Aviva's Auto Enrolment Pre-Review

November 2016

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"Our unwavering focus is to help people enjoy a secure and prosperous retirement"

Foreword

We're living long lives and healthier ones. But this creates a challenge; how do we support an ageing population? The British monarchy began the tradition of sending telegrams to centenarians in 1917. That year, King George V sent 24 telegrams. This year, the Queen will send over 10,000.

Auto enrolment is one way we can make a real difference. We have not yet completed the rollout for all small and medium businesses – but it has already proved hugely successful. But there is no time for complacency and we still face the challenge of people not saving enough for their retirement. So we need to build on the success we've had so far and work out exactly how we're going to crack this pension savings challenge. That's why Aviva has launched this Pre-Review of auto enrolment to help inform the Government's statutory review next year.

When I think about just how important this is, I think of people like Sue. Sue is a part-time HR Manager and lives in Stratford with her husband. She has two grown up children and wants to retire when her first grandchild is born so that she can spend more time with her family. But reality for Sue is very different from her aspiration. She has a small pension pot and she doesn't know what other savings she can use to help her retire. So our efforts should be absolutely focused on helping Sue.

At Aviva, we serve more customers in the UK than any other insurer. We're in business to support our customers - millions of people like Sue - as they prepare for retirement and help them enjoy it when they do. They trust us to look after their pension savings and we want to help them turn their aspirations into reality. We want to help them think carefully about what they're trying to achieve, how much to put aside at different stages of their lives and how long their retirement income might need to last.

Aviva's Auto Enrolment Pre-Review is our opportunity to reflect on the lessons we can learn so far and to help make the future of retirement saving in this country a real success. Our unwavering focus is to help people enjoy a secure and prosperous retirement. Our recommendations in this report are how we might all do that in practice.

Andy Briggs
CEO, Aviva, UK Life

"Over 250,000 employers have successfully implemented the system and more than 6 million new savers are now contributing to a workplace pension"

Executive Summary

Introduction

There has been a significant focus on pensions in recent years and the Government has initiated positive steps to addressing the societal challenge of supporting an ageing population. There is plenty of good news. Auto Enrolment (AE) was first introduced in 2012. Since then, over 250,000 employers have successfully implemented the system and more than 6 million new savers are now contributing to a workplace pension. Opt-out rates have remained stable with fewer than one in ten opting out[1]. When complete, all employers in the UK will provide a workplace pension. Prior to AE, 86% of employers did not offer workplace pensions or held empty pension 'shells' with no members[2].

This transformation needs to be acknowledged. AE has raised the understanding of pensions across society but its roll out is far from complete.

More importantly, we are still faced with a nation that is under-saving. Complacency is not an option and we must all work together to provide security for peoples' futures and build on the success of AE.

The last formal review of AE was in 2010[3]. Since then, AE has gone live, and we have had the new state pension, acceleration in the state pension age, pension freedom and choice and the new national living wage. The 2017 Government review of AE comes at a good time - we explain why in our comment on DWP's AE evaluation strategy.

SOURCE: 1. Department for Work & Pensions Employer's Pension Provision Survey 2015 I 2. Making Auto-enrolment work – a review for the Department for Work & Pensions, October 2010 I 3. Making Auto-enrolment work – a review for the Department for Work & Pensions, October 2010

Aviva's 10 steps to AE success

To help the Government with its review of AE in 2017 and plan the programme's future, we have set out where we at Aviva believe AE policy should go next. Our recommendations cover different aspects of potential reform. They are intended to provoke debate but also be realistic.

Aviva's 10 steps to AE success aim to build on the best, learn from abroad and go with the grain of success that comes from AE so far. We have looked at publicly available data, and conducted our own research and modelling. But the thinking doesn't end here and we would welcome comments and suggestions.

Adequacy

Current average contribution levels are not where they need to be to provide adequate replacement rates in retirement. To move people towards an adequate income in retirement, our recommendations are:

ONE. Phase towards 12.5% contributions by 2028

TWO. Adopt a flat rate of tax relief – save 2 get 1 free – and rename as a 'savers' bonus'

Scope

There are large parts of the population not captured by AE and they risk facing a significant shortfall in their retirement savings. To bring more people under the scope of AE, our recommendations are:

THREE. Capture multiple job-holders

FOUR. Explore options to capture the self-employed

FIVE. Remove the upper enrolment ceiling of the state pension age to encourage a longer working life

Consolidation

DWP estimated in 2011 that people will have on average 11 employers over their working life, and many will have more, meaning they could end up with multiple private pensions by the time they retire and have difficulty keeping track of their money. The new Pensions Dashboard will make a positive contribution in this area. In addition to the Dashboard, our recommendations are:

SIX. Officially encourage consolidation of small pension pots of £10,000 or less

SEVEN. Permit "without consent" transfers of contract-based workplace pensions, so long as savers are no worse off

Engagement

There continues to be strong evidence of a lack of saver engagement. To help make it easier for individuals to engage with their savings and plan for their retirement, our recommendations are:

EIGHT. Increase the eligibility threshold to £10,400 and lower the contribution threshold to £5,200 so that individuals can easily understand when they will be enrolled (once they earn more than £200 per week) and how much they will pay (contributions due on earnings over £100 per week)

NINE. Adopt Aviva's three rules of thumb:

- 40 year rule: Aim to begin saving at least 40 years before your target retirement date
- 12.5% rule: Aim to save at least 12.5% of your monthly salary towards your retirement
- 10 times rule: Aim to have saved at least 10 times your annual salary by the time you reach retirement age

TEN. Encourage the digitisation of pensions through government policy and regulation and a minimum level of digital functionality

Introduction

The success of AE so far is clear and the figures prove it – 6.7m employees have been auto enrolled to date – that's 75,000 London buses full of people (it's enough to fill every football and rugby stadium in the UK one and a half times over) - and over 250,000 employers have completed the process of enrolling their employees[4].

