PINBOX SOLUTIONS

SAVING THE NEXT BILLION FROM OLD AGE POVERTY

global lessons for local action

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THE EXPERIENCE WITH AUTO-ENROLMENT **IN THE U.K.**[1]

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[1] See also Chapter 23 on the way in which a 'Mission Office' or a Program Management Office was used to achieve robust implementation in the U.K., New Zealand, and India in the context of the U.K. experience.

INTRODUCTION

This chapter outlines the experience of the reform to private pension savings in the U.K. over the past 15 years. The reforms that the U.K. is undertaking are very significant. The reforms are focussed on improving the coverage of private savings for retirement, particularly amongst groups where savings were low – women, low earners, and those working for small companies. They are also aimed at trying to increase the number of people who will retire with an adequate income (defined by replacement rates). This chapter reviews the background to the reform, the historical trends that led to the debate, and how the proposals came about. It then discusses the implementation of the reforms, the challenges faced, key lessons learned, and things that could have been done differently. Getting the policy direction right is only the first challenge. The implementation of the policy is at least as big a challenge, and therefore also included in the chapter are the evaluation results to date, including the findings of independent reviews of the implementation.

The implementation of the reforms started in 2007, with the roll out of the reforms to businesses starting in 2012. The reforms will be completed in 2019 when the final contribution increase takes place. It is important to remain vigilant as a programme and not to declare success too early. The chapter therefore provides a summary of the approach the U.K. took and the lessons that have been learned thus far.

INITIAL CONDITIONS, CONTEXT AND HISTORY

Through the 1960s and 1970s, the U.K. had a successful private pension system with high levels of coverage when compared to other voluntary pension schemes. This success was based on large employers in both the private and the public sector providing good Defined Benefit (DB) pensions for their full-time workers. This meant that coverage of second tier pensions was very high, though there were pockets of employees without access. This coverage however declined through the 1980s and 1990s. This was partly driven by improvements in longevity, making these schemes very expensive for employers who bore not only the investment risk of the scheme but also the longevity risks. This reduction in coverage was also driven by changes in the labour market and industry. There was substantial growth in employment amongst small and medium employers, where the availability of good company pension schemes was usually lower. In addition, the industrial base moved away from manufacturing and towards retail where there was traditionally more turnover of staff and less of a tradition of providing pensions for the workforce. Female participation and part-time work also increased significantly through this period.

Many employers chose not to provide pensions to part-time workers or had reduced the generosity of the offer for newer workers. Women and others who took career breaks or moved jobs frequently were also penalised by long vesting periods and waiting periods to join schemes.

The State Pension System in the 1970s and 1980s was focussed on a high level of support from the State, including providing an earnings-related element. The State effectively provided a combination of a "zero" and "first" pillar in terms of the World Bank pensions taxonomy. In addition, the State support was uprated by earnings and therefore kept pace with rising living standards. Following concerns about the cost of State Pensions, reforms in the 1980s and the 1990s reduced the generosity of this support. One example of the reduction was the move from earnings indexation to price indexation in 1980. These changes helped control costs that came from significant increases in longevity. The State System became more focussed on poverty alleviation for current pensioners. The means-tested system for pensioners did increase in generosity and poverty rates fell significantly. The poverty rate for pensioners in the U.K. is now below the poverty rates for other age groups having previously being above them. However, as more means-testing came into the system, there was concern that this was reducing the incentives for people to save for retirement because extra income in retirement could reduce the means-tested benefits in old age.

Tax incentives for pensions were generous (currently around GBP 40 billion or USD 60 billion)[2] but largely focussed on better-off people. In addition there was increasing evidence that these did not lead to additional savings[3] and that people were generally confused and did not understand the impact of tax on retirement savings. Around two-thirds of expenditure on these reliefs go to those paying higher levels of taxation and, given that these are paid at the marginal rate of taxation, they are more generous for higher earners. The incentives for lower earners were less and also less understood by them. Over the decades, there had been multiple attempts to tackle the problem of low pension savings in relation to the growing need and gradually retreating coverage. Following the introduction of personal pensions in the late 1980s, the financial incentives to save were increased and this lead to an increase in the number of personal pensions held. However, when the costs of these incentives were cut back during the recession of the early 1990s, the persistency of savings was reduced. In addition, there had been significant mis-selling scandals that led to a loss of confidence in the financial industry to provide secure retirements.

The U.K.'s financial sector is one of the most developed in the world. However, despite this, insurance companies found it hard to distribute pensions to an increasingly disparate workforce at a reasonable cost. The growth of small and medium firms and the increasing prevalence of part-time work were challenges to providing pension schemes at a reasonable cost. A cost in a small company pension of over 1.5% per annum on

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[2] Converted at an exchange of USD 1.5 to 1 GBP.

[3] Chetty et al

assets under management was not unusual with some costs being significantly higher than this. To put this in perspective, a charge of 1.5% per annum reduced an average earner's pension pot by around a quarter, compared to an estimated reduction of less than 10% for a charge of 0.5 percent.[4]

Alongside these issues, the demographics in the U.K. continued to change in line with those of other Western economies. Improvements in health care and public health changes, such as reductions in smoking and improvements in diet, led to significant increases in longevity. In 1950 the dependency ratio was five people of working age for every pensioner. This was estimated to move to two to one without further reforms.[5]

THE PENSIONS COMMISSION

Throughout the 1990s and early 2000s, both the Major (Conservative) and Blair (Labour) governments tried to increase private pension savings by introducing simpler products, improving financial incentives and focussing on financial education.[6] However, the reduction in private pension saving continued. In 2002 the government set up a Pensions Commission to look at the issue of why people appeared to be "undersaving" for retirement and what the government needed to do to address it. The Commission was made up of three individuals. Adair Turner, the former head of the Confederation of British Industry, represented employers/ industry; Jeannie Drake, a senior official from the Trade Union movement, represented the worker perspective; and John Hills, a professor from the London School of Economics, represented the academic world.

Their first report, published in 2004, did not look at the policy issues but instead focussed on the nature of the problem. Their Report looked at various trends, international comparisons, and forecasts of future changes. The Report diagnosed the following problems with the U.K. pensions system – a useful breakdown that can also be seen in many other countries in the world.

- **Under-saving** - people were not saving enough for retirement;
- **Complexity** - people did not understand pensions and this caused an unwillingness to engage in the issues;
- **Inequalities of outcome** - the system was delivering unequal outcomes, between genders most notably, but also between several other groups; and
- **Sustainability** - increased costs due to an ageing population but these were not being borne in proportionate ways.

[4] Department for Work and Pensions, 2006, Security in Retirement: towards a new pensions system, TSO

[5] Department for Work and Pensions, 2006, Security in Retirement: towards a new pensions system, TSO

[6] This included the 'Stakeholder' suite of products including Stakeholder pensions. Employers with over five employees in fact had a duty to offer a stakeholder pension to their workers – which had its annual fees capped at 1.5% per year. However, employers had no duty to make contributions and there was no automatic enrolment or automatic deduction from salaries for workers so the spread of the product was very limited. But this experience was very useful in helping to develop the subsequent more successful approach as it highlighted the limits to improving coverage.

Whilst not proposing policy changes, the Report laid out the choices for the U.K. (and indeed any other economy facing these issues) very starkly. The U.K. could:

- Work longer
- Save more
- Have higher tax rates
- Or be poorer

This first Report was very important in building consensus around the need for radical change in the system. By using their first report to only lay out the analysis and issues, they were able to build a consensus about the scale of the challenges and the need for significant change amongst the various stakeholder groups. This consensus, about the size of the problem and the agreement that there were no other options apart from the four outlined above, was important. It meant that when the policy proposals from the Commission were put forward, it was difficult for the various groups involved in the debate – industry, employers, trade unions and individuals – to criticise the reforms without putting forward options of their own.

