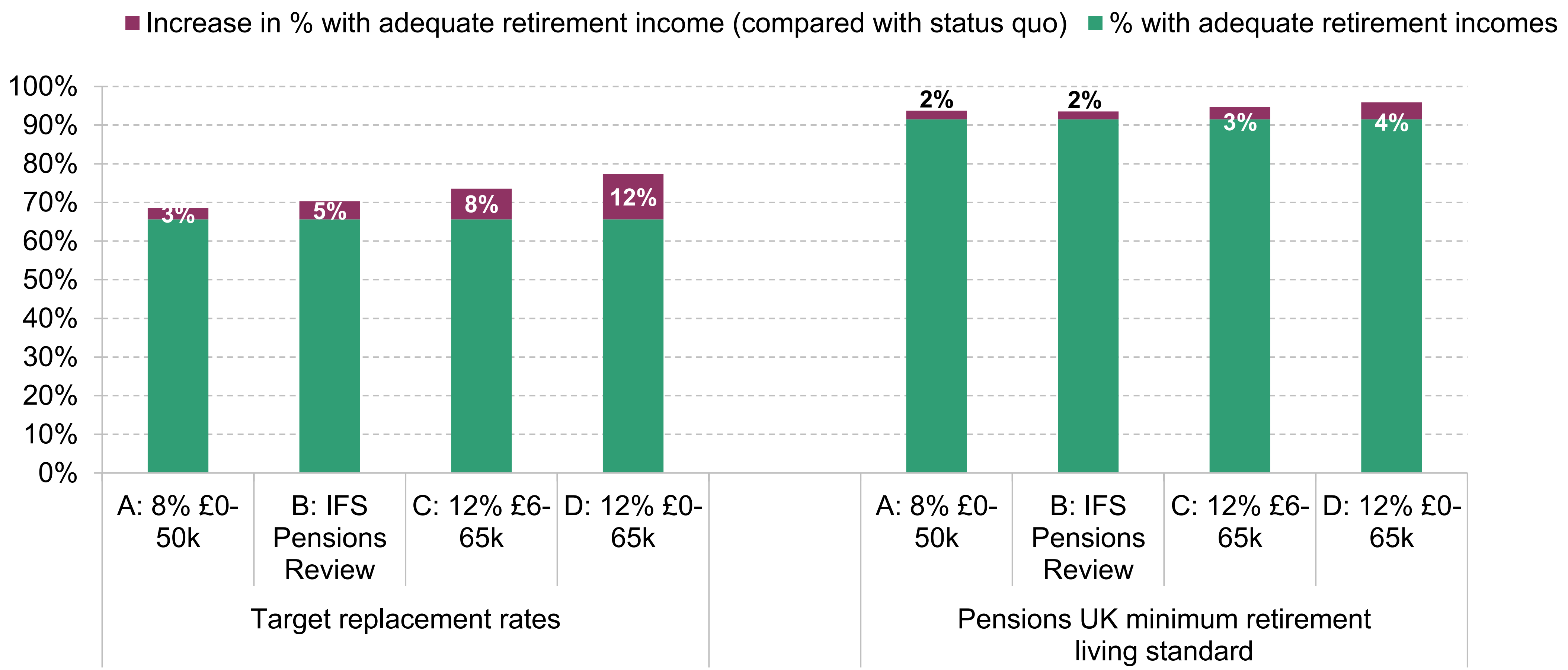


The effect of policy scenarios on adequacy measures

Private sector DC savers 25-59, individual level



Note: The sample contains 25- to 59-year-old private sector employees saving into a DC pension in Round 7 of the Wealth and Assets Survey. Individual level.