Recent government data challenges the perception that the younger generation are living for today and neglecting the need to save for their future. Under 35s now make up 34% (or 2.7 million people) of all contributors to personal pensions. This is the highest number since records began in 2001, and up a staggering 30% on the previous year (2013-14). The under 35s are arguably leading the way in the UK's pension revival. Participation in occupational pensions is also showing strong recovery, with active membership now at levels not seen since 1983[5].

But the journey is far from complete. As we write this, small and medium businesses are still in the process of enrolling their employees and contribution levels are not where they need to be to provide adequate replacement rates in retirement.

In its most recent Fiscal Stability Report[6] (published prior to the EU Referendum), the Office for Budget Responsibility stressed that "an ageing population will put upward pressure on public spending". They project total non-interest public spending to rise from 33.6% of GDP in 2019-20 to 37.8% of GDP in 2064-65, in response to our ageing society. This 4.2% increase is "equivalent to £79 billion in today's terms". To put this figure in context, £79 billion is what the Government (central and local) currently spends on defence, transport and agriculture combined.

The scale of the challenge facing the UK is clear. The need to rise to this challenge is undeniable.

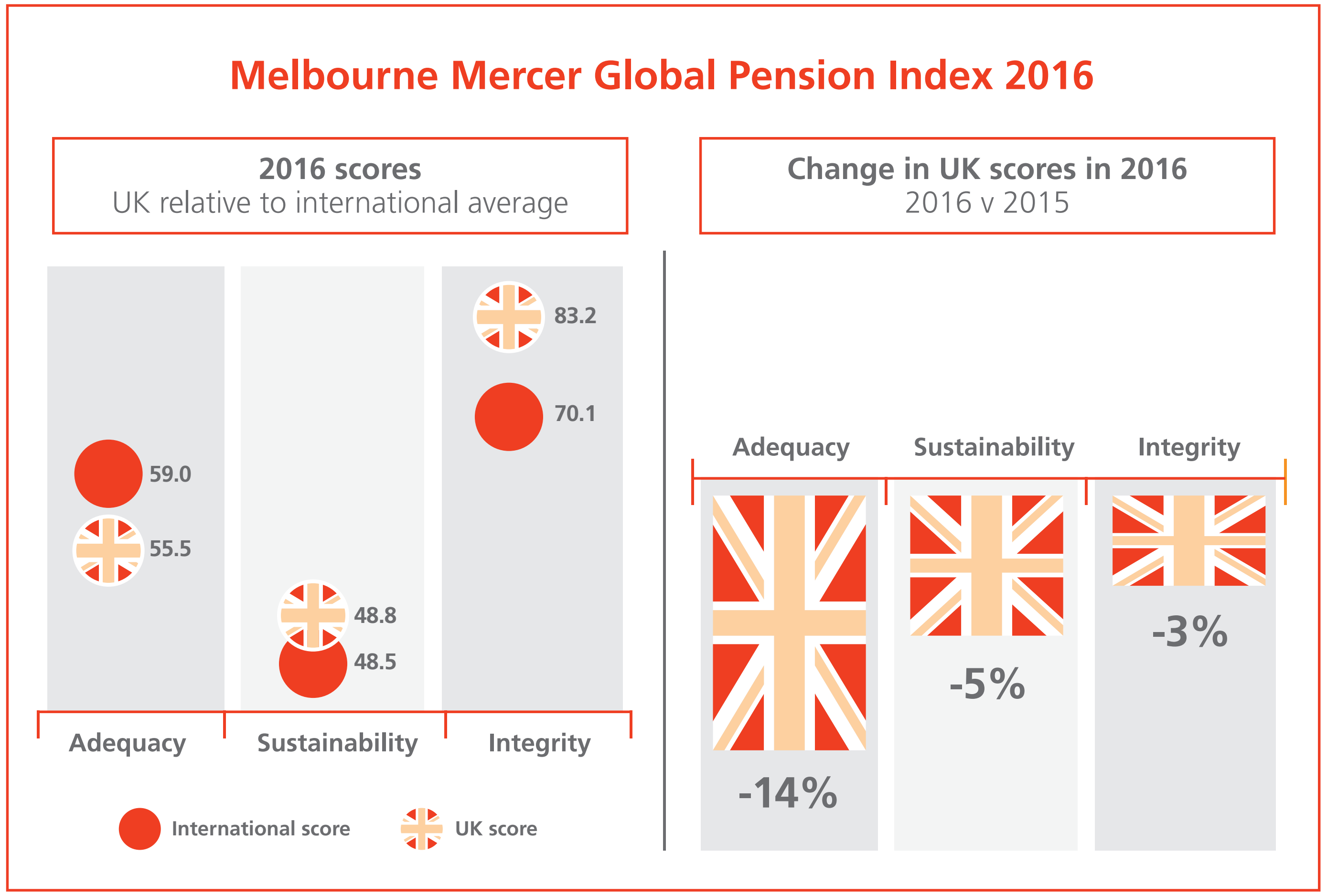
2017 will mark 15 years since the original Pensions Commission was established, giving birth to the concept of AE, and 5 years since the reforms went live. We now have real-life experience of over 250,000 employers and 6 million employees on which to guide the next phase of AE. Change is not easy and the temptation to delay can be strong but 2017 is the right time to act.

