Media Brief

Automatic Enrolment

June 2020

Note: This paper is intended as background information for the media. It is not intended as a comprehensive policy paper for The People's Pension.

What is automatic enrolment?

During the 1990s, the UK's system of workplace pensions began to break down. Due to a combination of tougher regulation and an ageing population, pension provision became more expensive and UK employers began to close final salary pension plans.

Attempts to get people to voluntarily save more in "stakeholder" pensions[1] did not succeed, and forecasts showed increasing numbers of people would be dependent on means tested benefits in retirement.

The 2003-05 Pensions Commission developed a package of reforms, including automatic enrolment, which the Government legislated for through the Pensions Act 2008. The policy requires all employers to offer workplace pension schemes and to automatically enrol eligible workers into their scheme. Auto-enrolment was introduced in 2012, with the largest employers joining first, followed by medium-sized and then small employers in stages until 2018.

What are the minimum contribution levels?

The government set minimum levels of contributions that must be paid into the scheme by both the employee and the employer. The contribution levels started at a total of two percent and have increased over time:

Date effective	Employer minimum contribution	Staff contribution	Total minimum contribution
Until 5 April 2018	1%	1%	2%
6 April 2018 to 5 April 2019	2%	3%	5%
6 April 2019 onwards	3%	5%	8%

Employers and employees can pay above the minimum contributions should they wish to.

It's important to note that under automatic enrolment, rather than calculating contributions from the first pound of an employee's salary, contributions are 8% on a band of earnings (currently between £6,240 and £50,000).

Who is eligible for auto-enrolment?

An employer has to sign an employee up to the scheme if they:

- Are employed in the UK.
- Are not already in a suitable workplace pension scheme.

- Are at least 22 years old, but under State Pension age.
- Earn more than £10,000 a year (tax year 2020-21) from one job.

How many people have been auto enrolled across the UK since 2012?

So far auto-enrolment has been a real success; the latest figures from The Pensions Regulator (TPR) show that 10.2 million eligible workers were signed into a company pension scheme by their employer since 2012.

Who's excluded under the scheme?

Not all workers are eligible for automatic enrolment. 9.5 million workers have been excluded from workplace pension since 2012 because they didn't meet auto-enrolment criteria.

Reasons for this include:

- They earn less than £10,000 from one job and don't meet the earnings threshold required for an auto-enrolment pension.
- They are under 22.
- They are part of the 15 per cent of the British workforce that are self-employed.

What issues have arisen from auto-enrolment that need to be addressed?

Adequacy of contribution levels:

The Government's 2017 review of Automatic Enrolment set out a way forward for UK pensions. It proposed removing the lower qualifying earnings band so that minimum contributions would be made from the first pound of earnings. And, it proposed reducing the age threshold to 18 so that people would begin saving when they enter the workforce.

The Government also acknowledged that contributions of 8 per cent won't provide enough of a retirement income for most people to live comfortably. There's a fine balance to be struck; increasing contributions, for example to 12 per cent, will make sense for many savers but not all. Any increase must pay attention to the needs of different groups and consider the affordability of further contributions for low earners.

Pensions Inequalities:

Gender pensions gap

Auto-enrolment is a success story, but it is in danger of not working for part-time women workers. Many more men than women are benefiting from the 'free money' which auto enrolment offers via employer and government contributions, because women are much more likely to be in low paid, part-time work and earning below the £10,000 earnings trigger.

This issue exacerbates the gender pensions gap – the inequality between men and women's pensions – which is currently more than double the size of the total gender pay gap, with the average female pensioner £7,000 a year poorer than her male equivalent[2].

Ethnicity pensions gap

The average pensioner from an ethnic minority is £3,350 a year worse off than other pensioners, representing a 24.4% gap in retirement income.[3] The divide is even bigger from a gender perspective. On average, our analysis – based on government surveys – shows that the gap in annual pension income between a female pensioner from an ethnic minority and a white male pensioner is 51.4%.