The Commission published their second report in 2005. This Report outlined their proposals in detail. It said that in order to address the size of the issue the U.K. should:

- **Work longer** – the report suggested significant and continuing increases to State Pension age;
- **Increase government spending** – the State offer needed to be simpler, increase with earnings, and provide much broader coverage; and
- **Save more** – the U.K. should introduce a system of Automatic Enrolment to affect the demand side problems in the market with a government-backed scheme to address supply side issues in the pensions market.

This chapter focuses on the changes around the "save more" agenda. However, it is important to understand the changes to the State Pension that have been made alongside the "Automatic Enrolment reforms". Since the Pensions Commission Report, there have been two major reforms of the State Pension System. The first provided greater coverage for those with caring responsibilities, which significantly benefited women by compensating them for time spent outside the labour market for childcare or other caring responsibilities. The complexity of the system was also reduced. In the second reform, a new State Pension was introduced with a single rate set above the poverty level (the Pensions Commission reforms started this process but still retained an earning related element). This was paid for by getting rid of the earning related elements. Alongside these reforms, the State Pension age has also increased through this period (currently moving to 66, with legislation for increases to 67 in the mid-2020s). These changes together should make it much clearer to individuals what the State will provide them at retirement (and when that will start). The simplification of this system should make the importance of private savings much clearer to individuals as well as ensuring that the incentives to save for retirement are not eroded by a means-tested system.

WHAT IS **AUTOMATIC ENROLMENT?**

The Pensions Commission put forward a three-pronged plan to "save more":

- that employees should be automatically enrolled into a retirement savings vehicle;
- that if they remained in the pension, then the employer should have to make contributions to that pension; and
- that the government should set up a pension scheme that would take any employer who wanted to use it. This scheme should be a low cost scheme (the Commission suggested a 0.3% annual management charge).

Through 2006-2008, the U.K. government worked through and legislated for these proposals. Some of the original Commission suggestions were changed as the practicalities of delivering them or securing a consensus for the whole package became apparent. For example, the original proposal for a government pension scheme (called the National Pension Savings Scheme – NPSS) was proposed as the default scheme was not introduced as it was felt that this would damage a lot of good existing provision. Instead the government scheme (the National Employment Savings Trust – NEST) is offered as an option for employers to choose (and which must accept any employer) among other options.

AUTOMATIC ENROLMENT – THE BASICS

The basic requirement in Automatic Enrolment is that all employers (regardless of size) provide access to a pension for all of their eligible workers (earning more than GBP 10,000 a year, over 22 and under state pension age). The earnings thresholds are the subject of an annual review by the government.

Employers need to automatically enrol their workers into that pension and, assuming the individual does not opt out,[7] the employer and the individual pay at least 8%[8] (of which a minimum of 3% must come from the employer) from a band of earnings. Employee contributions receive tax relief. So, if the employer pays the minimum 3% and the employee pays 5%, 1% of that will be made up of tax relief. This means that for the 4% contribution from the employee they will receive another 3% from their employer and 1% from government. This 1:1 ratio is important in communicating the reforms.

Employer who do not run a pension scheme, or do not want to set one up, can use the one set up by the government (NEST). NEST has a Public Service Obligation (PSO) and

[7] One of the main questions around this reform is why the Pensions Commission did not suggest a mandatory savings system, similar to the system set up in Australia for example. The Pensions Commission report does look at this as an option but dismissed it because it felt it may lead some groups to oversave. It is also clear in subsequent comments that the Commissioners have made that they did not believe that they could gain political acceptance for a mandatory pensions saving scheme as it would be viewed as an increase in taxation.

[8] Note that the level of contributions started at a total of 2% (1% from the employer, and 1% from the employee including tax relief), and will rise to 5% in April 2018 and to 8% in April 2019

must take any employer who wishes to join. Employers can decide which pension scheme to use as other pension schemes are available them. NEST is a public body that is accountable to Parliament through the Department for Work and Pensions (DWP) but runs at an arms-length from the government. It is set up as a trust, which means that it is legally required to work in the best interests of its members and is run on a not-for-profit basis.

Workers can opt out within a short window after they have been enrolled and their contributions would be refunded. After that window, workers can cease membership but their contributions cannot be returned and will stay within their pension fund. It is illegal for employers to try and persuade or induce their workers to opt out.

All employers must inform the Pensions Regulator that they have complied with the legislation and this must be done within five months of the start date of duties for that particular employer.

Every three years, employers must re-enrol all their workers who opted out or who have ceased membership in the intervening period.

These are legal duties on employers. If they do not fulfil their duties, they can be fined and ultimately can be subject to criminal sanctions.

AUTOMATIC ENROLMENT AND BEHAVIOURAL SCIENCE

The reforms were developed with a real desire to use and benefit from behavioural science. The early work of Leibsom, Benatzi, Madrian, and Thaler was very influential in the development of automatic enrolment. The "failure" of individuals to save for their retirement was viewed as the break down of perceived rationality. The work of the Pensions Commission showed that "initiatives to stimulate personal pension saving have not worked" and pointed to "the limited impact of providing better information and generic advice". Joining a scheme required an active decision, but there is strong evidence that people often experience inertia when confronted with such decisions. These are now well-known concepts but at the time were only entering the U.K. and global policy agenda.

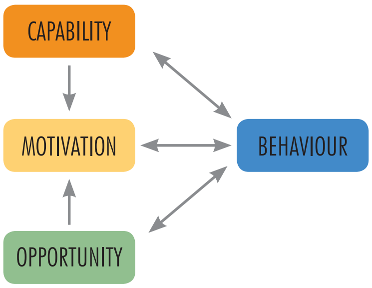
There are two main hurdles for people to overcome. First, they see the consequences of their actions as too far into the future because people find it difficult to imagine old age, and the decision to act does not seem to be a high priority and apparently is easily deferred. And second, regardless of how simple the product appears, pensions remain complex and confusing instruments. Selecting a pension scheme, even the decision to join one, is a complicated decision that requires significant mental effort. Therefore, loss aversion, hyperbolic discounting, and complex decision-making are all barriers to people behaving in an apparently "rational" manner when it comes to pensions.

Automatic enrolment overcomes these barriers by using people's inertia to encourage savings. The whole process is designed so that even if an individual does nothing they will be defaulted into saving for their retirement. The process places the employer in a central position and requires that they have to enrol the employee into savings and that the individual must make an active decision not to save. The reform also provides a "matching" contribution so the communication around the gains for the individual can be straightforward and clear.

Insights from behavioural science have been used throughout the design of the programme. From the letters sent to employers encouraging them to comply with their legal duties, to the design of the default fund in the NEST scheme. The original communication campaign for the programme used the slogan "we're all in" to highlight and stress the importance of this new social norm of saving.

Figure 3.1
A Behavioural Challenge

Why aren't people already saving more and working longer? What are the barriers?



- Large number of people working for employers who don't offer private pensions (opportunities)
- Yet even for those who did, not many choose to enrol
  - » Even if only employer contribute! (Capability? Motivation?)
- Informed choice?
  - » Fund charities to educate people, information campaigns... nothing made a difference!
- People wanted to save more, but didn't!

HOW WAS THE REFORM IMPLEMENTED?

The implementation of the reforms started alongside the policy development. The initial work was largely around the feasibility of the plans, pulling together the business case for the reforms and learning from other countries that had undertaken reforms of a similar nature (the Kiwi-Saver in New Zealand, the Superannuation reform in Australia, and the PPM reform in Sweden were particularly helpful in sharing their experiences). By 2007/8 the programme was ready to start formal implementation of the reform.