All evidence indicates that the processes that underlie the reforms are robust and well understood. They have been tested with thousands of employers and millions of employees. The failure rate amongst employers is tiny and the vast majority of employees have chosen to stay involved. Despite strong economic headwinds, support for AE remains strongly positive.

All evidence also indicates that we have further to go. The need to deepen and widen AE is articulated by Aviva in this report and other sources echo this view.

The respected Melbourne Mercer Global Pensions Index is now in its 8th year. It analyses and ranks the strength of pension systems around the world. Worryingly, the strength of the UK pensions system is declining. In its latest report, the UK's ranking has fallen from 9th in 2015 to 11th. Our grading has been downgraded from a B to a C.

Mercer analyses systems through three lenses – adequacy, sustainability and integrity. It is adequacy that is pulling the UK down. Adequacy in the UK is below the international average and adequacy has witnessed the fastest fall across all three metrics over the past year.



The further the UK falls, the further the UK will have to climb. AE is one of our best means of climbing, and we must begin doing so in 2017. At Aviva, we want to be part of the solution and we hope our 10 steps to AE success will build on the great work done to date in helping people enjoy a secure and prosperous retirement.

Source: 4 https://www.gov.uk/government/news/the-number-of-people-saving-as-a-result-of-automatic-enrolment-to-hit-10-million I 5 Office for National Statistics, Occupational Pension Schemes Survey, UK: 2015 I 6 Office for Budget Responsibility, Fiscal Sustainability Report, June 2015

DWP automatic enrolment evaluation – We give it 5-out-of-8

An AE evaluation strategy was developed by a cross Government steering group that included representatives from across DWP, NEST, the Pensions Regulator, HM Treasury, the Office for National Statistics and the (then) Department for Business, Innovation and Skills.

Eight questions were listed to evaluate AE against its initial policy ambitions. It must be remembered that the initial policy ambition was to provide a platform on which private retirement saving could be built. AE was not initially designed to ensure, on its own, that all achieved their desired income in retirement.

From this perspective, Aviva gives AE a score of 5-out-of-8, when judged against the 8 evaluation questions.

Aviva's review gives confidence that the system of AE is robust, but a further evolution is needed – especially in the areas of participation and adequacy of contributions.

The score however gives Aviva confidence that 2017 is the right time to agree the next phase of AE.

1: Were the Workplace Pension Reforms delivered to the planned timescales, and within budget?

As at September 2016, 256,888 employers have confirmed they have met their AE duties and 6.7 million people have been auto enrolled[7]. Since first introduced in 2012, only 741 of the strongest "escalating penalty notices" have been issued for non-compliance. This represents 0.3% of all employers[8].

2: Does NEST accept all employers who choose the scheme, while offering low costs to members and remaining financially viable?

Over 180,000 employers have signed up to NEST, meeting the needs of over 3 million employees[9]. NEST now routinely services 800 new employers per day[10]. The only shadow hanging over this question is the long term nature of the Government's loan.

3: Do employers know about, understand and comply with their employer duties?

The latest data from the Pensions Regulator shows a rise in compliance warning notices as more small employees come on stream[11]. There is clearly no room for complacency, but we should take confidence from the overwhelming number of employers who are meeting their AE obligations. Amongst the small and micro employers enrolling for the first time today, there is an awareness score of 96% and 90%, respectively[12].

4: To what extent do the Workplace Pension Reforms increase the number of individuals saving in workplace pensions?