Adequacy by income thirds

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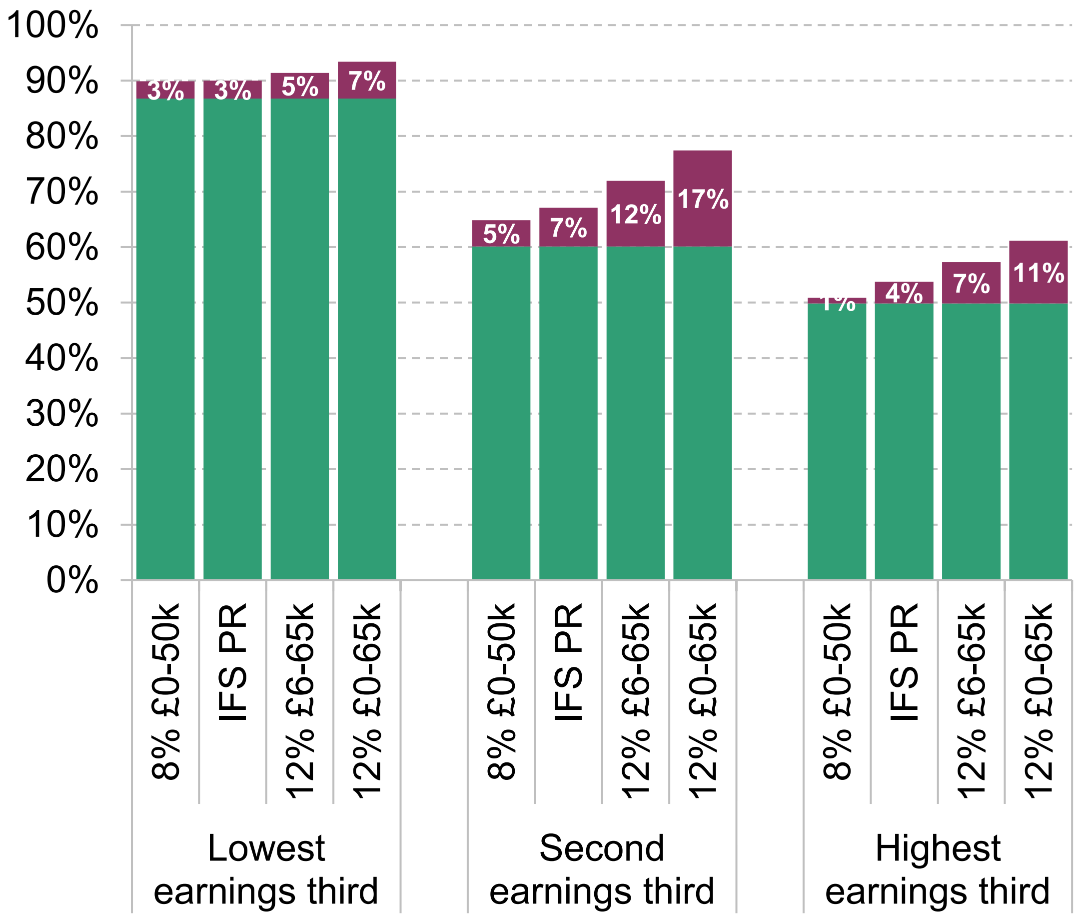
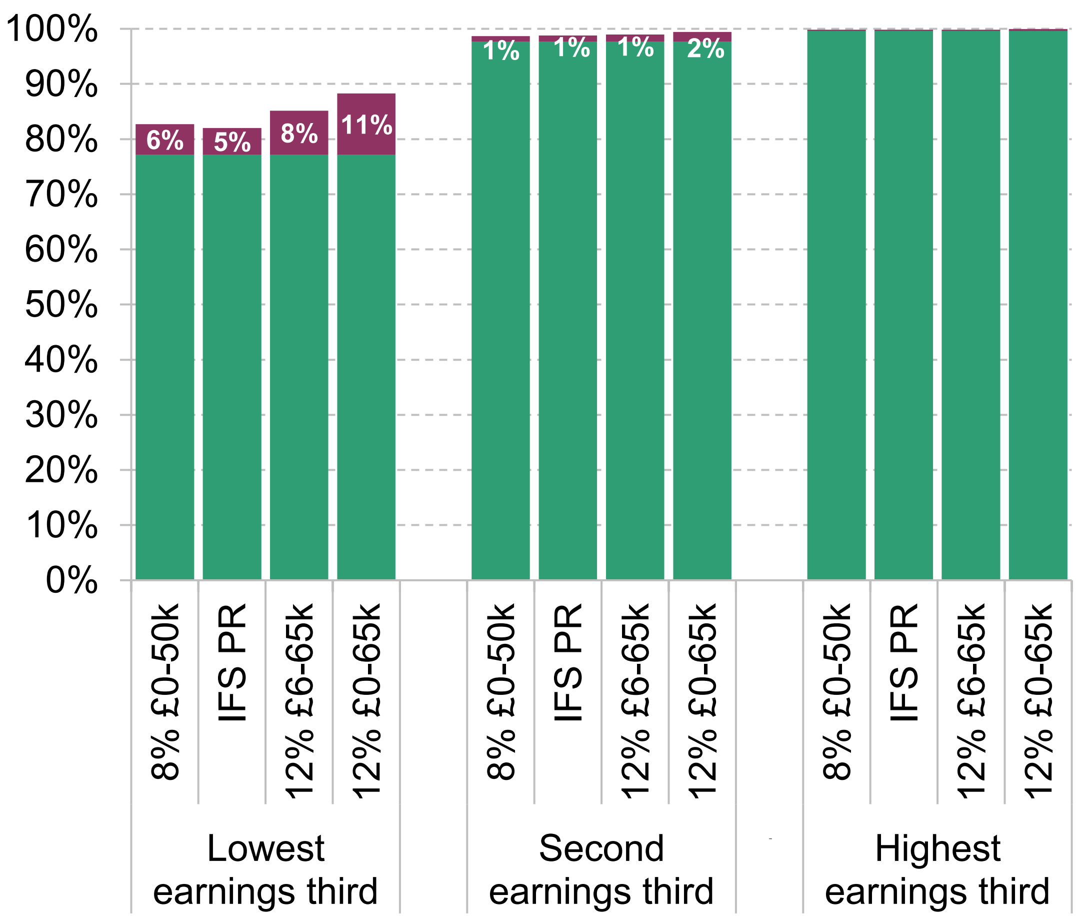
Effect of automatic enrolment proposals on the percentage of people projected to have an adequate retirement income, by earnings group

Target replacement rate



Pensions UK minimum standard



Note: The sample contains 25- to 59-year-old private sector employees saving into a DC pension in Round 7 of the Wealth and Assets Survey. Individual level. Average TRRs across the groups: 74%, 67%, 57%.

Illustrative hybrid measure

- The two adequacy measures give different answers in terms of who policy should focus on

- We have used an illustrative hybrid measure where an adequate retirement income is defined as:
  - At least Pensions UK Minimum retirement living standard (RLS)
  - Reaching target replacement rate for those with income between the Pensions UK Minimum and Moderate RLS
  - Moderate RLS for those with income at or above it, regardless of replacement rate

An illustrative hybrid measure

Increase in the percentage of people projected to have adequate retirement income, by earnings group, hybrid adequacy measure

Note: The sample contains 25- to 59-year-old private sector employees saving into a DC pension in Round 7 of the Wealth and Assets Survey. Individual level. Average TRRs across the groups: 74%, 67%, 57%.

Aggregate impact of scenarios

	Total additional contributions (£bn)	Additional employer contributions (£bn)	Additional employee contributions (£bn)	Tax relief (£bn)	Long-run tax relief (£bn)
A: 8% of £0-50k (earnings trigger £10k)	2.8	0.9	1.9		
B: IFS Pensions Review (earnings trigger £4k)	7.1	3.4	3.7		
C: 12% of £6-65k (earnings trigger £10k)	9.0	6.1	2.9		
D: 12% of £0-65k (earnings trigger £4k)	17.0	9.8	7.2		

Source: Authors' calculations using Annual Survey of Hours and Earnings.

