Summary
- A dramatic shift in the pensions market has been witnessed over the past 10 years as DC scheme membership skyrocketed.
- AE has helped increase workplace pension participation by more than 10 million people.
- However, questions have been asked about the adequacy of AE saving levels and the exclusion of certain groups.
- Industry experts hope that the changes recommended in the 2017 AE Review will be implemented by the mid-2020s.

A decade of auto-enrolment

October 2022 marks 10 years since the introduction of auto-enrolment in the UK. Jack Gray looks at how the marketplace has changed, whether the policy has met its aims and how it may evolve over the next 10 years

The pensions industry saw arguably its largest shake-up in decades when auto-enrolment (AE) was introduced in October 2012. Looking back on 10 years of the policy in action, it seems like it was a huge success, with over 10 million more people saving into a workplace pension.

It has certainly achieved its primary objective: To get more people saving for retirement. Opt-out rates were lower than expected and people are generally on a better path to retirement than they would have been without the policy, as the prevalence of defined benefit (DB) pensions continues to decline.

However, it may not be that simple. These past 10 years also highlighted the shortcomings of the policy, with fears that people relying solely on AE defined contribution (DC) pensions will not have enough savings for an adequate retirement. Additionally, due to the earnings and age thresholds, and employment type requirements, groups such as women and the self-employed are being disproportionately left out.

Industry experts have long been calling for reform to the policy to address these gaps. The 2017 AE Review recommended that the minimum age threshold should be lowered from 22 to 18 and the lower earnings limit should be removed. The government has previously promised that this will happen by the mid-2020s, but there appears to have been a lack of progress on this front.

Changing marketplace

In the past 10 years, the pensions marketplace has changed dramatically, says Aegon head of pensions, Kate Smith, noting that we are seeing the accelerated decline of DB schemes, the demise of single employer trust-based schemes and the acceleration of master trusts.

"Since 2012, the marketplace has changed significantly," adds LCP partner, Lydia Fearn. "We have seen a tenfold increase in membership of DC schemes, with over 10 million people actively contributing into their own DC savings.

"The past 10 years have shown that people are taking more notice and more interest in their DC pension savings."

Janus Henderson director of institutional DC, Dave Whitehair, states that the most obvious change is the growth in membership and assets under management. "New providers have entered the DC pensions market with an aim of disrupting the legacy providers and building technology-led solutions," he continues. "Consolidation has given rise to larger pools of assets and enabled investment decision makers to consider allocations to new investment areas

such as private assets and thematic sustainable investments."

B&CE, provider of The People's Pension, director of policy, Phil Brown, comments that while Nest was a necessary intervention, the AE market is healthy and competitive, and it is possible to deliver a quality product to small and micro employers.

However, not all of the changes have been positive, with PLSA director of policy and advocacy, Nigel Peaple, describing two changes that impacted future pension adequacy: "The first is the shrinking proportion of savers who will enjoy the comparatively high and guaranteed income provided by DB funds," he says.

"The second is declining home ownership. The number of households owning their property peaked at 70.9 per cent in 2003, falling to 63.9 per cent in 2018. If this trend continues, it could have grave implications for people's standard of living in retirement."

Meeting its aims

AE had one primary aim at its outset: Get more people saving for retirement. Its clear that the policy has achieved, if not exceeded, this target, with over 10 million more people enrolled.

"There is no doubt that, since its inception 10 years ago, AE has revolutionised long-term saving for millions," says Standard Life workplace managing director, Gail Izat.

"It has embedded a savings culture in UK workplaces, and normalised pension participation. In April 2021, the UK workplace pension participation rate was 79 per cent, up from 47 per cent in 2012."

Peaple adds: "In the 10 years since AE was first introduced the unprecedented success of this policy has become clear. Every year the number of people saving for a pension has increased.

"Opt-out rates remain lower than expected when the policy was originally introduced, and evidence suggests that people highly value pension savings and will continue to save in large numbers despite significant economic shocks. Moreover, continued support for the policy is widespread."