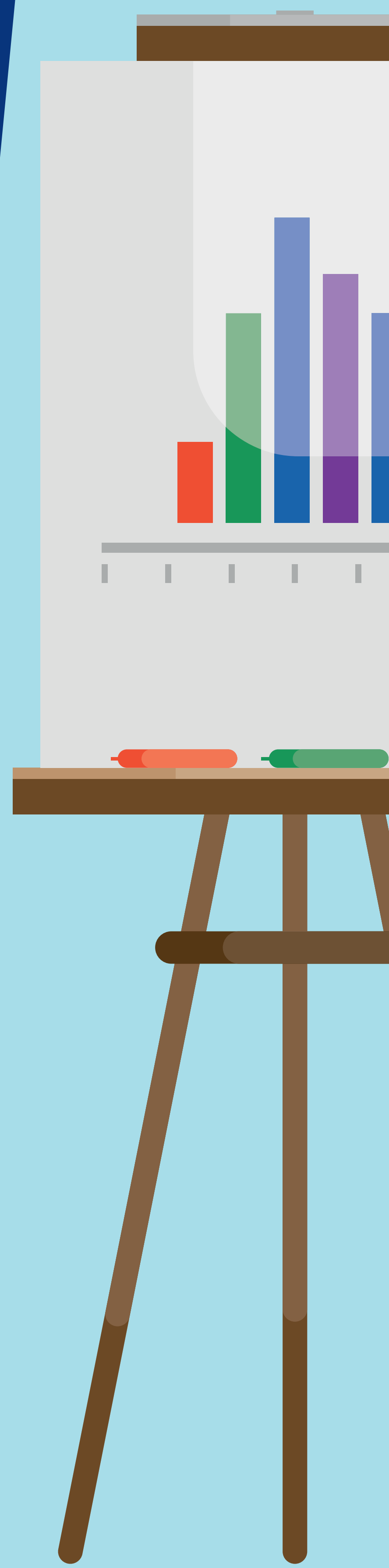
This is a mixed picture. As at September 2016, 6.7 million eligible workers have been auto enrolled[13]. This is out of an estimated target group of 11 million workers[14]. Latest official data shows opt-out rates averaging at 9%[15]. This is significantly below the "one-in-three" that was routinely anticipated prior to the introduction of AE.

Despite these strong numbers, DWP also estimate that one-quarter of all workers are ineligible for AE, and this excludes all self-employed. The ineligible workers population rises to 37% amongst women, 33% amongst workers with a disability and 28% amongst black and ethnic minority (BME) workers. AE is currently not the answer for many millions of people.

5: To what extent do the Workplace Pension Reforms increase the amount being saved in workplace pensions?

As with question 4, question 5 is also a mixed picture. Of the 11 million people in the eligible target group for AE, DWP estimate that 10 million will be newly saving or saving more as a result of AE by 2018. By 2019/20 it is estimated that there will be £17bn extra workplace pension saving per year as a result of AE.

The above numbers are strong, but the Pension Policy Institute (PPI) has estimated that even with the reforms only 50% of median earners, saving from age 22 (assuming minimum contributions), will achieve the same standard of living in retirement that they experienced in working life. The PPI also report that median employee contributions are falling as AE is introduced to new savers[16]. The latest data shows that for both employees and employers the minimum contribution level has become a target rather than a baseline on which to build[17]. The current target of 8% may have been sensible for the initial introduction of AE but it is clear this minimum acts as a powerful signal to employers and individuals and leads to contribution rates which are insufficient for the majority.



Source: 7. Automatic Enrolment, Declaration of Compliance Report, July 2012 – end September 2016 I 8. Automatic Enrolment, Compliance and Enforcement, Quarterly Bulletin 1 July to 30 September I 9. NEST Corporation Annual Report and Accounts, 2015-16 I 10. https://www.nestpensions.org.uk/schemeweb/NestWeb/includes/public/news/Its-your-turn-now-as-1.html I 11. TPR Automatic Enrolment, Compliance and Enforcement Quarterly Bulletin 1 July – 30 September 2016 I 12. Automatic Enrolment, Commentary and Analysis: I 13. April 2015 – March 2016 Automatic Enrolment, Declaration of Compliance Report, July 2012 – end September 2016 I 14. DWP, Workplace pensions: update of analysis on automatic enrolment 2016 I 15. DWP, Employers' Pension Provision Survey 2015 I 16. PPI The Future Book: unravelling workplace pensions, second edition 2016 I 17. ONS Annual Survey of Hours and Earnings Pension Tables: 2015 Provisional and 2014 Revised Results I

6: To what extent is delivery of the Workplace Pension Reforms achieved with a minimal burden on employers?

UK employers deserve recognition and credit for their contribution towards the success of AE to date. Prior to the introduction of AE, only 14% of employers offered a workplace pension[18]. Given the current low rate of non compliance we can reasonably expect this figure to rise towards 100%. DWP research identified that AE had (understandably) increased overall administrative costs for 62% of employers[19]. However, as reported above, there is no evidence of significant employer compliance failure. Aviva's own research identified that only a small minority of employers (10%) are not in favour of AE[20].

7: How has the pensions industry reacted to the Workplace Pension Reforms?

All evidence and data (see above) suggests the pensions industry's reaction to the reforms has been positive. Worries about NEST being the only provider in the small scheme market have proved to be unfounded with a number of providers choosing to participate, ensuring all employers have a choice when it comes to placing their scheme.

The industry has accommodated an Office of Fair Trading study, an Independent Project Board audit, the implementation of a charge cap, the implementation of independent governance committees, a new state pension and the transformational introduction of new pension "freedoms" at retirement. Governance of the growing master-trust market will be strengthened as part of the Government's new Pensions Schemes Bill.

8: What are the wider economic impacts of the Workplace Pension Reforms?

DWP analysis agrees that the reforms will have a positive impact on the health of privately funded incomes in the long-term. The analysis is understandably shaped by a number of assumptions – including wage growth, contribution rates, job churn, investment growth, employment, annuities and participation. The DWP's conclusion is that the reforms could boost median weekly private pension income from anywhere between £20 and £261 per week by 2070[21]. A closer look suggests that the £261 figure is powered, at least in part, by an assumed average employee contribution of 5% and an average employer contribution of between 8% and 9%. There is no evidence of this average materialising. If anything, averages are falling. Aviva estimates that, while positive, the impact of AE must be towards the lower end of DWP projections.