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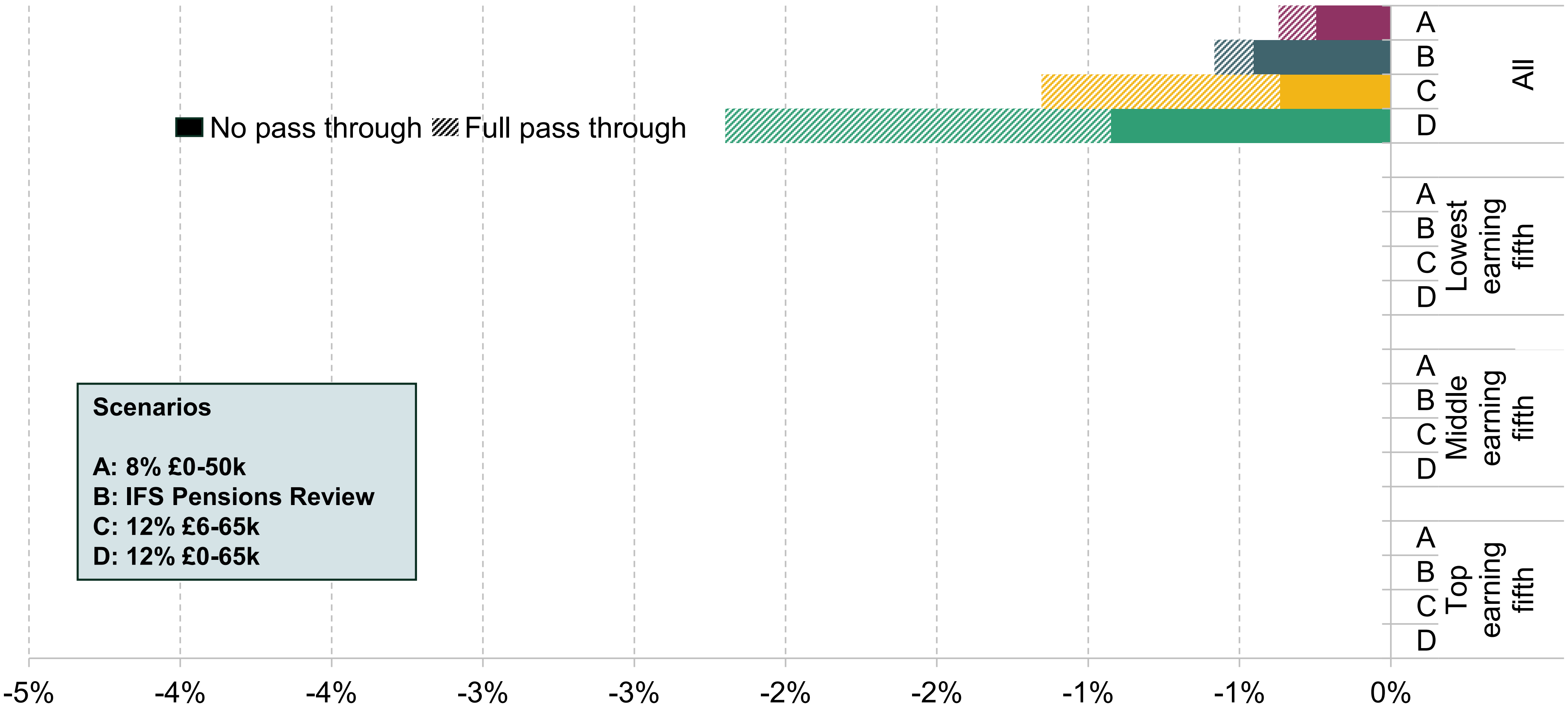
C: 12% of £6-65k (earnings trigger £10k)	9.0	6.1	2.9	3.6	2.2
D: 12% of £0-65k (earnings trigger £4k)	17.0	9.8	7.2	6.1	3.6

Source: Authors' calculations using Annual Survey of Hours and Earnings.