Removing barriers to membership of occupational pension schemes is crucial to closing the gap because ethnic minority employees are more likely to be low earners excluded from auto-enrolment.

Self-employed

Despite making up around 15 per cent of the UK workforce, self-employed people are not currently eligible for auto-enrolment. Measures intended to get people to save voluntarily for retirement have tended not to work: that's why we have automatic enrolment. So, the question now is how can automatic enrolment be replicated for the self-employed? In practice, this is going to be easiest through the tax system but there are many issues to work through before the self-employed can be brought into automatic enrolment.

Small pots and the General Levy:

The high rates of job churn and lower earnings among auto-enrolment savers means the Government's policy has led to a ballooning number of small pension pots – some with as little as one pence in them. These pots cost pension providers more to administer them than they receive in revenue, largely due to regulatory costs.

Auto-enrolment pension providers are required to pay the General Levy on Occupational and Personal Pension Schemes and the Fraud Compensation Levy. The former currently costs The People's Pension 65p per member and the latter costs currently 25p per member.

As the General Levy on Occupational and Personal Pension Schemes is calculated per pension pot, it has left large auto-enrolment master trusts paying a disproportionate share of the overall levy compared to the assets they hold, and unfairly subsidising regulatory activity for Defined Benefit pension funds.

For example, on the current system 10 master trusts will pay at least 25 percent of the total General Levy, despite only holding two per cent of assets.

On assets of £60bn and with 450,000 members, the largest pension fund in the UK would pay around £390,000. The Peoples Pension with its membership and much lower assets under management, would be liable for £2.9m.

At a time when the Government is proposing further increases to the General Levy – with one option which would see The People's Pension's bill rise by 245 per cent over three years – master trusts (multi-employer pension schemes) are questioning why their membership, with lower earnings and small pension pots carry the heaviest levy burden.

Net-Pay Anomaly:

People saving into an auto-enrolment pension receive tax relief, a top-up to their pension pot from the Government to encourage them to save. But a tax quirk means that hundreds of thousands of savers, overwhelmingly women, aren't receiving this further boost to their pension savings.

As a pension provider we offer employers a tax relief system that enables lower earners to get the basic rate of tax relief they're due automatically, but many pension schemes operate what's called a net-pay scheme, where pension contributions are put into people's pots before tax is deducted from their salary.

This system works well for most people, but not for those who earn less than the threshold for paying income tax. Even though they don't pay income tax they're still entitled to tax relief on up to £3,600 of pension saving a year, as an incentive to save, but if their scheme uses net-pay they won't receive it automatically.

This problem has grown as more people have been auto enrolled into pensions at the same time as the Government has increased the income tax threshold.

What is The People's Pension calling for?

We are calling on the Government to build on the success of auto-enrolment and make saving pay for the low paid by:

- Delivering on its pledge in the 2017 Auto-Enrolment[4] review to calculate auto-enrolment pension contributions from the first pound of earnings and lower the eligible age for auto-enrolment to 18 as pledged in the 2017 auto-enrolment review.
- Creating around 1.2 million new savers – the majority of whom would be women and 15 per cent of whom would be from ethnic minority backgrounds – by cutting the auto-enrolment earnings trigger to the Lower Earnings Limit of £6,240.
- Fulfil its manifesto pledge to review net pay anomaly which impacts 1.75m low earners estimated to be affected, two thirds and three quarters of whom are likely to be women.
- Review the structure of the General Levy on Occupational and Personal Pension Schemes and provide a breakdown of regulatory costs by pensions sector.

Footnotes:

1. Pensions: Challenges and Choices was published by the original Pensions Commission in October 2004.

2 The union Prospect published Tackling the Gender Pensions Gap in 2018

3 Read the Ethnicity pensions gap here

4 A number of recommendations were made in the Automatic enrolment review 2017