Source: 18. Making Auto-enrolment work – a review for the Department for Work & Pensions, October 2010 I 19. DWP: Automatic Enrolment Evaluation Report 2015 I 20. http://www.aviva.co.uk/media-centre/story/17607/workplace-benefits-boost-forecast-for-2016-as-one-/ I 21. DWP: Automatic Enrolment Evaluation Report 2015

Aviva's 10 steps to AE success

ADEQUACY

ONE
Phase towards 12.5% contributions by 2028

TWO
Adopt a flat rate of tax relief – save 2 get 1 free – and rename as a 'savers' bonus'

SCOPE

THREE
Capture multiple job-holders

FOUR
Explore options to capture the self-employed

FIVE
Remove the upper enrolment ceiling of the state pension age to encourage a longer working life

CONSOLIDATION

SIX
Officially encourage consolidation of small pension pots of £10,000 or less

SEVEN
Permit "without consent" transfers of contract-based workplace pensions, so long as savers are no worse off

ENGAGEMENT

EIGHT
Increase the eligibility threshold to £10,400 and lower the contribution threshold to £5,200 so that individuals can easily understand when they will be enrolled (once they earn more than £200 per week) and how much they will pay (contributions due on earnings over £100 per week)

NINE
Adopt Aviva's three rules of thumb:

- **40 year rule:** Aim to begin saving at least 40 years before your target retirement date
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TEN
Encourage the digitisation of pensions through government policy and regulation and a minimum level of digital functionality

Adequacy

Before considering reform of AE it is worth reminding ourselves what the policy was originally designed to achieve.

The Pension Commission, led by Lord Turner, gave birth to the concept of AE. It identified that millions of people were not saving enough to deliver the income in retirement they would like. They saw reform of the state pension and an increase in private saving as the means of addressing this weakness. A new state pension was introduced in 2016, and AE was launched in 2012 as a means of increasing private savings.

The Commission concluded that "incremental increases in voluntary saving alone would be insufficient, whilst compulsion risks forcing some people into saving more than they need to[22]". They recommended instead that the State should "strongly encourage people to save in private pension provision, whilst also providing a platform on which to build this saving". AE was to be the platform on which people could build their savings.

The Commission also agreed a target gross replacement rate of 45% as a minimum target for median earners. They calculated that, to reach this level, a median earner would need to save around 8% of earnings for 40 years.

It is worth noting that the Commission's final recommendation was for a system on which further private saving could be built. AE alone was not intended to satisfy everyone's retirement income aspirations but this message seems to have been diluted. Average contribution rates in DC pension schemes have consistently fallen since 2012[23] as employers and employees have adopted the minimum level of contribution as a default contribution level. More people are saving for retirement at inadequate levels than at any time in recent history.

[22]**Source:** 22. Making Auto-enrolment work – a review for DWP, October 2010 I 23. PPI The Future Book: unravelling workplace pensions, second edition 2016

Increasing contributions

Current rules require a minimum contribution of 2% of an eligible employee's banded salary, and at least 1% of this must come from the employer. From April 2018, the minimum rises to a total of 5%, of which at least 2% must come from the employer. From April 2019, the minimum rises to 8%, of which at least 3% must come from the employer.

There is general agreement that contributions of 8% are not enough. In 2013, the PPI carried out modelling which showed that even if an individual on median income started saving at 22 he or she had less than a 50% chance of hitting their replacement income in retirement[24] if they contributed the minimum.

The adequate replacement rate can be defined as the percentage of working income needed in retirement to maintain an individual's accustomed standard of living.

It is common for analysis to assume a target replacement rate of around 70% of working income. Indeed, the Organisation of Economic Cooperation and Development (OECD) consider it reasonable to use a gross 70% rate as the adequate retirement income benchmark for the average individual. This would allow the individual to enjoy a standard of living in retirement that is similar to the standard he or she enjoyed prior to retirement[25]. Aviva has used this figure as a guide for its analysis, but has varied the replacement rate to reflect the needs of different income groups.

Our analysis uses net 67% as the replacement rate for those with a typical annual income. However, we have assumed those on lower incomes would need a higher net replacement rate to cover essential costs. Conversely, those on higher incomes could satisfy their essential needs with a lower net replacement rate.

We have used a net[26], not gross, replacement rate, to avoid National Insurance biasing results.

Source: 24. PPI Automatic Enrolment Report 1 I 25. OECD Private Pensions Outlook, 2008 I 26. Net replacement rate excludes national insurance from the salary. NI is not paid in retirement. This approach is to avoid NI exaggerating the size of the income needed to match the target replacement rate.

Based on current annuity rates and including a full state pension, our calculations show that 8% isn't enough to reach adequate replacement rates unless you are a very low earner. For those on the lowest incomes, the state pension can be sufficient to deliver a target replacement rate.

The table (right) shows the percentage of salary that set income levels would need to save from set ages to achieve set net replacement rates.

Our analysis of incomes up to £40,000 each year covers 80% of the working population.