Effect on take-home pay

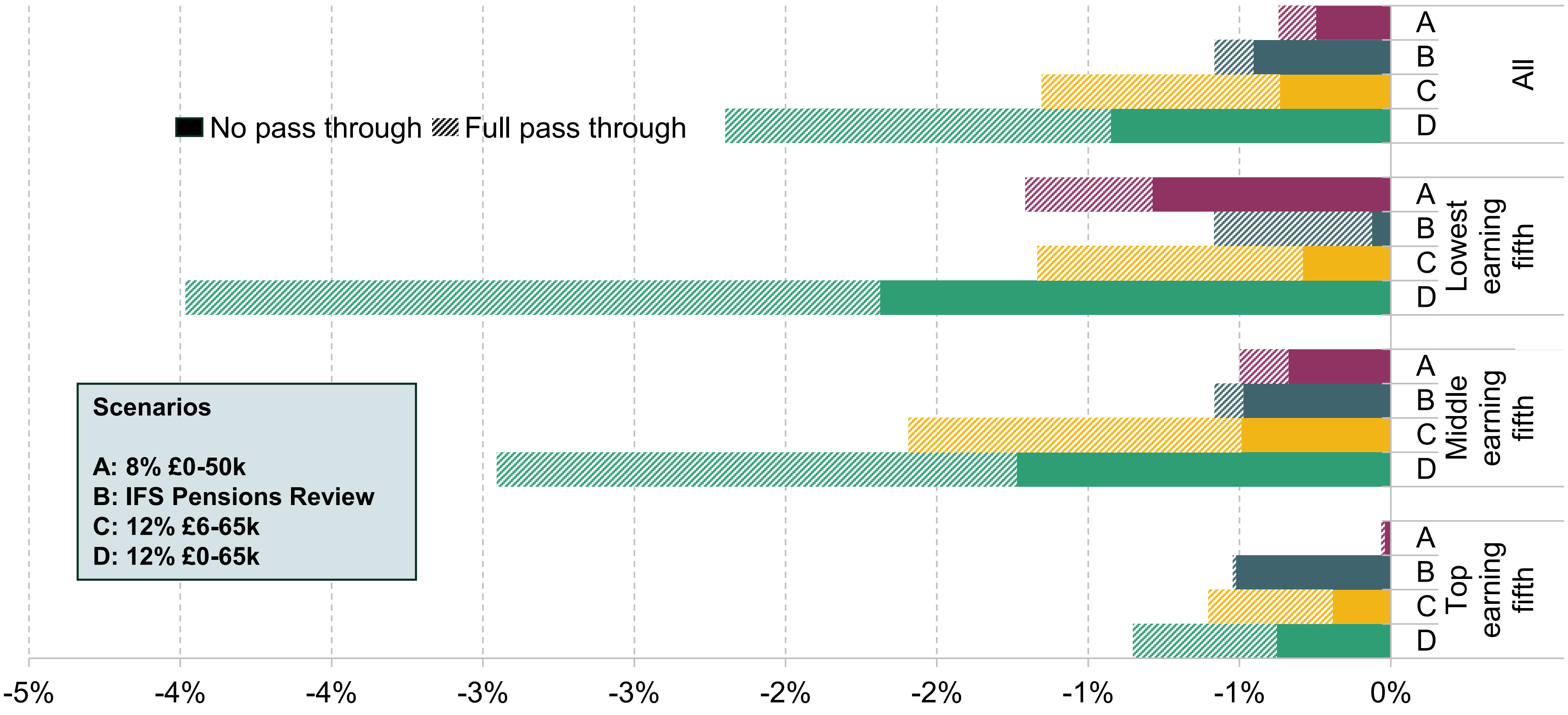
With and without pass-through of employer contributions to wages



Note: Modelled percentage change in take-home pay from different scenarios (A to D), for the top, middle and bottom quintile of the take-home pay distribution, with and without pass through of higher employer contributions onto pay. Authors' calculations using Annual Survey of Hours and Earnings. Among all private sector workers aged 25-59 saving in a DC pension.