There are three main delivery bodies within the programme, each with a different role:

- **Department for Work and Pensions:** has the overarching responsibility for the delivery of the programme, is responsible for the legislation (and owns the policy), communication to individuals and stakeholder handling. In addition, it is the "sponsor department" for the other two stakeholder organisations.

- **The Pensions Regulator:** has lead responsibility on maximising employer compliance, educating and supporting employers to make the necessary changes and enforcing the law if they do not, working with employer groups and delivery partners such as payroll providers, pension schemes, and accountants to support employers. For more details on the role of the Pensions Regulator see Chapter 23 on the Mission Office.
- **NEST:** provides a low cost scheme that is required to take on any employer that chooses to use it. It is set up as a trust that has to act in the interests of its members and is responsible for investing members' money.

NEST – A NECESSARY GOVERNMENT INTERVENTION?

One of the more contentious parts of the package proposed by the Pensions Commission was to establish a government backed scheme in the sector. The response from consumer groups to this proposal was generally positive. They felt that it would ensure that people received good value on their savings and that this would provide a challenge to the perceived high charges in financial products at the time. However, the existing pensions industry felt that such an intervention was not necessary. They argued that the introduction of automatic enrolment would reduce costs in the industry by increasing demand and that they would be able to serve most of the market. Some argued that the government should pay them to take on unprofitable business rather than starting a separate scheme.

Part of the compromise was to change the default for employers. The original Pensions Commission proposal required all employers to use the NEST equivalent scheme unless they could show that they were providing something better. The legislation allowed employers to choose any scheme they wanted as long as it met certain "qualifying conditions". This approach was criticised by some who felt this put the government scheme at a disadvantage as it would allow the private sector operators to "cherry pick" the best employers and then leave the least profitable business to the government scheme.

The next challenge for the establishment of the NEST scheme was to agree that the proposal met the conditions for "State Aid" with the European Commission. It was clear that this was an intervention into a market and a case was needed to be made that the intervention was proportionate. This was agreed in 2010 and the scheme was established.

Since the start of the reforms, one of the areas of continuing debate has been around NEST and its place within the market. It seems fair to say that NEST is now accepted by most people as an essential part of the reforms. However, the debate on its size and possible market advantage continue. The criticism comes in two forms. First, a belief that NEST is too large and distorts the market. With over four million members, NEST is a very large pension scheme for the U.K. (by members it is probably the largest pension scheme in the U.K.). However, its assets under management remain relatively low at GBP 1.4 billion (although these assets will, of course, grow over time). The alternative criticism is that it is too costly and that it will take too long to repay its loan to government. In some ways these two criticisms are contradictory.

Most commentators view the NEST intervention as a positive one and central to the success of automatic enrolment. They view it as addressing the market failures that the Pensions Commission highlighted. The average salary for a NEST member is significantly below the national average and NEST market share is highest amongst the smaller companies. Its mission to provide low charges in the market has also provided a clear incentive for others to reduce their charges to savers. In addition, it has been very innovative in how it approaches investment and communication.

DELIVERY TIMELINE

- Oct 2004 – Pensions Commission analysis report
- Dec 2005 – Pensions Commission report on policy recommendations
- 2006 – Government response to the report (May and December publications). Through this period there was also an "Industry Challenge" to come up with different models after criticism that the Pensions Commission approach was too government led and a more market-based approach may work better.
- 2007 and 2008 – legislation written and passed[9]
- 2010 – change of government and review of the policy and programme[10]
- 2011 – NEST went live
- 2012 – first employers required by law to auto enrol their workers
- 2012-2015 – all large and medium firms (with more than 30 employees) roll out
- June 2015 – test group of small and micro employers (1-29 employees) were subject to duties
- 2016-2017 – all small and micro employers subject to duties in a staged roll out
- 2018 and 2019 – increases in contribution levels, and employers established since October 2017 subject to duties

IMPLEMENTATION APPROACH

Big bang or cohort by cohort?

The sheer scale of implementation meant that a big bang implementation was never an option. In total there are approximately 1.3 - 1.4 million employers in the U.K. who would have new legal duties as a result of automatic enrolment, and approximately 10 million workers would be directly affected by the change and would be put into a pension scheme or be saving more in a pension scheme. The pension schemes would not be able to deal with this administration and the Pensions Regulator would have been unable to build sufficient capacity to deal with its role.

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[9] Pension Act 2007 and Pensions Act 2008

[10] Making Automatic Enrolment Work

An important decision made in 2008, was that the roll out would start with the very largest employers, and would be sequenced by size. Once implementation reached employers with fewer than 30 employees, the implementation would be randomized and each month a certain number of employers would be subject to the duties until all employers were covered.

The advantage of starting with large employers was that it would set the tone for success. Large employers were most likely to be compliant, both from a reputational perspective, and also because they were most likely to be familiar with pension issues as most of them already offered a pension scheme, even if it did not cover all their employees.

Larger employers are also more complex and so many would find implementation harder. However, it was felt that they would have the resources to make the implementation work.

Finally, larger employers employ a large proportion of the U.K.'s workforce and therefore millions of workers would benefit from an early adoption of automatic enrolment. While it is true that many of these employers already had schemes, these schemes were not necessarily available to all staff from day one of their employment or to all types of staff. So, for instance over a 100,000 workers were put into pension schemes by just four employers in the early months of the roll out of Automatic Enrolment.

The original implementation was planned over three years – starting in 2012 and ending in 2015 (this was seen by some as a delay from the original Pensions Commission proposal to go live in 2010 and complete in 2012, which was assessed as not possible when looked at in greater detail).

The original timeline was set before the financial crisis, and the U.K.'s coalition government decided in 2010 to extend the implementation. While implementation to large organisations would still begin in 2012, the roll out to micro and small employers would now be delayed until 2015. This gave small organisations breathing space while the economy was recovering from the financial crisis.

The implementation plan included a small test phase with a group of 30,000 small and micro employers to test systems before going live with the remaining 1.2 million employers. These employers took on the duties six months prior to any other small and micro employers, and allowed the programme to test its communications and enforcement approaches and to understand the behavioural pattern of these employers.

Phasing

The other major implementation decision made up front was to 'phase in' contributions levels. The idea behind this was to provide a gradual increase in contributions so as to have both a minimal impact on worker's take home pay and to cushion the costs for employers.

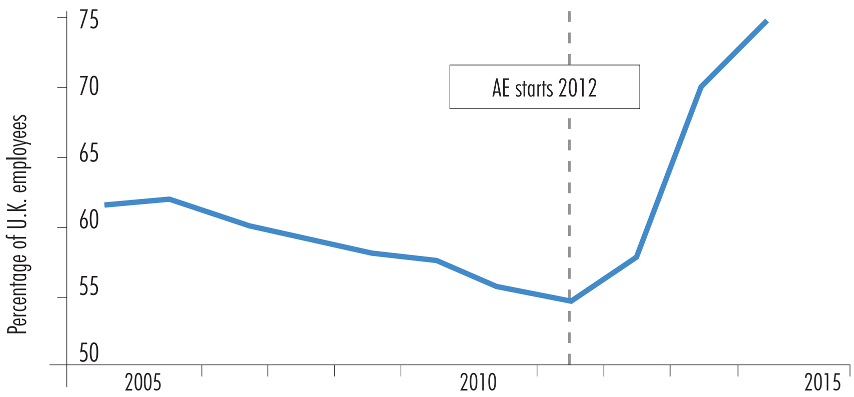
There are three phases. In phase one, employers pay 1% of earnings and employees pay 1%, though this includes a contribution of 0.2% by government in the form of tax relief. In phase two, this increases to 2% from employers and 3% from employees (including tax relief by government), and in phase three this increases again to 3% from employers and 5% from employees (including tax relief) from government. Phase two is due to come into effect in April 2018 and phase three in April 2019.

