

## PPI Response “Review of automatic enrolment - initial questions”

### About the PPI

1. The Pensions Policy Institute (PPI) is an educational research charity, which provides non-political, independent comment and analysis on policy on pensions and retirement income provision in the UK. Its aim is to improve the information and understanding about pensions policy and retirement income provision through research and analysis, discussion and publication. Further information on the PPI is available on our website [www.pensionspolicyinstitute.org.uk](http://www.pensionspolicyinstitute.org.uk).
2. This response uses key evidence from PPI research to address relevant questions. Questions which have no related PPI evidence are not included in the response.
3. The PPI is currently undergoing research projects which are relevant to this enquiry and these are highlighted throughout the response.

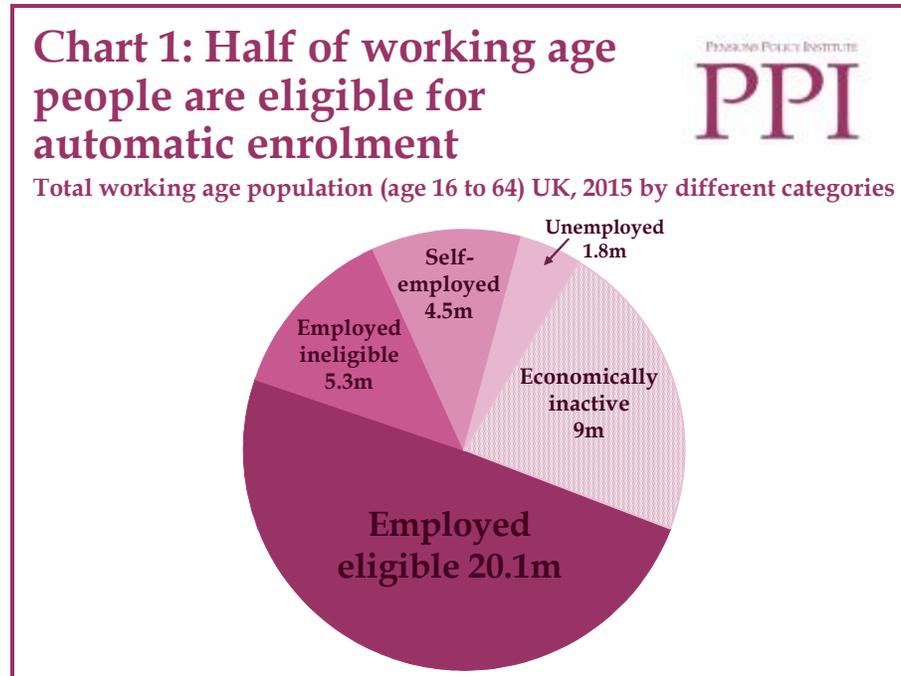
### Questions

#### **Theme 1 - Coverage:**

4. Do the earnings trigger (£10,000 in 2017/18) and age criteria (22 to SPA) continue to bring the right people into automatic enrolment?
  - a. Is there a case for bringing individuals not currently eligible for automatic enrolment into scope, and on what grounds?
    - 4.1 Analysis of the employed population from the Labour Force Survey identifies how people would be affected by the removal of the earnings trigger and earnings band on contributions.
      - 3.3 million individuals would become eligible for automatic enrolment if the earnings trigger was removed.
      - 77% of employees earning less than the earnings trigger are women.
      - Over 50% of part-time workers earn less than the earnings trigger, and 81% of part-time workers are women.
      - Over 40% of employees earning less than the trigger income are in receipt of child benefit.
    - 4.2 There are 40.7m people aged between 16 and 64 in the UK (Chart 1). Of these, around half, 20.1m, are eligible for automatic enrolment. The remaining 20.6m are ineligible due to either not meeting the eligibility criteria, being self-employed, being unemployed or being economically inactive. Therefore, half of the current population aged

22 to SPA do not have access to a workplace pension scheme through automatic enrolment. Though some may be saving in a pension scheme via other means.

