

# People benefiting from private pension reform: explanation of participation estimates – September 2009

## Summary

Our estimates of how participation in workplace pension schemes will increase as a result of the current reforms have changed since those published in the Impact Assessments accompanying the introduction of the Pensions Bill 2007. The most important change is that we expect more people to save in existing forms of workplace pension scheme, rather than in the personal accounts scheme.

Specifically, we expect:

- 10-11 million people to be eligible for automatic enrolment, compared to our previous estimate of 9-11 million;
- 5-9 million people to be newly saving or saving more in all forms of workplace pension schemes, compared to our previous estimate of 6-9 million;
- 3-4 million people to be newly saving or saving more in existing forms of workplace pension scheme, compared to our previous estimate of 1-2 million; and,
- 3-6 million people to participate in the new personal accounts scheme, compared to our previous estimate of 4-7 million.

These differences arise from improvements to our participation estimates modelling, updated data, and new evidence and insight into employers' likely choice of scheme. This includes new assumptions about the balance between employers who will use existing forms of workplace pension arrangement, and those who will use the new personal accounts scheme.

We will continue to update these participation estimates as we approach the implementation of the reforms, and as new evidence and data become available.

## Background

The workplace pension reform provisions aim to encourage and enable more people to save towards their retirement. They represent the second part of a package of radical reforms to the UK pensions system. These were initially set out in the May 2006 White Paper *Security in Retirement: towards a new pensions system*. The first part, a fairer and more generous state pensions system, was taken forward by the Pensions Act 2007.

The Pensions Act 2008 sets out a number of pension reforms with the aim of encouraging more people to save for their retirement, including automatic enrolment of eligible workers into a workplace pension arrangement, a compulsory minimum employer contribution and the introduction of a low cost pension scheme targeted at

those not served by the existing market, currently called the personal accounts scheme. This factsheet presents analysis on the impact of the reforms on the number of people saving in a workplace pension scheme.

From 2012, workers between the age of 22 and State Pension Age, with annual earnings in at least one job of more than £5,035 (2006/07 earnings terms) will be eligible for automatic enrolment into a qualifying pension scheme, unless they are already participating in such a scheme. It will be for the employer to choose the qualifying scheme into which they enrol their jobholders. The new personal accounts scheme will be one option open to employers and aims to complement existing workplace pension provision.

This factsheet sets out our current assumptions about what participation in workplace pension schemes will be after the reforms, particularly focusing on how our analysis and assumptions have changed since the previous participation estimates factsheet, published in November 2007. This previous factsheet was published alongside the Impact Assessment for the Pensions Bill 2007 (now the Pensions Act 2008) and explained how our participation estimates had changed between the May and December 2006 Regulatory Impact Assessments<sup>1</sup> and the 2007 Impact Assessment<sup>2</sup>.

Our current assumptions indicate that around 10–11 million<sup>3</sup> people will be eligible for automatic enrolment in a workplace pension scheme from 2012. This will lead to 5-9 million people newly saving or saving more in workplace pension schemes than before the reforms.

Employers will be able to choose between enrolling eligible jobholders into either an existing form of workplace pension scheme or into the new personal accounts scheme, or a combination of both. We estimate that there will be 3-4 million more people saving or saving more in existing forms of workplace pension scheme, and 3-6 million people participating in the personal accounts scheme; this includes some who were previously saving in existing forms of workplace pension scheme, and some who opt in.

There is inherent uncertainty around these figures. We can not be certain about how the pension and economic landscape may change in the years leading up to the reforms. And although our assumptions are informed on a programme of research, we can not be certain about how employers and individuals may change their behaviour in response to the reforms. This is why we have developed low, principal and high scenarios for all our trend and behavioural assumptions, and why figures in the factsheet are generally presented as broad ranges. The analysis presented here also assumes that all employers meet the requirements of the reforms, both to

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<sup>1</sup> Security in retirement: towards a new pensions system – Regulatory impact assessments and technical appendices, published in May 2006; and Personal accounts: a new way to save Regulatory Impact Assessment, published in December 2006

<sup>2</sup> Available here: <http://www.dwp.gov.uk/docs/pensionsbillimpactassessment-final2.pdf>

<sup>3</sup> All employee figures in this document are rounded to the nearest million unless otherwise stated. Note that this analysis focuses on the private and not-for-profit sectors. Self employed workers are exempt from these reforms and it is envisaged that most public sector employees will already have established pension schemes in their workplace.

provide a workplace pension scheme, and automatically enrol their eligible employees into it.