The original Pensions Commission Report recommended that the U.K. should aim for a replacement ratio in retirement of two-thirds of the final wage for the average worker. With State Pension and contributions through Automatic Enrolment of 8%, the total pension likely to be accrued by workers is below this. There will be a continued debate in the U.K. about how to increase contributions further in the 2020s.

WHAT HAS BEEN ACHIEVED? EARLY EVALUATION FINDINGS

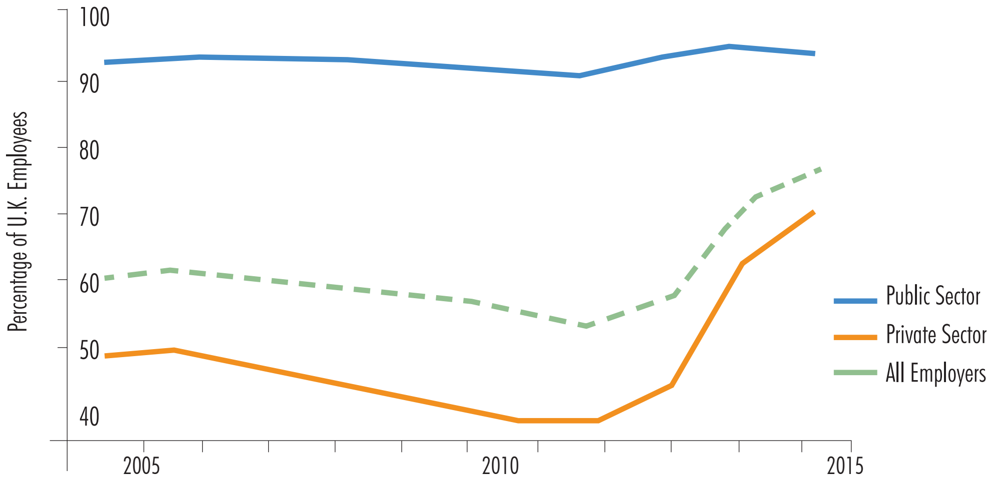
Automatic enrolment has reversed the long term decline in pension savings in the U.K.. Between the introduction of the reforms in 2012 and April 2015, the overall proportion of eligible employees saving into a workplace pension increased by 20 percentage points from 55% to 75% (as seen in Figure 3.2). Much of this has come from increases in private sector saving, which has increased by 28 percentage points (from 42% in 2012 to 70% in 2015), whereas public sector participation increased by three percentage points (from 88% in 2012 to 91% in 2015). This can be seen in Figure 3.3.

Figure 3.2
Proportion of all eligible employees belonging to a workplace pension[11]



[11] Automatic Enrolment – Commentary and Analysis", The Pensions Regulator, July 2016

Figure 3.3
Eligible workers' participation in workplace pensions by sector



By January 2016, over seven million workers had been auto-enrolled into a DC pension scheme and a further 600,000 are due to be put into a DB (Defined Benefit) pension scheme in 2017.

The opt out level by individuals is less than one in 10 (originally estimated at around one in three), and while it is still too early to confirm, indications are that re-enrolment (three year cycle for all employers) is also increasing pension savings. Even workers that originally opted out when enrolled a second time have a high rate of remaining in a scheme. A total of over 250,000 workers have been re-enrolled through this process.

Before automatic enrolment began, 35% of women employed full-time in the private sector had a workplace pension. As of 2015 this had risen to 65 percent [12]

From a compliance perspective, most employers are doing the right thing and are becoming compliant within the expected time. The Pensions Regulator has taken a firm stance with employers who do not, and to date has issued:

- Over 27,000 compliance notices (these are a warning notice from the Regulator that the employer may get fined if they do not become compliant); and
- 7,500 penalty notices (these are financial penalties).

Overall compliance levels have been excellent with over 99% of medium and large organisations compliant, and over 95% of micro and small employers, who have been subject to the duties, compliant.

[12] The Institute of Fiscal Studies (IFS), "What happens when employers are obliged to nudge? Automatic enrolment and pension saving in the U.K.", Jonathan Cribb and Carl Emmerson, 17th November 2016

The programme has been subject to many independent reviews, including the U.K.'s National Audit Office who called the programme a "tremendous success" and value for money.

In November 2016, the Institute of Fiscal Studies (IFS) issued their report on automatic enrolment titled "What happens when employers are obliged to nudge? Automatic enrolment and pension saving in the U.K.".[13] The research exploits data on almost half a million jobs from April 2011 to April 2015 to look at how contributions to workplace pensions by private sector employers and their employees have been affected by automatic enrolment.

KEY FINDINGS BY THE IFS

- Their estimates suggest that in April 2015, a total of GBP 2.5 billion a year more was saved as workplace pensions as a result of automatic enrolment. This amount is highly likely to increase significantly over the next few years as more employers are brought into the scope of automatic enrolment and as minimum contributions increase from 2% to 8% of qualifying earnings. The increase in pension saving arises from a big increase in pension membership.

- Automatic enrolment increased pension participation among those eligible by 37 percentage points, so that by April 2015, 88% of these private sector employees were members of a workplace pension scheme. In contrast, prior to automatic enrolment, around half of these employees were members of a workplace pension and membership had been falling over time.

- In 2012, there were around 5.4 million private sector employees who were members of a workplace pension. By 2015, this had increased to 10 million. At this point one-quarter of eligible private sector employees (3.4 million) worked for an employer that was yet to be brought into the scope of the policy.

- Automatic enrolment boosted pension coverage the most among those aged 22 to 29, those earning between GBP 10,000 and GBP 17,000 per year, and those who have been with their current employer for less than a year. For each of these groups, for whom pre-reform coverage rates were particularly low, automatic enrolment has increased membership rates in workplace pensions by over 50 percentage points. In 2015 coverage among all of these groups had risen to over 80%.

- Automatic enrolment has also increased the number of employees putting considerably more than the current minimum amount into a workplace pension. The proportion placing 5% or more of their total earnings into a workplace pension has increased by seven percentage points.

- The IFS find no evidence of employers reducing employer contributions for newly-hired employees or existing members of workplace pensions.

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[13] The Institute of Fiscal Studies (IFS), "What happens when employers are obliged to nudge? Automatic enrolment and pension saving in the U.K.", Jonathan Cribb and Carl Emmerson, 17th November 2016

WHAT WERE THE MOST DIFFICULT AND **IMPORTANT CHALLENGES?**

This section outlines what were the most difficult challenges for the programme during the past 10 years or so. These challenges are unlikely to be unique to the U.K.

STAKEHOLDER SUPPORT AND RETAINING A CONSENSUS

A key challenge has been to maintain strong political and stakeholder support for the policy and for the implementation. The Pensions Commission did a significant amount of work to gain consensus for reforms. However, this is difficult to maintain when there are challenging periods and when there are changes in government.

Following the Pensions Commission, all political parties were in agreement but there was still a need for political parties to "own" the programme. The Labour Government set up the Pensions Commission and was committed to the implementation of its key recommendations. It committed to start the roll out of automatic enrolment in 2012.

The DWP worked hard over the period from the launch of the Pensions Commission Report until the passing of the legislation in 2008 to maintain consensus, working with stakeholders on the detail of the legislation. All stakeholders supported the principle of automatic enrolment, but to turn this into a piece of legislation that everyone could support was a major challenge. Issues related to NEST positioning were key to this, and this challenge is described in detail below.