Effect on take-home pay

With and without pass-through of employer contributions to wages



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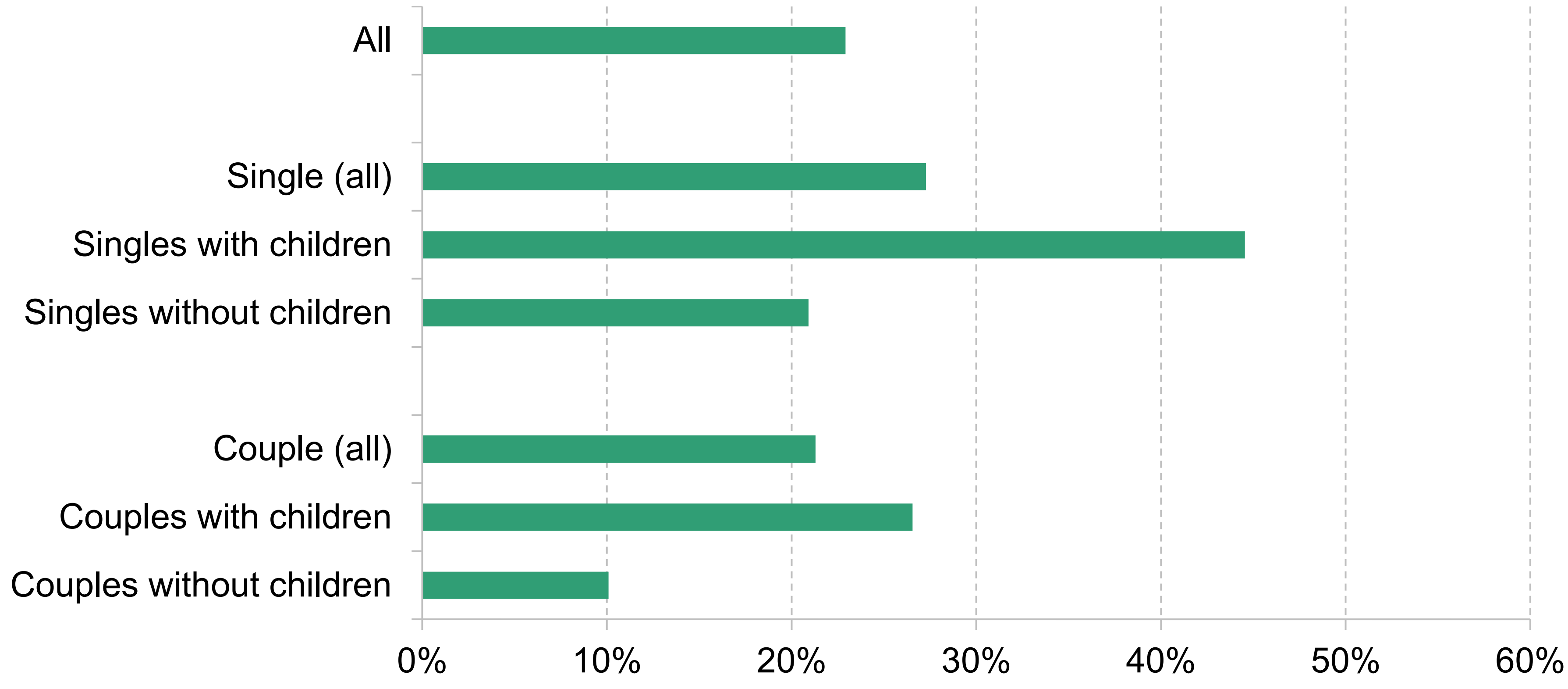
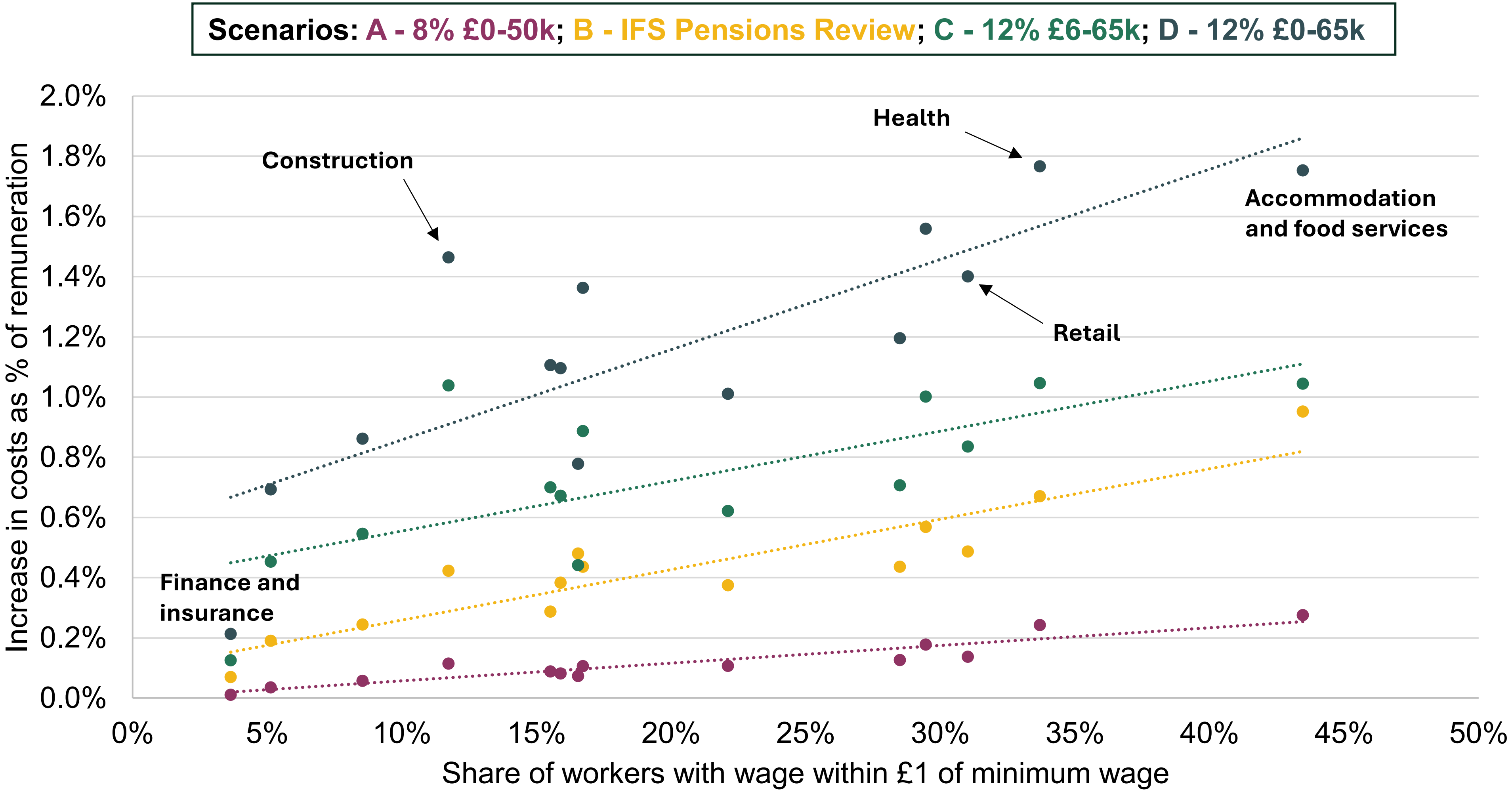
Many working-age people not reaching the minimum living standard

Share of people in working households with income net of housing costs below the minimum Pensions UK retirement living standards, 2026



Note: Single/couple households with children have their income equivalised to the level of a single/couple household without children before being compared with the PLSA standards. Equivalisation uses the OECD modified scale. Working-age households with someone in paid work are included. Source: Authors' calculations using the Family Resources Survey, 2024–25 , uprated to May 2026.

Costs rise more for industries with more minimum wage workers



Source: Authors' calculations using Annual Survey of Hours and Earnings 2024. Among all private sector workers not saving in a defined benefit pension.

What are the key priorities for pensions access?