Chart 1<sup>1</sup>



**4.3** The likelihood of meeting the automatic enrolment qualifying criteria is not evenly spread across the workforce. Some groups, for example, Bangladeshi, Pakistani and Black/ African/Caribbean employees, women, people with disabilities, carers and people who work for small employers or in the service industry are far less likely than other employees to meet the qualifying criteria (Table 1). This is because people from these groups are more likely to work in low-paid, part-time or casual work or to be self-employed. Some groups, such as Bangladeshis, are more likely than others to be illegally paid below the minimum wage.

<sup>1</sup> PPI analysis of Labour Force Survey data

**Table 1: employed people meeting automatic enrolment qualifying criteria (does not account for those pension saving independently of automatic enrolment)**

	Gender	Ethnicity	Disabled people and carers
<b>Proportion meeting automatic enrolment qualifying criteria</b>	Men - 84% Women- 68%	Black/African/ Caribbean- - 71% Pakistani – 68% Bangladeshi – 67%	Carers -19% Disabled - 70%

For more information on this topic please see:

[www.pensionspolicyinstitute.org.uk/publications/reports/ppi-automatic-enrolment-changes-report](http://www.pensionspolicyinstitute.org.uk/publications/reports/ppi-automatic-enrolment-changes-report)

[www.pensionspolicyinstitute.org.uk/briefing-notes/briefing-note-75---who-is-ineligible-for-automatic-enrolment](http://www.pensionspolicyinstitute.org.uk/briefing-notes/briefing-note-75---who-is-ineligible-for-automatic-enrolment)

- 4.4** The PPI is planning to publish a Briefing Note towards the end of March exploring women’s working patterns and the impact on retirement income of working one year longer. This Note will be the third PPI Briefing Note in the Well-being, Health, Retirement and the Lifecourse (WHeRL) research project conducted in collaboration with the Institute of Gerontology at King’s College London, Dalla Lana School of Public Health, University of Toronto; Research Department of Epidemiology and Public Health, University College London; Institute of Psychiatry, Psychology & Neuroscience also at King’s College London; Manchester University; Age UK; and the Department for Work and Pensions.
- 4.5** The PPI is also planning to conduct work on policies which could encourage greater private pension saving among the self-employed.
- 5.** Do the categories of non-eligible jobholders and entitled workers continue to make sense in terms of enabling those who are not eligible to be automatically enrolled to save into a workplace pension?
- 5.1** According to the Employers Pension Provision Survey, the opt-in rate is around 5% on average (2015). Opt-ins are higher among small employers (though small employers may have fewer eligible employees).<sup>2</sup> More work needs to be done on employer characteristics

<sup>2</sup> DWP (2016) Employers Pension Provision Survey

to determine whether those who would benefit from opting-in are making use of the option.

**6. How can self-employed people be encouraged and enabled to save more for later life/ for retirement?**

**6.1** While self-employed people are allowed to join a private pension scheme the majority of self-employed people still do not save in one. The proportion of self-employed people saving in a pension has decreased over the past few decades. 22% of self-employed men were saving in a private pension in 2013, a drop of 40% over 16 years.

**6.2** Lower saving levels among the self-employed can be partly attributed to the lack of an employer prompt for saving or an employer contribution, though the self-employed are eligible for tax relief on pension contributions. Self-employed people are not eligible to be automatically enrolled into pension saving (except in the case of some personal services contracts) though they can voluntarily join some private pension schemes. People may dip in and out of self-employment during their working lives and some will be automatically enrolled while in employment.

**6.3** Knowledge of tax-relief, pensions and other financial products is relatively low among self-employed people and many hold negative views about personal pensions. This indicates that while some of the self-employed people not currently saving in a pension scheme might benefit from joining one, they may need support and guidance in order to make that decision.

**6.4** While self-employed people stand to benefit from the new State Pension, unless a significant proportion of self-employed people choose to join a private pension scheme, private pension saving amongst this group will remain low and/or continue to decline.