The first major potential challenge to the programme came after the 2010 election, which led to a coalition government of Conservative and Liberal Democrats. Both parties had supported the principle of automatic enrolment and in the negotiations that followed the election, its implementation was included in the Coalition Agreement – the coalition government's equivalent of a manifesto.

How it was to be implemented was, however, under discussions and the government set up a review called "Making Automatic Enrolment Work".[14] The review focused on four key questions:

1. Is there a case for excluding a substantial additional tranche of workers from automatic enrolment, for example those earning below a particular threshold, or those above a certain age?
2. Is there a case for excluding any group of employers, in particular the very smallest employers, from the additional responsibilities implied by the policy?
3. Would any changes to the proposed regulations, implementation and details surrounding automatic enrolment, enhance the policy? and

[14] Making Automatic Enrolment Work – a review for the Department of Work and Pensions" (DWP), 27th October 2010

4. Under what circumstances is NEST necessary for the successful implementation of automatic enrolment and are there changes to the rules surrounding NEST that would be helpful?

THE REPORT CONCLUDED THAT :

1. The earnings threshold at which someone would be automatically enrolled was too low, well below the income tax threshold, potentially enrolling low earners into a pension leading to a higher level of income in retirement than they can get in their working lives. In addition, contributions were due from the first pound earned above that threshold. This meant that many people on very low earnings would build up very small pots. They proposed that people should only be automatically enrolled once they reached the income tax threshold but that contributions should be on earnings in excess of the National Insurance earnings threshold. This would avoid automatically enrolling those not earning enough to pay income tax, would ensure that the very tiny levels of pension contribution possible under the original proposals are avoided, but would ensure that many who would benefit from automatic enrolment are not excluded by a higher threshold.[15]
2. The review looked at whether some employers should be excluded from the automatic enrolment duties, say those with fewer than 10 or five employees. In the end it concluded that no such change should be made, because it would exclude 1.2 million employees from pensions, potentially create a barrier to employer growth, and create major issues in enforcing the regulations at the margins of employer size.
3. The report also looked at the detailed regulations and found four areas where it believed change could improve the regulations:
    - Introduce a three month 'waiting period' for employers. This would mainly help employers who employ seasonal staff, allowing them in effect to not enrol these staff if their contracts were for less than three-month periods.
    - Introduce a new certification process for earnings.
    - Allow employers in the first stage of automatic enrolment the flexibility to bring forward their staging date by three months.
    - Introduce a three-month window around the three yearly re-enrolment date, again giving employers flexibility to choose a date that aligns with other business processes.
4. Finally, the review considered whether there was a need for NEST. It concluded that, along with the recommendation to not exclude any employers from scope, NEST was needed as the smaller end of the market was not profitable for other providers. It also concluded that some restrictions on NEST (a contributions cap and a ban on transfers in and out) should be lifted at the end of staging, and that the government should legislate for this earlier than necessary to provide clarity.

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[15] The programme will undertake a statutory review in 2017. One area that it will consider is whether very low earners are being excluded from pension savings and whether these rules need to be reviewed.

The review recommendations were accepted by the government and this gave the green light for the subsequent implementation of Automatic Enrolment starting in 2012.

There was a further change of government in 2015, although this was a change from a Conservative-Liberal coalition to a Conservative majority government. This again introduced some uncertainly around the programme. However, by this stage, the rollout was proceeding well and the results were even better than had been anticipated. On this occasion, no further changes were made to the regulations.

The support of all political parties introduced complexity to the policy delivery (for more on this, please see the sub-section on complexity) but ultimately was key to policy success. Getting all the main political parties to agree on areas such as implementation was very difficult. It did mean that there was early debate on major issues and this created stability and reduced "tinkering" to support the successful implementation.

NEST CAPACITY AND DELIVERY

One of the biggest challenges and risks for the programme was the setup and delivery of NEST. From day one, NEST had to be ready to take any employer that wanted to use it. The scheme has a PSO unlike others in the market and, therefore, it could not turn away business if it had capacity problems. As the largest employers come in first, NEST's functionality had to be in place from day one as the largest employers had the most complicated workforces. It was also clear that NEST would become a very large pension scheme. It was set up to focus on small and micro employers as well as employers that were unprofitable for other businesses to provide pensions to, and this market was a significant size.

In addition to these challenges, NEST also had to serve its market whilst providing a low charge (an equivalent of 0.5% of assets under management or AUM). To ensure that NEST remained focused on its target market (and as part of achieving a continued consensus on reforms), the government placed restrictions on what it could provide (there was initially a ban on transfers and a maximum contribution of GBP 4,900 at 2016-17 levels) which made it more challenging to deliver.[16]

From day one, NEST was clear that in order to meet these challenges, it would need to use technology very effectively and support most employers with a self-service facility. NEST partnered with Tata Consultancy Services (TCS) to run nearly all the operational aspects of the scheme.

NEST dealt with these challenges very well. Alongside TCS, it designed customer journeys to reduce the need for employer contact with TCS staff so it could deal with such a large scale of input. NEST has also continued to enhance its online functionality so that it could automate more employers. More recently NEST, like a number of other providers, has integrated its core pension payment site with the payroll software that most employers use to manage employee benefits. This further increases the ease with which employers

[16] These restrictions were in place from NEST's launch until April 2017.

can meet their obligations and hence further reduces costs. In line with the programme approach, to test and learn, NEST has also tried to ensure that it tests its processes on a smaller scale before expanding their availability. The programme is now at a position where the vast majority of employer sign-ups and contributions are completed online with no direct input from NEST or TCS staff.

As NEST is financed by a loan from government, its viability is constantly monitored. The loan will be repaid through charges levied on members but it is important also that costs are kept as low as possible. The current expectation is that NEST will pay back its loan in line with the original timetable.

Currently, NEST has over four million members and serves over 250,000 employers. It has GBP 1.4 billion in assets under management.[17] It continues to grow and it is not unusual for 1,000 employers a day to join NEST as the roll out for small and micro employers continues. However, the systems it has put in place continue to hold up well. In addition, it receives very good customer satisfaction scores from both the employers and employees who use it.

SCALE OF MARKET CHANGES AND OTHER PROGRAMMES ROLLING OUT IN PARALLEL

While the introduction of NEST was an important intervention, the entire existing pension system would be required to adapt to the changes in Automatic Enrolment. In order to be used for automatic enrolment, Defined Contribution (DC) pension schemes would have to become qualifying – meaning they would have to:

- be a personal or occupational scheme;
- be tax registered;
- accept minimum contributions;
- ensure that there is nothing in the rules of the scheme which would act as a barrier to automatic enrolment; the jobholder must also not be required to provide any information or express a choice, such as choosing funds; therefore, the scheme will need to have a suitable default fund in place; and
- apply a charge cap to default funds in workplace pensions schemes being used for automatic enrolment, the charge is set at 0.75% of funds under management or an equivalent combination charge.

DB schemes could also be used, though different criteria are set for them. It was expected, and has turned out to be the case, that the use of DB schemes is low.

The other important supplier to employers were payroll providers. The basic processes that an employer needs to do for automatic enrolment are:

- check whether each employee is over an earnings threshold or within an age band;

[17] These figures are at January 2017.

- calculate the pensions contributions to be made by the employees and the employer;
- deduct these contributions and pay them to the scheme; and
- inform the employee what they have done and how much their deductions are – usually via the payslip.