We will continue to monitor trends within the pension landscape and the economic context into which these reforms will be introduced, and so continue to improve our understanding of how the reforms will affect employers, individuals and the financial services industry.

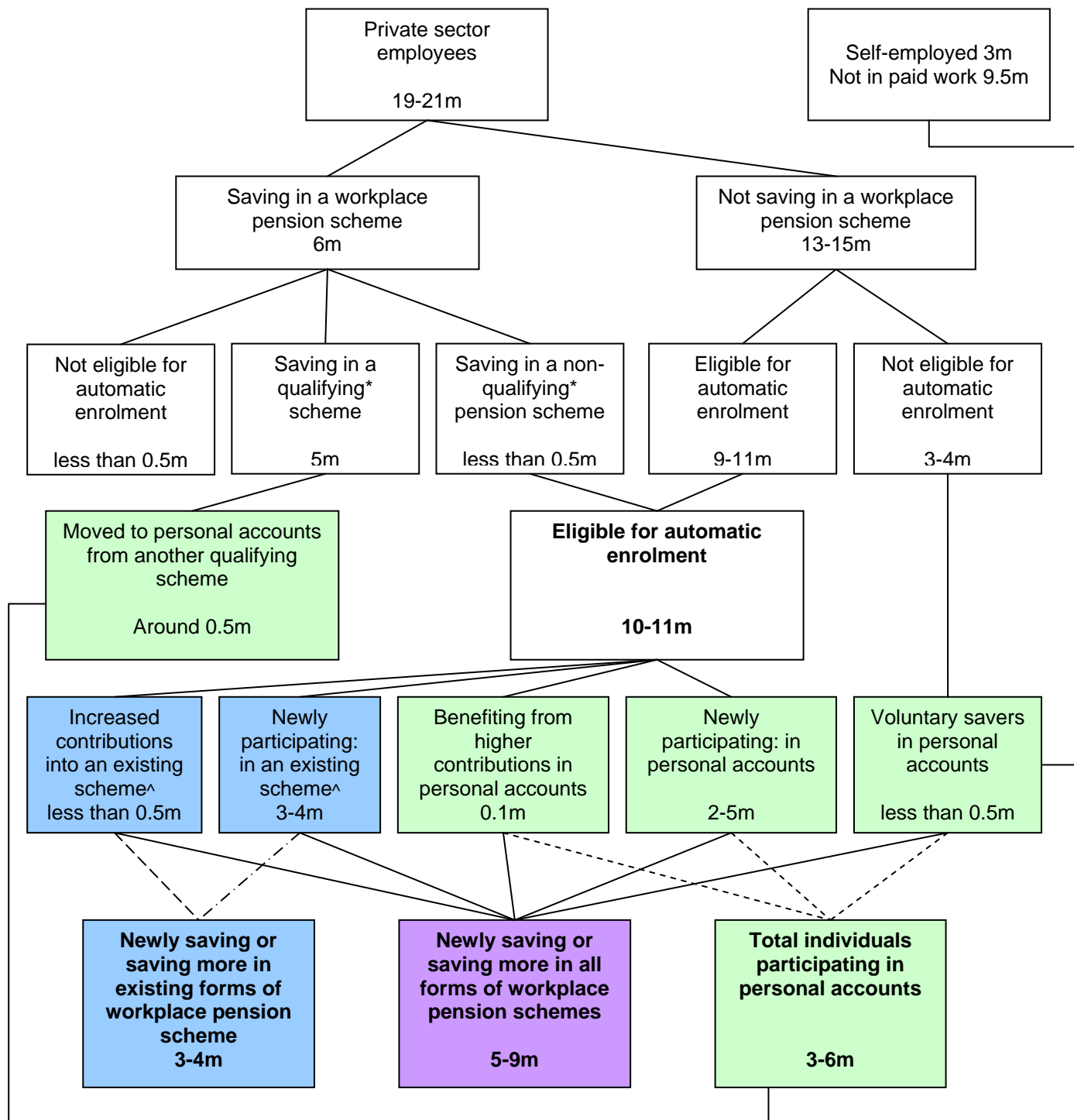
## **Headline Figures**

As a result of the reforms we expect there to be around 10-11 million people eligible for automatic enrolment into a workplace pension scheme. After accounting for people who opt out we expect this to result in:

- 5-9 million people newly saving or saving more in all forms of workplace pension scheme;
- 3-4 million people will be newly saving or saving more in existing forms of workplace pension scheme; and
- 3-6 million people saving in personal accounts, including some who were previously saving in existing forms of workplace pension scheme, and some who opt in.