For more information on this topic please see:

[www.pensionspolicyinstitute.org.uk/publications/reports/the-underpensioned-2016](http://www.pensionspolicyinstitute.org.uk/publications/reports/the-underpensioned-2016)

**Theme 2 - Engagement:**

**7. What examples are there of effective communications and engagement tools that have delivered:**

- sustained workplace pension saving over the long term, and
- increased levels of savings resulting from changing contribution rates?

8. In an individual's automatic enrolment journey, what are the most and least effective touch points when appropriate engagement can help reinforce personal ownership of pension saving? What form should that engagement take, who should deliver it and how?
9. What are the challenges and barriers to sustained or timely engagement for different cohorts and individuals, and how can they be overcome?
  - 9.1 There are many behavioural factors which explain why people do not always make rational decisions.
    - Choice overload;
    - Information overload;
    - Framing effects and choice architecture;
    - Heuristic decision-making - Anchoring heuristic, Representativeness heuristic, Availability heuristic;
    - Present bias and time inconsistency;
    - Overconfidence;
    - Risk aversion;
    - Low levels of self-control;
    - Procrastination and inertia.
  - 9.2 Behavioural interventions have been suggested as a way to improve decision-making in order to produce better outcomes as a result.
  - 9.3 There are examples of behavioural techniques which have been successfully used in other policy areas to reduce harmful behaviour:
    - Choice architecture redesigns have increased organ donor registration.
    - Creating new anchoring heuristics has been used to decrease alcohol consumption.
    - Decreasing availability and salience has also been used to decrease alcohol consumption.
    - Financial incentives have been used to counteract present-bias among smokers.
    - Refocusing risk in terms of others, rather than personal risk, has been used to increase use of safety precautions by reducing overconfidence.
    - Influence of social norms has been used in order to encourage behaviour that reduces risk.
  - 9.4 However, alongside behavioural techniques, a range of policy levers are necessary to ensure positive outcomes in pensions:
    - **Compulsion:** Options that people must take whether they wish to make an active choice or not.
    - **Defaults:** An option given to people who do not make an active choice.

- **Safety nets:** Policy mechanisms designed to help those who find it difficult to support themselves financially and are in danger of falling into poverty as a result.
- **Consumer protection:** Legal and regulatory measures put in place to protect people from fraud or poor governance.
- **Freedom:** Policies which allow greater freedom to individuals such as removal of tax regulations which prevent people from taking all of their DC savings in cash.

**9.5** The Behavioural Insight Team finds that if interventions are Easy, Attractive, Social and Timely (EAST) they are more likely to motivate action. (The below is a direct quote from the referenced BIT publication).

**9.6** *Make it Easy*

- *Harness the power of defaults.* We have a strong tendency to go with the default or pre-set option, since it is easy to do so. Making an option the default makes it more likely to be adopted.
- *Reduce the 'hassle factor' of taking up a service.* The effort required to perform an action often puts people off. Reducing the effort required can increase uptake or response rates.
- *Simplify messages.* Making the message clear often results in a significant increase in response rates to communications. In particular, it's useful to identify how a complex goal can be broken down into simpler, easier actions.

**9.7** *Make it Attractive*

- *Attract attention.* We are more likely to do something that our attention is drawn towards. Ways of doing this include the use of images, colour or personalisation.
- *Design rewards and sanctions for maximum effect.* Financial incentives are often highly effective, but alternative incentive designs – such as lotteries – also work well and often cost less.

**9.8** *Make it Social*

- *Show that most people perform the desired behaviour.* Describing what most people do in a particular situation encourages others to do the same. Similarly, policy makers should be wary of inadvertently reinforcing a problematic behaviour by emphasising its high prevalence.
- *Use the power of networks.* We are embedded in a network of social relationships, and those we come into contact with shape our actions. Governments can foster networks to enable collective action, provide mutual support, and encourage behaviours to spread peer-to-peer.
- *Encourage people to make a commitment to others.* We often use commitment devices to voluntarily 'lock ourselves' into doing something in advance. The social nature of these commitments is often crucial.