A range of saving rates are needed to achieve the target replacement rates across all other income levels - from 10.75% for younger savers on £20,000, up to over 50% for some who take no action until aged 50. This analysis is based on various cautious assumptions, including use of guaranteed annuities at retirement and no assumption is given for assets that an individual may have at retirement, beyond their DC pension savings.

Our conclusion is that 8% is a positive first step, but it is clearly inadequate. There is then a judgement call as to how far and how fast this rate should be raised.

We hold on to the original intention that AE's purpose is to provide a "platform" on which further private savings can be built. Its purpose has never been to solve all retirement challenges on its own.

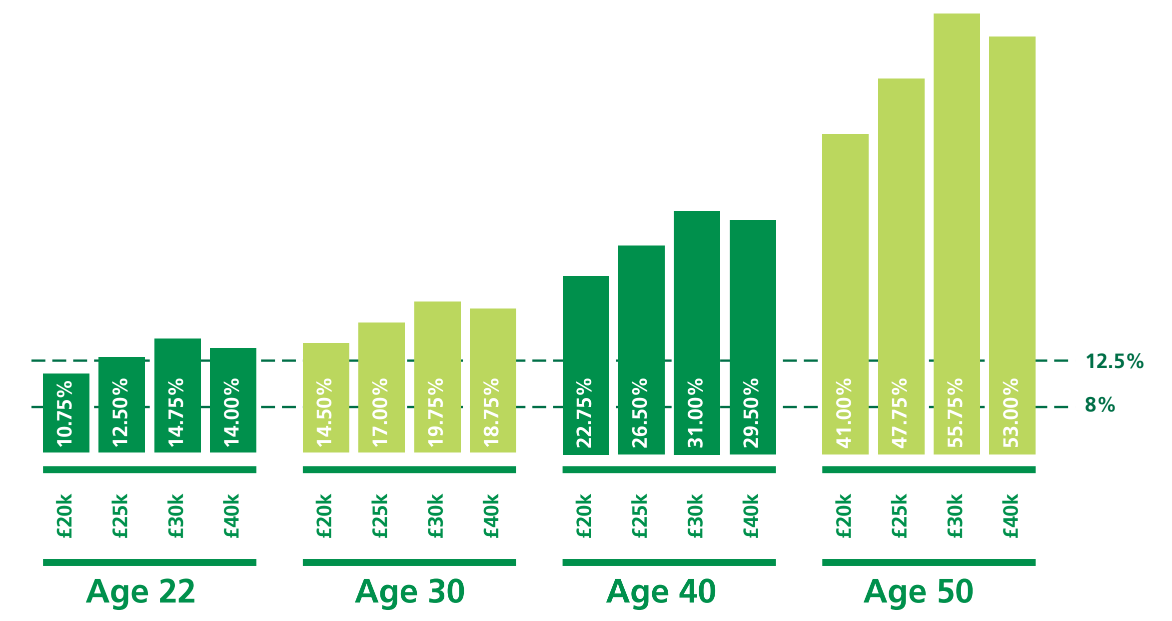
This belief restrains our desire to push the minimum too high. For this reason, we advocate phasing towards 12.5% contributions by 2028.

Gross salary today	Net salary today	Target replacement rate (% of net income)	Target net income in retirement	Gross income required in retirement (assuming all income is taxable)
£10,000	£9,767	80%	£7,814	£7,814
£20,000	£16,767	70%	£11,737	£11,921
£25,000	£20,167	67%	£13,512	£14,140
£30,000	£23,567	67%	£15,790	£16,988
£40,000	£30,367	60%	£18,220	£20,025

Percentage of banded earnings needed to reach replacement rate at age 67

Gross salary	Age 22	Age 30	Age 40	Age 50
£10,000	0.00%	0.00%	0.00%	0.00%
£20,000	10.75%	14.50%	22.75%	41.00%
£25,000	12.50%	17.00%	26.50%	47.75%
£30,000	14.75%	19.75%	31.00%	55.75%
£40,000	14.00%	18.75%	29.50%	53.00%

Percentage saving required to achieve target replacement rate



Targeting 12.5% by 2028 reflects the urgent need for action, while phasing the impact on employers and employees.

RECOMMENDATION: Phase towards 12.5% contributions by 2028

The current minimum of 8% will be reached in 2019. We then propose a freeze of four years, until 2023, to allow this level to embed, and allow advance preparation for the subsequent increases.

Between 2023 and 2028 we propose employer and employee contributions each phase towards 5%. These contributions should be complemented by a new form of tax relief - "save 2 get 1 free".

In the table below we have worked under the assumption that this would come into force in 2020 and we have articulated this new form on page 19.

Year	Employer Net	Employee Net	Savers' Bonus / Tax relief added	Total
2019	3	4	1	8
2020	3	4	2	9
2021	3	4	2	9
2022	3	4	2	9
2023	3.5	4	2	9.5
2024	4	4	2	9.5
2025	4	4.5	2.25	10.75
2026	4.5	4.5	2.25	11.25
2027	4.5	5	2.5	12
2028	5	5	2.5	12.5

Whilst we acknowledge the potential challenges of increasing contributions for business and employees, perhaps through restricted pay rises, we believe this is a challenge we have to face.