Figure 1 below sets out the range our estimates take for the number of people eligible for automatic enrolment, and the increase in number of people we expect to be participating in the personal accounts scheme or in other forms of workplace pension scheme after the reforms are introduced.

**Figure 1: Estimates of number of people newly saving or saving more after the introduction of the reforms**



Source: DWP modelling

Notes: Ranges are rounded to the nearest million, and therefore may not sum.

\* Taking an employer contribution of at least 3% into a current workplace pension scheme as a proxy for a defined contribution scheme that is likely to qualify under the Pensions Act 2008. We have assumed that all defined benefit schemes qualify in this analysis.

^ This is an existing or newly set up workplace pension scheme, other than the personal accounts scheme.

## **Assumptions underpinning participation estimates**

Our post-reform participation estimates are modelled in four key steps. First we model the current pension landscape in terms of employer provision of pension schemes and participation in them by employees. Second, we project this landscape forward to when the reforms will be implemented. Third, using evidence from research with employers we make assumptions about whether employers will use the new personal accounts scheme or existing or other provision to fulfil their duty to provide a qualifying pension scheme to their workers. Fourth, using evidence from research with eligible individuals we make assumptions about how many people will opt out of a scheme after being automatically enrolled by their employer. This section gives further information about each of these steps.

### **Current pension landscape**

Our estimate of the current pension landscape is derived from the Employers' Pension Provision (EPP) survey<sup>4</sup>, weighted to the Small and Medium Enterprise (SME) statistics. Since the last factsheet was published the EPP and SME data used has been updated from the 2005 to the 2007 versions, and we have incorporated the non-profit sector into our analysis for the first time. The 2007 EPP survey shows that 21 per cent of 1.3 million employers already offered a pension scheme with an employer contribution of 3 per cent of pay. This means that around 79 per cent, or around 1 million employers were not offering a qualifying<sup>5</sup> pension scheme.

We have also incorporated new data from the 2007 Annual Survey of Hours and Earnings (ASHE) to identify the number of people who would be eligible for automatic enrolment. Combining EPP and ASHE data we estimate that in 2007 around 36 per cent of the eligible population were already in qualifying pension schemes.

### **Projecting forward the 2007 landscape**

To understand the number of employers and employees that the pension reforms will affect when they are introduced, it is necessary to project forward the 2007 landscape as defined above. Since the last participation estimates were published we have updated our employment and employer projections, and our pension provision and membership projections.

#### *Employment and employer projections*

Our projections of the overall private sector employed population are based on the actual growth figure for 2008; the summary of independent forecasts published monthly by HM Treasury for 2009 and 2010; and an assumption about long-term employment growth. This change in methodology has not changed our principal estimate that there will be 20 million private sector employees when the reforms are

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<sup>4</sup> Forth, J and Stokes, L, 2008, Employers' Pension Provision Survey 2007. DWP Research Report 545.

<sup>5</sup> Taking an employer contribution of at least 3% into a current workplace pension scheme as a proxy for a scheme that is likely to qualify under the Pensions Act 2008.

implemented, within a range of 19-21 million. We estimate that 16 million of these, within a range of 15-17 million, will be within the eligible group as defined by the Pensions Act 2008.

We utilise information from the Office for National Statistics on the birth and death rates of enterprises from 2002-2007 to develop assumptions about how the number of employers may change. We estimate there will be up to 1.3 million employers with duties under the reforms when they are implemented.

### *Pension projections*

To project forward our 2007 estimates of the pension landscape we reviewed the available evidence on pension membership and provision to individuals, and scheme provision by employers. Our principal scenario assumes that trends in pension provision observed between 2003 and 2007 continue. We assume that the trends in employer provision of pension schemes are reflected in membership trends, with employers turning away from occupational schemes in favour of less expensive workplace pension schemes. In this scenario 34 per cent of the eligible population are in a qualifying pension scheme when the reforms are implemented, compared to 36 per cent in 2007.

In our high scenario we assume that employers start to increase the quality of their pension provision in anticipation of the reforms, and consequently pension membership in qualifying pension schemes is slightly higher than in the principal scenario, at 36 per cent before the reforms take place. In our low scenario we assume that there is a more rapid trend away from occupational schemes and towards other workplace pension schemes, and consequently lower pension membership than in our principal scenario. In this scenario we estimate 32 per cent of the eligible population are saving in a qualifying pension scheme before the reforms take place.