All of these tasks are ones that payroll software carries out in each pay period in order to deduct tax. The process is basically a payroll one. If payroll carries these out, then the burden on employers is minimised. Getting the payroll providers ready was a major task.

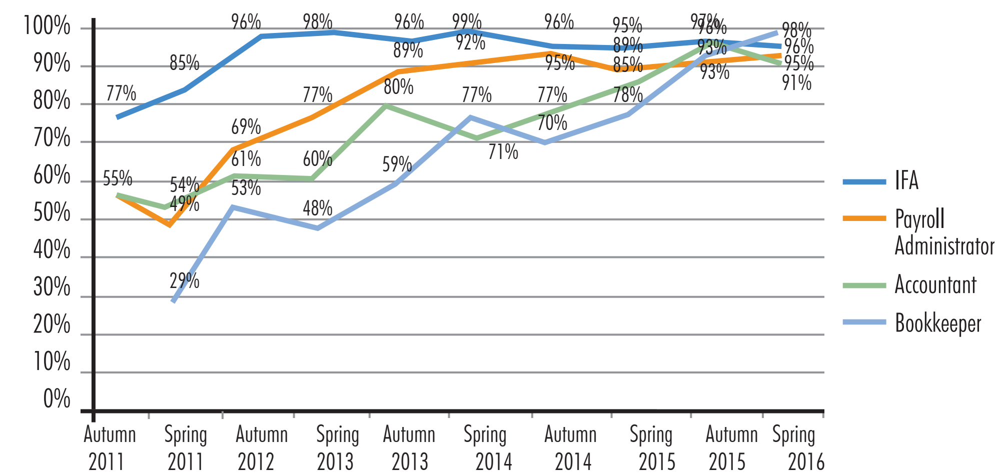
The Pensions Regulator recognised the importance of this market early. It set up a specialist team that travelled the length and breadth of the country focused on educating the suppliers on the regulations, and diving deep into product specifications to ensure that the products were Automatic Enrolment compliant. It also conducted training of technical staff and front-line support staff.

While both the pensions and payroll industries are relatively concentrated, there is a long tail of small suppliers. Getting the large players compliant was the key to success but getting to this tail has been a challenge.

Similarly, many employers already have advisers either providing advice or carrying out processes for them. Very often, payroll is outsourced to an accountant, bookkeeper, or bureau. It was essential that when employers turned to their advisers for help with Automatic Enrolment, the advisers were ready and knowledgeable. The following chart tracks levels of understanding of the key adviser groups and is an indication of the types of critical success factors that can be used in a Mission Office as set out in Chapter 23.

Figure 3.4

Level of understanding amongst key adviser groups PLEASE GIVE SOURCE



Source: TPR published data

As we see in Figure 3.5, understanding reached near universal levels in the early months of implementation to micro and small employers. Again, the Pensions Regulator set out a detailed and comprehensive programme of education and enablement to this group. It set up a panel of professional advisory bodies that provided huge support to and education of their members, using material supplied by the Pensions Regulator.

Finally, a major complication to the implementation of Automatic Enrolment came when HMRC (the U.K. tax authority) announced that it was to implement Real Time Information (RTI) in the same time frame (2011-12 and 2012-13). This initiative meant that employers would be assessing, deducting and paying employee income tax in real time (at every payrun) rather than at the tax year-end. This transformational programme had many advantages, but it did mean that payroll companies were adjusting their software to enable RTI at the same time that large employers were implementing Automatic Enrolment and many large employers had to implement both at the same time. RTI could not wait for the roll out of Automatic Enrolment to complete, and similarly Automatic Enrolment could not be delayed. The programmes ran in parallel. There was good cooperation between HMRC (who adjusted their roll out timelines to ease the pressure on large employers) and the Regulator who worked alongside HMRC to ensure consistency of messaging.

SCALE OF THE ROLL OUT TO SMALL AND MICROS AND UNCERTAINTY OF BEHAVIOURS

Sitting at the top of the Automatic Enrolment programme's risk register was the uncertainty around employer behaviours. It was expected that large employers (those with more than 250 employees) would largely behave in accordance with the new law. They might need help (see the section on complexity) but typically they would not wish to be in breach of the law, be fined, and risk the reputational damage that comes with it. Additionally 89% of private sector employers with more than 250 employees offered a workplace pension in 2011 and these could often be used for Automatic Enrolment).

In total there are approximately 45,000 large and medium sized employers (250+ and 50-249 workers respectively) and 1.3 million small and micro employers.

Table 3.1
Breakdown of U.K. Employer sizes

Size band	Approx number	Percentage
Large (250 + workers)	11,000	0.8%
Medium (50-249 workers)	34,000	2.5%
Small (5-49 workers)	540,000	39.6%
Micro (1-4 workers)	780,000	57.1%
Total	1,365,000	100%

Source: TPR data

Of these, only 23% had existing pension schemes in 2011, and many of these were 'shell' schemes set up through earlier legislation called 'stakeholder pensions'. These pensions were set up by employers (with five or more employees, because it was the law, but few joined them and fewer still kept making contributions).

An additional complication is that many of these employers are not employers in the traditional sense. They employ someone in the home, either as a domestic worker or as a personal care assistant ('carer'). In total it is believed that there are approximately 150,000-200,000 such employers with about 100,000 of them employing a carer. They would not respond to messages aimed at businesses.

The Pensions Regulator's challenge was to get the message to all employers irrespective of size and to tailor this message so that an employer with 100,000 employees knew what it had to do just as an employer of a carer did. The staging profile was an important lever for this segmented communication message, allowing The Pension Regulator (TPR) to focus first on the messages to the very largest employers and then adapt its messages for the smallest employers.

The Regulator's strategy is to educate, enable and enforce. It chooses to enforce only where employers have not responded to its education and enabling messages. We conducted detailed qualitative and quantitative research on all the messaging, both offline and online, to ensure that it was fit for purpose.

The key message that resonated with all employers irrespective of their size was "It's the Law". Change theorists would argue that in order to make major change happen, you need to identify the benefits of a change and be able to answer the question "What's in it for me?". A message focused on the benefits of pensions or the desirability of being a good employer may have met this challenge. However, employers were clear that this message would be patronising, and that the message that would resonate was the simple reminder that it is the law.

TPR also designed a direct mail campaign under which all employers receive five letters from the Regulator. The first is sent 12 months before the staging date of the employer and is the call to action; the second is sent six months before the staging date and calls on employers to choose a pension scheme; the third is in the month before staging and reminds the employer to complete its preparation; the fourth is in the month after and tells the employer what it must do to enrol its workers; the final letter is four months after staging and a month before the declaration of the compliance deadline and prompts the employer to comply to avoid a fine.

A key enabler to this campaign is the support that HMRC have provided. TPR receives a data feed from HMRC based on its Pay as You Earn (PAYE) records. This tells TPR who each employer in the country is and allows it to derive a staging date. TPR then informs the employer of the staging date. The employer can also look this up on TPR's website using a simple tool.

Nearly 75% of employers are triggered into taking action by one of TPR's letters.

For the largest employers with the most complex implementation challenges, TPR published detailed guidance of over 250 pages. This guidance was comprehensive and designed to turn the legislation into plain English. It also published complementary guidance to software providers.

Gradually TPR adjusted its guidance so that it was focused on medium-sized employers.

The year 2015 marked a major change in the programme. Instead of TPR continuing to evolve its communications to smaller and smaller employers, it took a different approach. It now focused on employers with one or two employees. It considered that if it could design a campaign and a set of tools that were fit for these employers, then they would also likely work for employers with 5 to 30 employees.