Employment rate falls gradually with age

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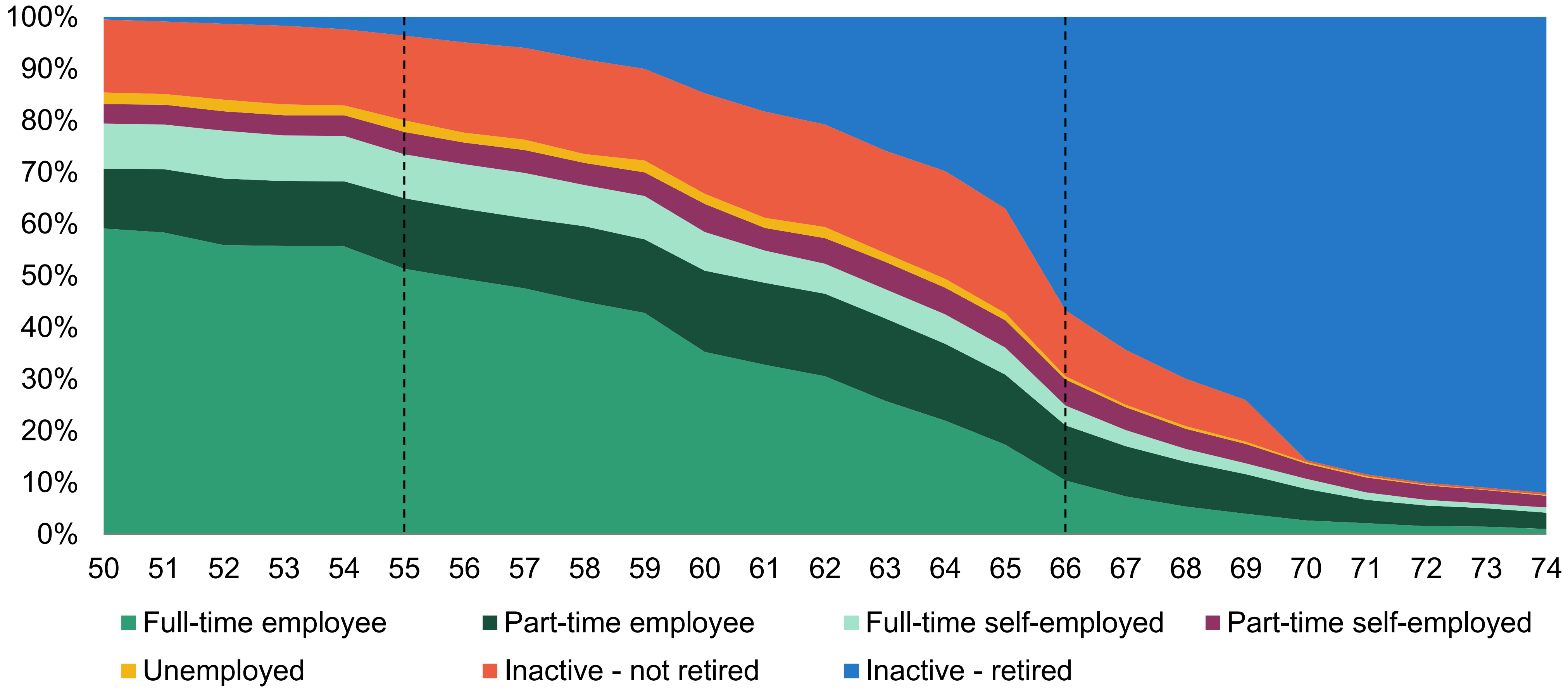
Proportion of population in paid work, retired, and out of work by age, 2021–2025



Note: Economically inactive people aged 70+ are considered retired. The vertical lines indicate age 55 (age from which people can access their private pensions) and age 66 (state pension age over the period in question).

Source: Authors' calculations using the Labour Force Survey 2021Q4 to 2025Q3.

Decumulation decisions are still relatively low stakes for most

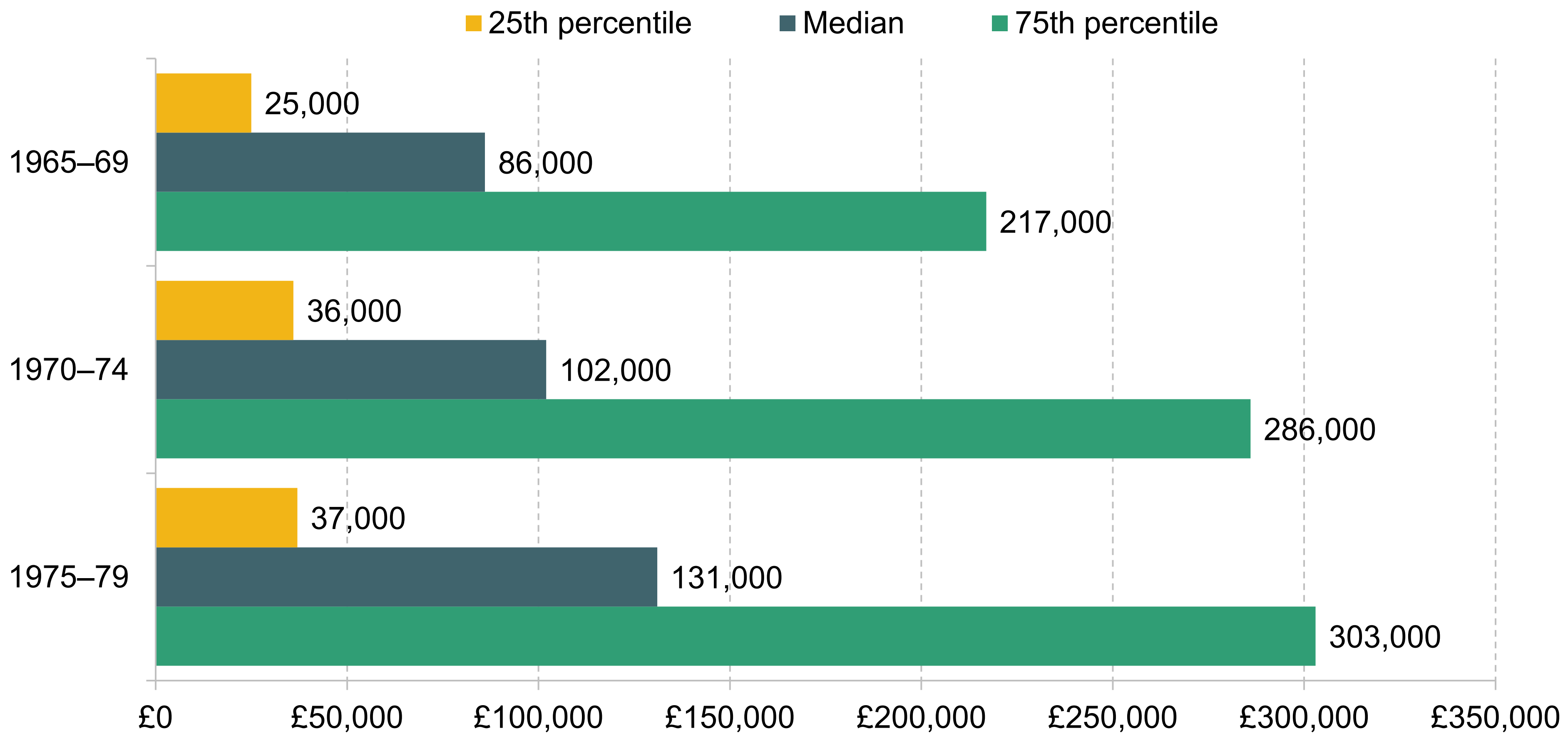
Share of 55- to 64-year-olds with different levels of pension wealth in 2018–20