**9.9** *Make it Timely*

- *Prompt people when they are likely to be most receptive. The same offer made at different times can have drastically different levels of success. Behaviour is generally easier to change when habits are already disrupted, such as around major life events.*
- *Consider the immediate costs and benefits. We are more influenced by costs and benefits that take effect immediately than those delivered later. Policy makers should consider whether the immediate costs or benefits can be adjusted (even slightly), given that they are so influential.*
- *Help people plan their response to events. There is a substantial gap between intentions and actual behaviour. A proven solution is to prompt people to identify the barriers to action, and develop a specific plan to address them.<sup>3</sup>*

For more information on this topic please see:

[www.pensionspolicyinstitute.org.uk/publications/reports/consumer-engagement-barriers-and-biases](http://www.pensionspolicyinstitute.org.uk/publications/reports/consumer-engagement-barriers-and-biases)  
[www.behaviouralinsights.co.uk/wp-content/uploads/2015/07/BIT-Publication-EAST\\_FA\\_WEB.pdf](http://www.behaviouralinsights.co.uk/wp-content/uploads/2015/07/BIT-Publication-EAST_FA_WEB.pdf)

**9.10** The PPI will publish the second and third reports in the Engagement series in May/June, and on July 4<sup>th</sup>. The second report looks at international examples of engagement policies while the third segments the population by level of engagement, life stage and what policy interventions may help people to achieve better pension outcomes.

### **Theme 3 – contributions:**

- 10.** What are the key drivers, opportunities and barriers for individuals and employers that may affect their behaviours in relation to sustaining existing, or managing increasing, contribution rates?
- 11.** Is there scope for a more flexible approach to contribution rates to reflect an individual's life and employment journey?
- 12.** Do you have any evidence or views on the most appropriate/effective balance between employer and individual contribution levels? What are the options for encouraging, 'nudging' and enabling people to save more into their workplace pension?

**12.1** Default contribution rates for automatically enrolled employees are typically low. The minimum contribution rate is currently 2%, of which at least 1% must be paid by the employer. This

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<sup>3</sup> Service, O. Hallsworth, M. Halpern, D. Algate, F. Gallagher, R. Nguyen, S. Ruda, S. Sanders, M. with Pelenur, M, Gyani, A. Harper, H. Reinhard, J. & Kirkman, E. (2014) EAST: Four simple ways to apply behavioural insights Behavioural Insight Team

is set to rise to 5% (with 2% employer contribution) in April 2018, and then again to 8% (with 3% employer contribution) from April 2019. If people remain at these default saving rates they are unlikely to have a sufficient level of income replacement in retirement.

**12.2** There is a possibility that opt-out rates could increase as contribution rates increase. There may be a trade-off between trying to get as many people saving for retirement as possible and encouraging those who are saving to accumulate larger pots through higher contribution rates.

**12.3** An 8% band earnings minimum is not necessarily sufficient to achieve an acceptable standard of living in retirement. Even if a median earner contributes 8% of band earnings into a pension scheme every year from age 22 until State Pension age, they only have 50% chance of achieving the same standard of living in retirement that they experienced in working life (using private and State Pension income) and assuming that the State Pension is uprated in line with the triple-lock.