We explored whether compulsion or mandatory auto-escalation could help solve the adequacy problem but believe neither are appropriate.

The low levels of opt-outs so far do not justify the imposition of compulsion. In line with freedom and choice at retirement, we believe people should retain freedom and choice while saving. The ability to opt out is also a big component in mitigating some of the risks associated with enrolling some people who may rationally decide that pension savings is not right for them based upon their personal circumstances.

A mandatory upgrade of systems to implement auto-escalation could be imposed but would be complex and expensive to implement. A lack of clarity over future costs and the possible introduction of perverse incentives to cap pay rises risks further complication and disengagement. We believe resources should be focused on phased increases of minimum contributions to 12.5% by 2028.

Employer engagement is a stand out story of success from the current system. Over 250,000 employers have implemented the new reforms and by 2018 we will have transformed ourselves from a situation where workplace pensions were active in only 14% of employers in 2011 to a situation where they will be active in 100%.

Throughout our research, we have been encouraged by the support behind AE - 70% of our small and medium business customers and 93% of our large business customers support the policy. Only 13% of our small and medium business customers and 2% of our large business customers said they were "not supportive at all" of AE. We also found that employers care about the impact of retiring later - 67% of our large business customers expressed concern that an employee may not be able to afford to retire and the impact that could have on their business.

Individuals also clearly understand the value of employer contributions and are willing to increase their own contributions. Our consumer research shows that 75% of people would be willing to increase their pension contribution if their employer's contribution also increased. Even more encouragingly one in three said they would be willing to contribute 10% (or more) of their salary into their pension. We also tested our recommendation with large employers - 68% said they would be willing to contribute more than the minimum 2019 contribution of 3%. When asked how much they would be willing to contribute, 58% said either 5% or 6%. We tested this recommendation with small and medium employers too – 42% said they would be willing to contribute more than the minimum. We are encouraged that on average, more than one in two employers would be willing to contribute more than the minimum 2019 contribution of 3%.

In discussions with employers and financial advisers, both thought the target has to be seen as achievable and the discussion focused around gradual increases. We understand that this may be a challenge for all businesses but with sufficient time to plan, 12.5% is an achievable target – the 2008 Pensions Act was brought about at the height of economic and business instability but the policy worked as businesses were given sufficient time to plan for the introduction of AE.

Employers in support of AE:

70% *SMALL AND MEDIUM SIZE BUSINESS EMPLOYERS*

93% *LARGE BUSINESS EMPLOYERS*

The international experience – phasing towards higher contribution rates

Australia is often held up as a country that encouraged the UK's adoption of AE. The Australian occupational pensions system is called the superannuation, or just "super". Unlike the UK's AE system, it is a compulsory pension system with no opt-out. And unlike the UK's AE system, all compulsion lies with the employer, not the employee.

The Australian system was launched in 1992, with an initial minimum contribution of 4% of salary (or 3% if the employer's payroll was Aus$1 million or less). Over the next decade this steadily rose by 1% every two years, reaching 9.0% in 2002. Further increases of 0.25% in 2013 and 2014 mean that contributions are now 9.5%.

The next phase was set to begin increasing again from 2018, but Parliament has agreed to postpone this until 2021. The current system is intended to eventually reach 12% in 2025.

In the initial phase, the Australian system increased by 5%, from 4% to 9% over a period of 10 years – i.e. 0.5% each year. The full increase of 8%, from 4% to 12%, will conclude over a period of 33 years – i.e. 0.24% each year on average.

Aviva is proposing the UK follows Australia's lead, but using a revised system of pension tax relief to reach 12.5%.