Not only has the policy met its initial aims, it has arguably exceeded expectations, notes Brown. He draws a comparison with the roll-out of the minimum wage, with both policies having low non-compliance and becoming part of the UK's labour market framework.

"Most of the flaws in AE are, like the gender and ethnicity pensions gaps, a product of wider labour market inequalities, or, like the adequacy issue, the result of deliberate decisions taken at the outset," he adds.

Smith states that while it is good that participation is high, AE is a "double-edged sword": "It has got participation up but unfortunately people aren't saving enough and they're not aware enough of what is going on; it just happens to them. So, when they come up to retirement and they have difficult decisions to make, that just causes problems."

"There is no doubt that, since its inception 10 years ago, AE has revolutionised long-term saving for millions"

In hindsight

Despite the successes of AE, issues have arisen that, with the benefit of hindsight, could have been considered and addressed earlier. The spotlight has been shone on aspects of the policy, such as the minimum age threshold, earnings trigger and contribution level, that could lead to problems as people approach retirement with purely DC savings build up through AE.

"The success of the AE policy has magnified some of its shortcomings, with too many people falling short on reasonable definitions of pensions adequacy," explains Peaple.

"This is even more acute for recognised under-pensioned groups, like the self-employed, part-timers, multiple job holders, gig workers, women, single mothers, those responsible for others' care and people from ethnic minority backgrounds.

"There are also very different outcomes across generations, largely driven by how much DB provision different demographics have."

Smith adds that a lot of regulations

have been added over the past decade: "I never understood why AE contributions had to be paid based on a band of earnings," she states.

"The way it was communicated was not effective because people think they are paying 8 per cent, when they are paying less than that. That could have been done better. They should have brought things in earlier, like the charge cap and default funds, and we should have had some sort of small pot solution from day."

Fearn notes that, despite the successes, improvements could have included a simpler earnings test, and including the self-employed and younger people in the policy.

"There is still time to take action and the government has made commitments that it will happen at some point," she continues. "However, we need these changes to happen as soon as possible."

These commitments include enacting the 2017 AE Review's recommendations: Lowering the minimum age threshold from 22 to 18 and removing the lower earnings limit. The government has repeatedly claimed these will be changed in the mid-2020s, but many in the industry are unconvinced that progress is on track. Smith states that "we need to get a plan" for implementing the recommendations, preferably to be phased in over time.

"There are several areas that need attention," says Whitehair. "Firstly, it is widely accepted that contribution rates which drive so much of the expected retirement outcomes are not high enough. There are also cohorts of people where participation in pensions remain very low.

"The part-time who do not reach the lower earnings limit and the self-employed remain another group missed out by the current policy."

The next decade

Although AE has spearheaded positive engagement, there is still more to be done, according to Izat. "The well documented rise of the gig economy and the move away from traditional employment towards more flexible ways of working presents opportunities for the future development of AE structures," she says, calling for minimum contributions to be raised to 12 per cent alongside the 2017 AE Review recommendations.

"Recognising that policy interventions must balance the current cost-of-living crisis with preventing millions of people falling short in retirement over the coming decades, a timeline must be introduced to increase minimum AE contributions," adds Peaple.

"But we are not proposing any changes to contributions before the mid-2020s. We believe that 12 per cent should become the new default contribution level, and that this should be introduced on a gradual basis over the next decade."

Smith states that she would like to see a movement from enrolment into engagement, and for employers from compliance into engagement: "We need to be able to nudge people into making active decisions and allow providers to give more personalised communications and guidance."

Brown concludes: "There is a need for a new consensus on what AE is there to actually do. Currently, it's providing roughly half what's needed for an adequate income on top of a full state pension. There's a need for a new consensus over whether that's appropriate and, if not, what should be done about it. We see setting formal objectives for the UK pension system as critical so that people know what to expect from AE minimum contributions."

Written by Jack Gray