		Defined benefit wealth			
		None	£1–£50,000	£50,000–£100,000	£100,000+
Defined contribution wealth	None	18%	4%	3%	19%
	£1–£50,000	21%	2%	1%	6%
	£50,000–£100,000	5%	0%	0%	3%
	£100,000+	12%	1%	1%	4%

Note: Percentages are from the Wealth and Assets Survey (WAS), adjusted using a scaling factor from the English Longitudinal Study of Ageing.
Source: Authors' calculations using the Wealth and Assets Survey, Round 7 (2018–20), and the English Longitudinal Study of Ageing, Wave 9 (2018–19).

DC wealth slowly becoming more important

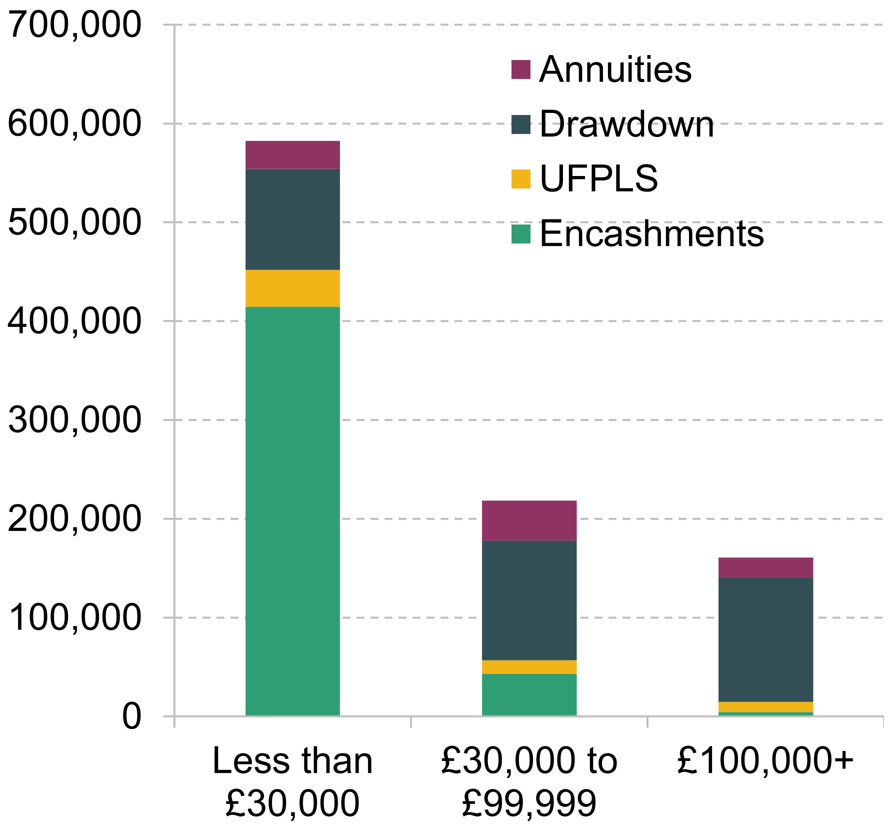
Projected 25th percentile, median and 75th percentile DC pension wealth at retirement among those with some DC wealth, by birth cohort



Source: Authors' calculations based on projections using the Wealth and Assets Survey, 2018–20. Figure 2.3. of Boileau et al., 2025.