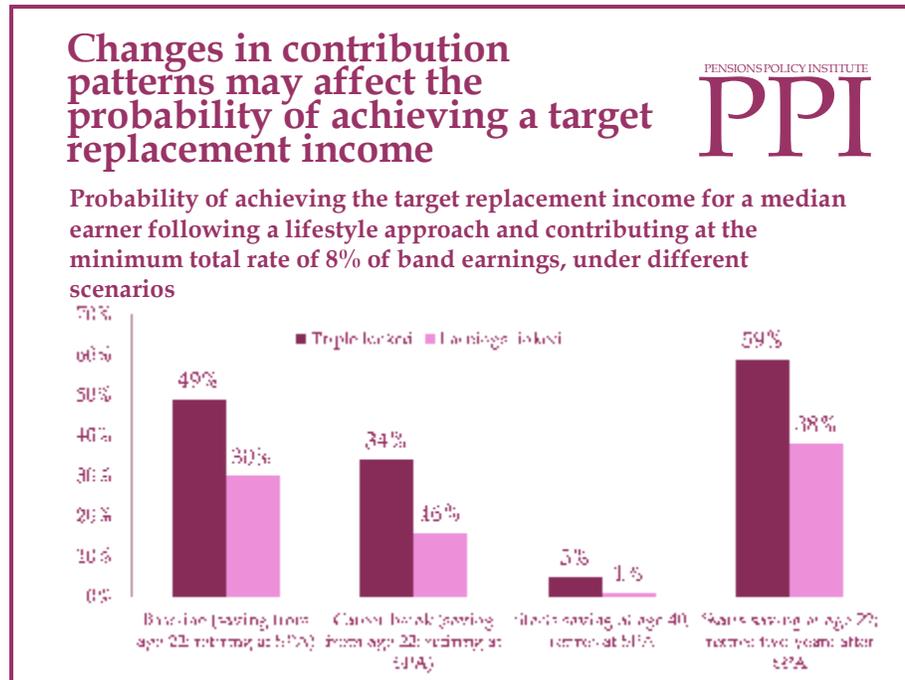
**12.4** In many cases, people will not contribute steadily for their entire working life and would require a higher percentage of contribution to achieve a 50% likelihood of replicating working life living standards. A median earner might need to contribute between 11% and 14% of band earnings to have a 2/3 chance of replicating working life living standards if contributing between age 22 and State Pension age. For people who begin contributing later to have a 2/3 chance of replicating working life living standards, required contributions could be as high as 27%.<sup>4</sup> A median earner who takes career breaks of seven years would need to contribute 18% of salary to have a 2/3 chance (Chart 2).<sup>5</sup>

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<sup>4</sup> If they start contributing from the age of 40

<sup>5</sup> the individual is assumed to start saving at age 22. Between the ages of 32 and 39 they take time off to care for children. They return part-time at age 39 earning at 50% of full-time earnings. They return to full employment at age 41 and retires at their State Pension Age (SPA).

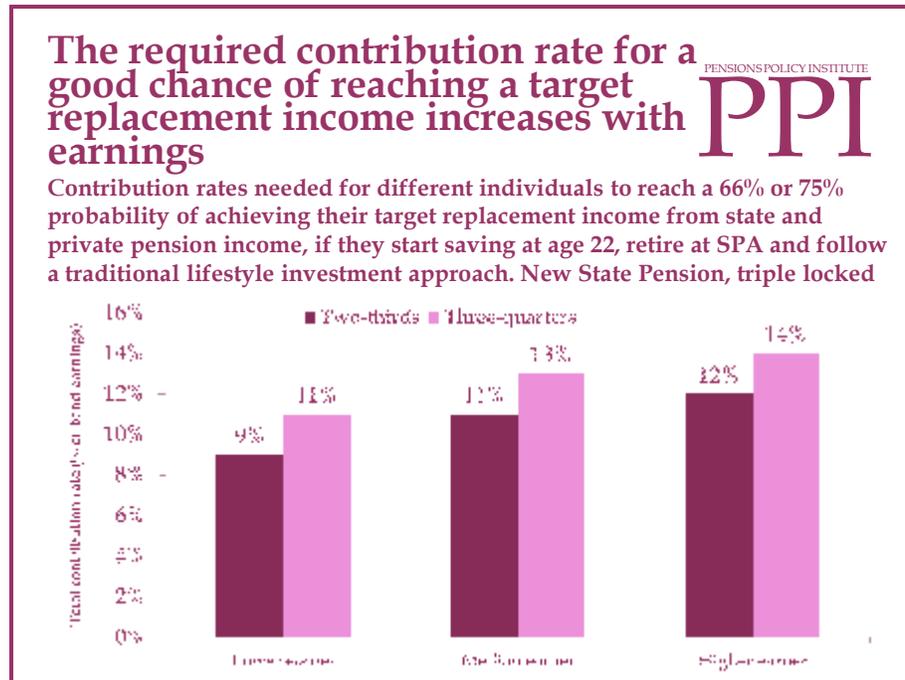
Chart 2<sup>6</sup>



**12.5** The probability of people achieving their target replacement income through their state and private pensions varies according to their earnings profile. Lower earners have a higher probability than median or higher earners because the new State Pension (nSP) represents a higher proportion of lower earners' pre-retirement earnings than for median or higher earners (Chart 3).