Using these projections, our assumption is that between 10 and 11 million workers will be eligible for automatic enrolment when the reforms are introduced. This compares to our previous assumption that between 9 and 11 million workers would be eligible for automatic enrolment. These totals include around 0.5 million people who we expect to be receiving an employer contribution of less than 3 per cent.

### **Employers' choice of pension scheme**

Employers can choose what sort of scheme they use to fulfil their new duties. We make assumptions to determine whether an employer chooses to place some or all of their employees into an existing form of workplace pension scheme, or into the new personal accounts scheme. It is likely that employers will make this decision separately for existing employees who are pension scheme members, existing employees who are not pension scheme members, and new employees.

Our previous assumptions about employer choice were based on the DWP Employers' Attitudes Survey (EAS)<sup>6</sup> carried out in 2007. Our current assumption uses more recent results from research commissioned by the Personal Accounts Delivery Authority (PADA). The Employer Decision-Making (EDM)<sup>7</sup> research was carried out between December 2008 and January 2009 and contains responses from 3,000 employers about the choices they might make and the advice they may seek. The survey also has responses from 400 accountants, Independent Financial Advisors (IFAs) and Employee Benefit Consultants (EBCs) about the advice they are likely to offer employers.

Based on the findings of this research we have been able to refine and develop our assumptions about whether an employer will choose to enrol some or all of their employees into the personal accounts scheme, or into an existing form of workplace pension scheme when the reforms are implemented. This is primarily through an assessment of the likely influence of intermediary advice on employers' choice of scheme, and a better understanding of how many employees may be enrolled into the personal accounts scheme by employers offering multiple pension provision. We now expect between 40 and 55 per cent of all those newly automatically enrolled into a workplace pension scheme to be enrolled into the personal accounts scheme.

We estimate that 0.9-1.2 million employers will use the personal accounts scheme for at least some of their employees, and this will result in 5-6 million employees being automatically enrolled into an existing form of workplace pension scheme, and 4-7 million being automatically enrolled into the personal accounts scheme.

### **Opt out by individuals**

Although all eligible employees will be automatically enrolled into a qualifying pension scheme, participation is not compulsory. Employees will have the opportunity to opt out. Our estimate of the proportion of those automatically enrolled who will opt out has not changed from that described in the factsheet published in November 2007.

To estimate the number of individuals who will opt out we use evidence from the Individuals' Attitudes Survey (IAS)<sup>8</sup> carried out in 2007. Using the responses to this survey, and taking account of the age distribution of those in the group eligible for automatic enrolment and making assumptions about the possible behaviours of those who were not certain what they would do, we estimate an opt out rate of around 25 per cent, within a range of around 20 and 45 per cent. We also assume that all those who are already saving in a pension scheme will continue to do so even if automatically enrolled into the new personal accounts scheme.

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<sup>6</sup> Grant C, Fitzpatrick A, Sinclair P and Donovan JL, 2008, Employers' attitudes and likely reactions to the workplace pension reforms 2007: Report of a quantitative survey. DWP Research Report 546.

<sup>7</sup> Employer Decision Making Survey, forthcoming.

<sup>8</sup> Webb, C, Pye, J, Jeans, D, Robey, R and Smith, P, 2008, Individuals' attitudes and likely reactions to the workplace pension reforms 2007: Report of a quantitative survey. DWP Research Report 550

## **Other savers in the personal accounts scheme**

Individuals must meet the eligibility criteria in order to be automatically enrolled into a workplace pension scheme. If individuals do not meet these criteria then they might choose to voluntarily enrol into a pension scheme. Our estimates of the number of people who, although not eligible for automatic enrolment, might opt in specifically to the personal accounts scheme is unchanged from those described in the previous factsheet published in November 2007. These assumptions use information about the number of employees (and current participation rates) of those aged less than 22, the self employed, the inactive (who can continue to save once they have a personal account), the unemployed, and those earning less than £5k. Overall, we estimate that less than 0.5 million people will voluntarily opt in to the personal accounts scheme.

## **Conclusion**

Our estimates of how participation in workplace pension schemes will increase as a result of the current reforms have changed since those published in the Impact Assessments accompanying the introduction of the Pensions Bill 2007. The most important change is that we expect more people to save in existing forms of workplace pension arrangement, rather than in the personal accounts scheme.

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**September 2009**