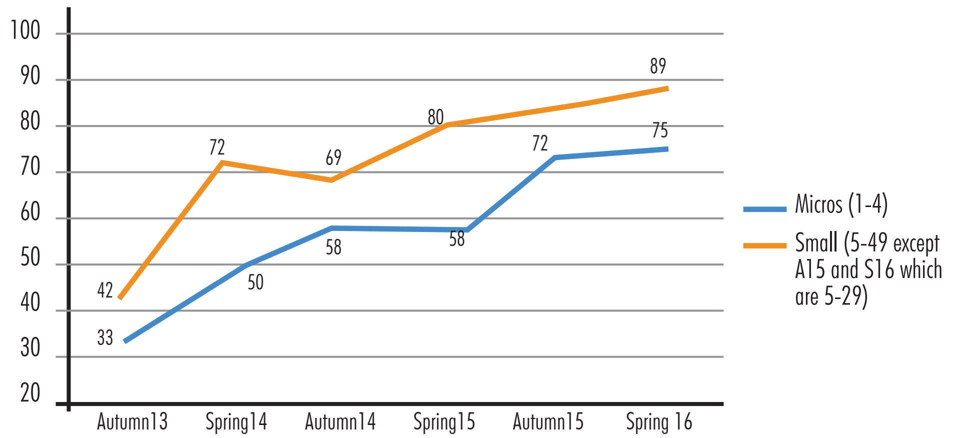
These employers told TPR that "we just want to be told what to do". TPR therefore devised a 'duties checker' that enabled employers to work out which duties applied to them and which did not. This filtered out employers with no workers who had no duties, those with no workers earning over the threshold of GBP 10,000 per year and who had duties but did not need to set up a pension scheme unless someone opted in, and the rest who had full duties. It also filtered those with domestic or care workers who got a customised journey designed specifically for them.

Alongside this, the Regulator introduced a simple five-step process which, if followed, allowed employers to become compliant. This process stripped out all the options that are available to employers and in so doing simplified the process substantially. Clearly employers could choose to follow a more complex journey and many have, often with the support of advisers. However, for employers who choose to manage the process for themselves and want to be told what to do, these five steps are sufficient.

Another challenge for the programme was to raise TPR's profile so that all employers had heard of it. HMRC is well known, and somewhat feared by employers. The Pensions Regulator was not. Only large companies, particularly with DB schemes, would have heard of TPR. But almost no small companies were aware of the Regulator.

TPR's letters acted as a major mechanism to increase such awareness, as did its campaigns through advisers and employer bodies. It also conducted advertising with the Department for Work and Pensions (DWP) using a memorable character which promoted both workplace pensions and the Regulator. Finally, TPR also ran radio campaigns with its brand as the strapline. These campaigns had real impact. The Figure 3.5 shows how the proportion of small and micro employers with some knowledge of TPR grew over time.

Figure 3.5
Knowledge of Pension Regulator by employer size



COMPLEXITY

The need for building a strong political and stakeholder consensus has been discussed above. This, however, also had a downside as the interests of many stakeholders needed to be reflected in the legislation. The U.K. has a relatively mature pensions system and to enable the new legislation to work alongside existing pensions practices for industry and employers, a large number of options were designed into the legislation including, but not limited to:

a. the concept of pay reference periods;

b. the need to reflect multiple earnings types and multiple ways to calculate the contribution levels;

c. the desire to allow as many people as possible to save, while allowing opt-outs and enabling opt-ins; and

d. widening the field of pension to allow all sorts of pension schemes to be used.

This complexity has meant that codifying the legislation into online processes was complex and, once done, difficult to change. For employers, this complexity has meant that preparation time has been longer than many would have wished.

Additionally, there is a plethora of legacy schemes and payroll providers. There are no single data standards between these two industries, which has meant that, simplistically, each scheme has had to provide a customised solution to work with each payroll provider and vice versa.

Two attempts were made to create a standard, with the 'PAPDIS' gaining some traction. However, the transfer of data between employers and pension schemes through payroll has been a major issue and continues to be so. Gradually, the issue is reducing as more schemes and payroll providers have established linkages and as more modern technical solutions (including APIs) are becoming established. However, this remains a cause of frustration for many employers, as also their payroll software providers and scheme providers. This issue is particularly acute in the U.K. as it has a long history of pensions, much of it in a pre-digital era. For new adopters, it should be possible to do away with these concerns if sensible steps are taken on data protocols.

FIVE KEY LESSONS LEARNED

A very clear and shared goal or vision – the programme is designed to get 8 to 10 million people saving or saving more. This clarity helps guide all decisions. It brings all the partners together with a single goal. From this simple, shared goal, the programme developed a small number of clear and long standing Critical Success Factors (CSFs). These are:

- The programme is able to commence within budget;
- NEST accepts all employers who choose the scheme, whilst offering low costs to members and remaining financially viable;
- Employers know about, understand, and comply with their duties;
- An increase in the number of those saving into a workplace pension; and
- Increases in the total amount saved in workplace pensions.

Having a very clear objective that is known by everyone within the programme has provided clarity at difficult times. It has also allowed the programme to consider how to make certain trade-offs. All of the programme team have worked on other programmes where the overreaching goal was not clear or where different partners have different ideas of what success is. Having a very clear shared sense of the objective is very important in a successful programme. This is echoed in the experience of other countries, highlighted in the book, and in the Outcomes Based Assessment Methodology for Pensions that puts clarity on long-run outcomes at the heart of the approach.[18]

Three delivery partners – having three delivery partners created some real tensions at times. This approach seemed to complicate delivery at the beginning. The fact that the different organisations came from different perspectives and saw problems and issues differently often led to decisions being slowed down or simply to disagreement. There was obvious tension in discussions and often hard negotiations. A good example of this was in the discussion about around implementation. The Department had a political imperative to get

[18] See "Outcomes Based Assessments for Pensions: A handbook" by William Price, John Ashcroft and Michael Hafeman, World Bank 2016

things done quickly, whilst NEST and the Regulator argued for more time. NEST wanted small employers to go first as they were less complicated, whilst the Regulator wanted larger employers to go first as they were more likely to comply with their duties.

The constant debates and conflicting views also had a number of advantages. Multiple discussion meant that all assumptions were challenged and undoubtedly led to better answers. It also meant that the programme did not suffer from "optimism bias". As all the parties had to agree to assumptions, if anything, the programme had a slight "pessimism bias" and has therefore outperformed in areas such as on-time compliance by employers and lower opt-out by individuals.

The key to success was to be clear about individual accountabilities This separation of accountabilities meant that each partner was able to deliver to its own core focus. Most importantly, each partner was responsible for its own area specialisation and for knowledgeable and specialist staff.

Importance of strong programme management – this was a complex implementation, with three core implementation partners and around 1.4 million target employers, and which would impose important changes on the pensions industry, payroll providers and business advisory community.

Strong programme management within the Department and in each of the delivery partners was essential. Both TPR and NEST decided to enter into major outsourcing contracts to support their processes. These contracts, and ultimately the third party suppliers, became critical to the success of the programme. Both TPR and NEST put in place top-quality contract management processes and both contracts have delivered very good outcomes.

At the heart of the programme management approach has been:

A clarity of goals and critical success factors

- Clear accountabilities between the three parties;
- Continuity of senior personnel;
- A strong and active risk management approach, with constant monitoring of the effectiveness of risk mitigations;
- Active stakeholder management;
- A realistic business case that did not suffer from optimism bias;
- Regular external reviews to keep the programme on its toes, and to provide reassurance that nothing was badly off track.

Test, Adapt and Change – where it was possible the programme tried to test processes and products before they went live. In addition, processes and changes were rolled out in phases rather than using a "big bang" implementation approach.