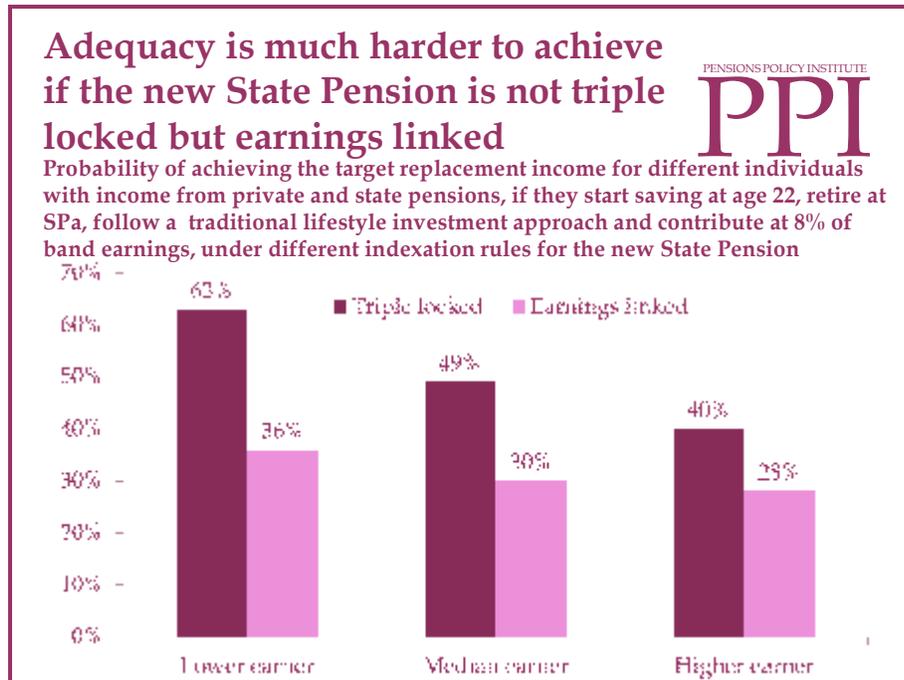
<sup>6</sup> PPI and King's College London modelling analysis.

Chart 3<sup>7</sup>



**12.6** Adequacy will be sensitive to the indexation mechanism used for the nSP. Currently, the nSP is uprated by the triple lock - the higher of changes in average earnings, changes in the Consumer Prices Index (CPI) or 2.5%. Current legislation stipulates that the nSP must be uprated at least in line with changes in average earnings. However it will be up to the government of the day to decide whether anything more than average earnings is needed. Adequacy is much harder to achieve if the nSP is increased in line with average earnings rather than triple locked (Chart 4).

<sup>7</sup> PPI and King’s College London modelling analysis.

Chart 4<sup>8</sup>

**12.7** There is a policy discussion around raising minimum contribution levels in the future using behavioural methods. One such approach is the Save More Tomorrow (SMarT) programme which schedules increases in contribution rates to coincide with pay rises. This approach utilises two behavioural biases in particular:

- Procrastination and inertia
- Endowment effect

**12.8** The PPI is currently undergoing a project looking at how changes to contribution legislation (such as different balance between employee and employer contributions and the potential impact of raising minimum contribution levels) could affect behaviour and outcomes from pension saving. This paper will be launched in July or September 2017.

**Forthcoming:**

- BN – the difference a year makes (WHERL – early April)
- BN (PhD Series 1): The impact of auto-enrolment in Italy, New Zealand and the USA (should be published by 22/3)

<sup>8</sup> PPI and King's College London modelling analysis

- Self-employed project (timetable being agreed)
- Consumer engagement: international lessons (due end May / June)
- Consumer engagement: life cycle journey (due 4th July)
- Relationship between employer and employee contributions (timetable being agreed)