Larger pots are drawn differently

Method of pensions accessed for the first time, by pot size

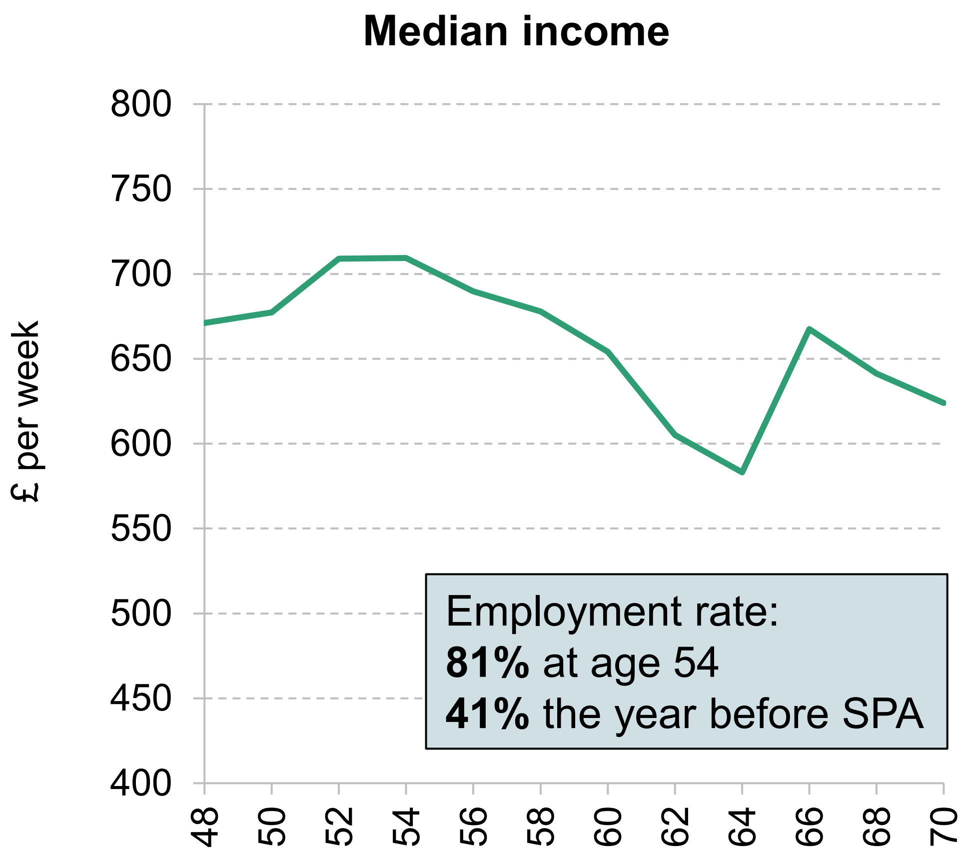


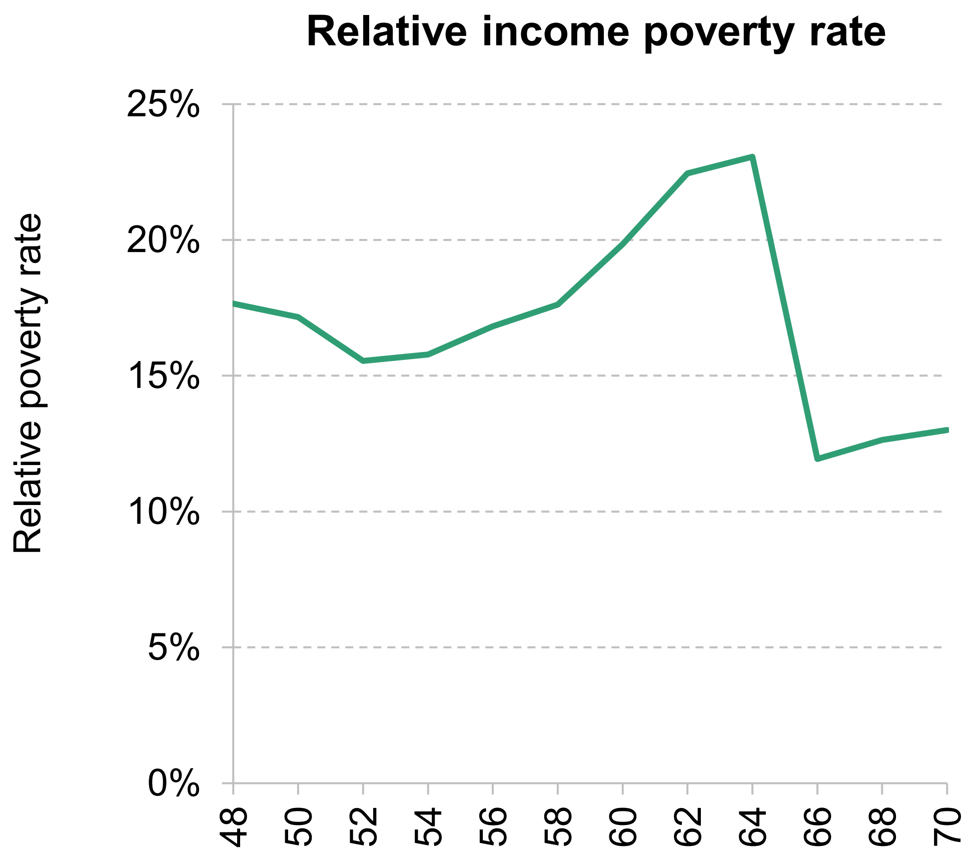
Regular withdrawal rates, by pot size

Source: Authors' calculations using FCA Retirement income market data 2024–25.

Early 60s can be a period of particularly low incomes

Relative income poverty rate and median equivalised net household income (after housing costs), by age





Source: Authors' calculations using FRS 2021 to 2024.

What are the key questions for the Commission?

Key trade-offs to consider for increasing pension contributions

- There is no one size fits all answer to how much people should save into private pensions
  - More saving will come at the cost of lower take-home pay today – question on whether this is the right group to focus on?
  - Different structures could help with targeting, but increase complexity
- What should the qualifying earnings band be?
  - 12% of ‘what’ makes a huge difference for saving and take-home pay
- How to mitigate higher costs for employers? Just phasing, or some other ‘sweeteners’?

What are the key priorities for pensions access?

- Policy and regulation on decumulation already moving ahead
  - To what extent should this be a key priority for the Commission?
- Would current or new reforms prevent/discourage ‘bridging’ to SPA?
  - Potentially important for lower-income people facing less generous working-age benefit system

Overall considerations

- The success of the first Commission was based on wide-spread consensus building
  - Policy certainty and stability important
- Difference this time: tougher political and public finance backdrop, shorter timeline
- Key goal should be to ensure policies are credible and sustainable for the future
  - → Achieving consensus within the timeframes of the Commission may mean avoiding more controversial and complex reforms
- Commission's policy choices should be guided by clear priorities and objectives – can help justify the trade-offs

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