The staging profile was designed so that only a small number of employers were subject to the duties in the first phase (only four in the first month, though collectively they employed half a million workers), but by the end of the profile, 80,000-100,000 employers per month were subject to the new duties. This staging approach allowed all parties to test their capacity and ready themselves before they were tested at scale.

It was recognised that the challenges that small and micro employers would face would be completely different to those of larger employers. A pathfinder (test group) was therefore built into the roll out profile. This tested actual behaviours of micro-employers against their new duties, and also tested education material, processes, and systems before expanding volumes. Behavioural insight experts advised on these tests. The employers in the test group were subject to the duties six months prior to any other employers with less than 30 employees. This gave the programme time to learn from these employers and adapt its approaches. Some of the key learning from this was:

- Communications must be direct – "just tell us what to do"; a simple five step process was created for employers;
- Communications should be frequent – the Pensions Regulator writes five letters to employers starting 12 months before employer duties and ending with a letter just before deadline day;
- Employers need simple tools to help them to become compliant; and
- Some employers have specific needs and segmented communication was necessary (for example, an employer of one carer is very different to a florist employing two or three staff).

Educate and enable before enforce – or "prevention is better than cure". The Pensions Regulator's approach has been to help employers and their advisers to get it right by providing them with all the information they need, segmented to various audiences. It carries out comprehensive campaigns by writing to all employers in the lead up to each employer's duties, by e-mailing employers several times in the lead up to their duties, and by making available a range of tools for them. These tools include a 'know your duties date', a duty checker, an assessment tool that allows employers to know which workers to enrol, and the level of contributions. It also provides videos, case studies, as well as social media information.

The Pensions Regulator has a well-resourced and trained call centre available to provide telephone support to employers and to their agents. It also has a whistleblowing line available for employees who have concerns that their employer is not fulfilling its duties.

However, the Pensions Regulator made it clear that non compliance was not acceptable. It set out and published a compliance and enforcement strategy in which it described its approach to enforcement. It has taken the view that it is simply not fair on a worker if they are not provided with the pension that they are due in the law, and it is not fair competitively if one employer had an advantage by being non-compliant. It, therefore, uses its powers, including fining employers, to ensure that workers do get what is due to them. Interestingly, the Regulator innovated its approach to the use of fines as a result of the huge volume of employers involved in Automatic Enrolment, but did so within the same principles of educate, enable and enforce. This highlights the benefit of having clear regulatory principles to guide behaviour that can then be adapted to changing roles and circumstances on the ground.

The programme recognised early that automatic enrolment would not be a success unless the 'supply chain' to employers was also ready and able to support employers and provide them with the necessary products. The Pensions Regulator, therefore, put in place dedicated teams that support pension providers, payroll software providers (because for most employers, the bulk of the set up and ongoing processing is payroll-driven), accountants, bookkeepers, etc. It has information and guidance available on its website specifically for these groups.

Finally, the programme has supported all this activity with a substantial advertising campaign. For large employers this focused around the catch line "We're all in", and for smaller employers around a character called 'Workie' around the catch line "Don't Ignore the Workplace Pension".

WHAT WOULD WE DO DIFFERENTLY?

Whilst the programme has been very successful to date, there are still a number of areas that we would have liked to have handled differently. These, of course, all have the benefit of hindsight but it is an interesting exercise and challenge to think of what we could have done better.

- **Complexity** – some areas of the policy could have been simpler. The programme could have challenged itself more on having simpler solutions to problems and imparting the advantages of these to employers and individuals. Not all areas of the legislation are intuitive for employers, particularly for small employers. In simplifying the legislation for the future, it will be important to find solutions that match other business processes that an employer is familiar with. In 2017, there is a year-long review of Automatic Enrolment and the question about whether the policy can be simplified will be a central part of that review.
- **Industry regulation** – this has developed throughout the programme. The regulation of trust based DC schemes in the U.K. is not traditionally strong. Historically, they have not represented a great risk as there was often an important link between an employer and a scheme, which led to good governance and oversight. DC pensions offered by insurance companies were subject to strong regulation, but Trust based occupational schemes were not subject to the same level of oversight. This was less of an issue as these tended to be large schemes that were established by larger

employers. The care and attention of the trustees, who are required to act in the best interests of members, meant that they were generally well run. And they were frequently large schemes where they had the resources and scale to develop expertise.

There have been two significant reforms to improve industry regulation since the start of Automatic Enrolment. In 2015, after much debate, the government placed a cap on charges on schemes used for automatic enrolment of a maximum of 0.75% of AUM. Whilst there was little evidence that many people were paying more than this under automatic enrolment, it seemed important to give people certainty that there would be a maximum charge for these schemes. This introduction of the charge cap allowed the government to provide greater assurances that consumers would not suffer losses on account of high fees and charges.

In addition, the introduction of Automatic Enrolment has seen a rapid growth in what are known as "master trusts". These are trust-based DC schemes for multiple employers. NEST is set up as a master trust. Many of the large master trusts have very high levels of governance and oversight. However, with the rapid growth in the number of such Trusts being set up, there are concerns that not all of them have such high governance standards.

There is currently legislation going through Parliament to introduce a fit and proper test for those who run these schemes and to put in place capital adequacy requirements. This new regime should be fully in place by 2018. Both changes could have been part of the original reform although it is not clear whether it would have been possible to achieve consensus around these changes.

In terms of lessons for other countries, perhaps the key one is accepting that it is not possible to get everything right at the front-end and that there will always be a need to adjust the policy based on implementation experience. It is difficult of course to balance this against a need for stability as the reforms are implemented.

- **Choosing a scheme** – this is the area that most small and micro employers have found difficult. While most of the processes can be automated for employers through the payroll, a decision on the choice of the pension scheme is not possible to automate.

  The vast majority of small and micro employers did not have a pension scheme before Automatic Enrolment and had no experience with choosing a scheme. This presented a potentially significant burden on employers, and a real concern by them that they may make the wrong choice. Some employers took advice from independent financial advisors, but this advice could often be expensive. Some chose NEST simply because it was "government backed".

  To address this issue, the Pensions Regulator decided to publish a list of schemes that could be used by small and micro employers. Schemes had to apply to be on the list based on criteria set by the Regulator including that the scheme should be open to all employers irrespective of their size and the value of their business, and that the scheme would either be a Group Personal Pension (a type of contract base pension) regulated by the Financial Conduct Authority or a master trust whose standards of governance and administration were independently audited in line with standards agreed by the Institute of Chartered Accountants of England and Wales and the Pensions Regulator.

While this list has helped, it is still the single biggest challenge for employers.

SUMMARY

The U.K. pension reforms have been very successful to date. They have increased pension coverage amongst the group they were designed to help and have led to an increase in savings in pensions in the U.K.

There still remain a number of challenges for the reforms as they continue to roll out. In particular to reach the remaining hundreds of thousands of employers that are yet to reach the date on which the reforms apply to them, and to increase contributions for employers and employees to the 8% rate.

The reforms are generally seen as very positive. The implementation to date has gone relatively smoothly, but that should not be seen as a sign that these are simple reforms. The success of the implementation is due to the hard work of many people over a long period of time, not just within the programme but within employers and pension schemes throughout the country.

There is significant hope that by the end of the programme the long term decline in pension savings in the U.K. will be reversed and that many people who were previously excluded from pensions will have the opportunity to build up savings for their retirement.

The reforms show how a careful analysis of the issues, a realistic understanding of human behaviour when it comes to savings, allied to a rigorous approach to building consensus and supervising an efficient pension value chain were able to deliver a historic improvement in the U.K.'s pension outcomes and reverse decades of previous decline in pension coverage.

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