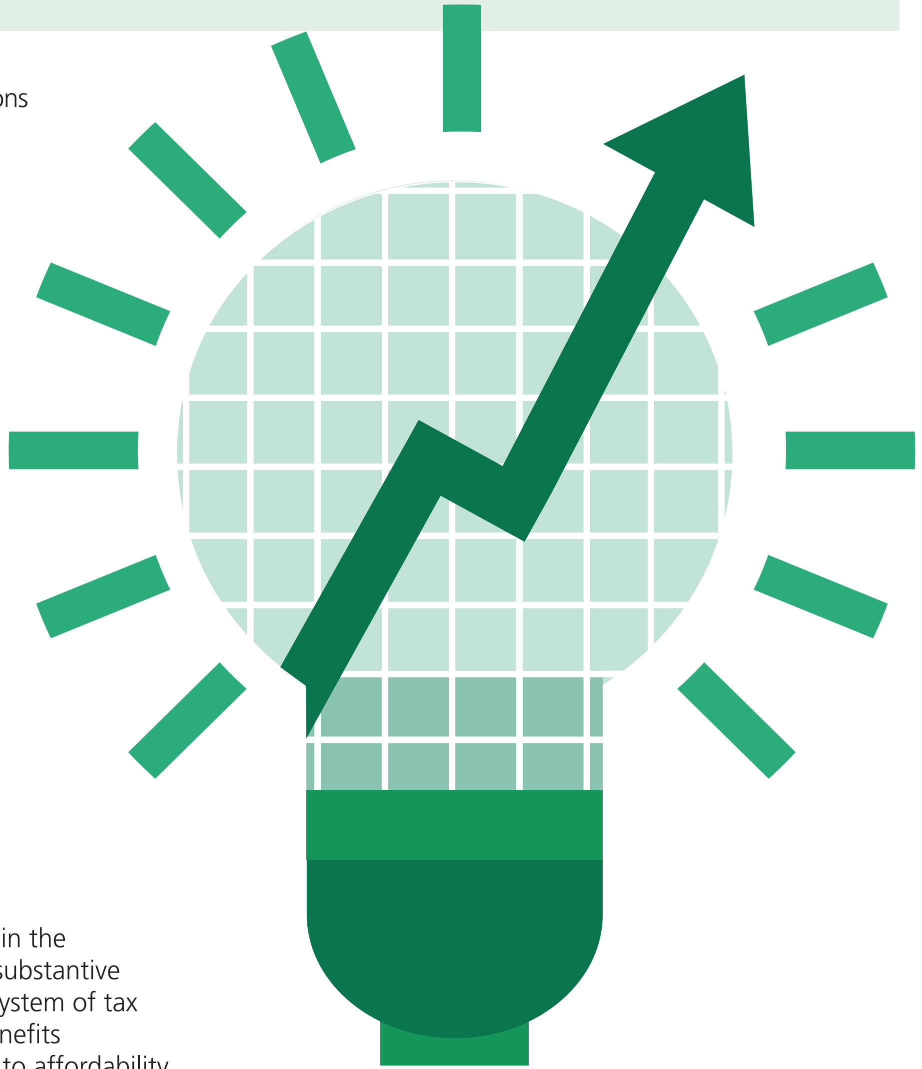
Our proposed increases in pension contributions are a reflection of the need to balance:

- a solution that addresses the savings gap as quickly as possible;
- the challenge of employer and employee affordability; and,
- the need for stability in the post Brexit period.

Employers have told us that they need time to plan for and manage costs. We have proposed that employer contribution rates are frozen until 2023 and gradually increased over 6 years.

Affordability is cited as the number one reason why employees don't save for retirement. We have proposed no change in net cost for employees until 2025, although higher and additional rate tax payers will see an increase in cost associated with the introduction of a flat rate savings bonus.

Increased contributions will see an increase in the cost of tax relief for government. Delaying substantive increases to allow time for changes to the system of tax relief, as well as the crystallisation of the benefits of Brexit, is designed to mitigate any threat to affordability for the state.



The savers' bonus

Our research shows that two thirds of people struggle with the complex nature of pension tax relief. Aviva research has found that 66%[27] of those surveyed had little or no understanding of how the tax system impacts pension contributions.

It must be clear that it always pays to save for retirement and we need to incentivise people to do so. As we push for greater pension contributions, these incentives must be clear, understood and appreciated to mitigate the risk of increasing opt-outs. Our evidence suggests the current system is not fit for purpose.

We need a system that is easier for all to understand and value, and the simplification of pension tax reform is a route to this.

Our research also shows that one in ten have never heard of pension tax relief and almost half believe the language used when it comes to pensions is unclear and difficult to understand.

RECOMMENDATION: Adopt a flat rate of tax relief – save 2 get 1 free – and rename as a 'savers' bonus'

We believe savers should get a flat rate of incentive from the Government, regardless of their earnings. Matched contributions have been shown to incentivise savings and the current system can be redesigned to give a simple accompanying message of "save 2 get 1 free" so for every £2 someone contributes to a pension the Government will contribute £1. This is fair and doesn't give the biggest incentives to those earning the most. It is often affordability that holds many people back from making increased contributions so our proposal recognises that people need a clearer up front incentive to encourage long term savings.

We believe that a save 2 get 1 free bonus is affordable to Government without making changes to the tax and NICs treatment of employer contributions if we:

- take action to remove salary sacrifice (including a general anti-avoidance measure);
- address the current inequity in the way in which defined benefit pensions are valued for annual allowance and lifetime allowance charges;
- use the annual allowance as a further control on expenditure.

We need to make the language we use to talk about pensions simpler and easier to understand. Given that one in ten haven't heard of the term "pension tax relief", we recommend that the term should be scrapped. Instead, we should call it what it is, a 'savers' bonus'.

Source: 27. http://www.aviva.com/media/news/item/uk-two-thirds-of-people-in-the-dark-over-pension-tax-relief-17526/

One in ten people have never heard of pension tax relief

Almost half of people believe the language used when it comes to pensions is unclear and difficult to understand

Scope

Bringing more people under the scope of AE

AE has helped more individuals save into a pension. Despite this, there are still large parts of the population that are not captured by AE and who risk facing a significant shortfall in their retirement savings. Current reforms exclude people with multiple low-paid jobs and people without an employer.

Despite the success of AE, the DWP report that 24% of all workers are not eligible for AE. The latest ONS data[28] states there are 26.8 million employees in the UK, so it could be interpreted that there are more than 6 million ineligible workers in the UK. The DWP also report that 37% of female workers are ineligible[29]. This could be more than three million people.

This is in addition to the self-employed who represent about 4.7 million[30]. In short, the headline data suggests that over 10 million workers could be missing out on AE.

Multiple job-holders

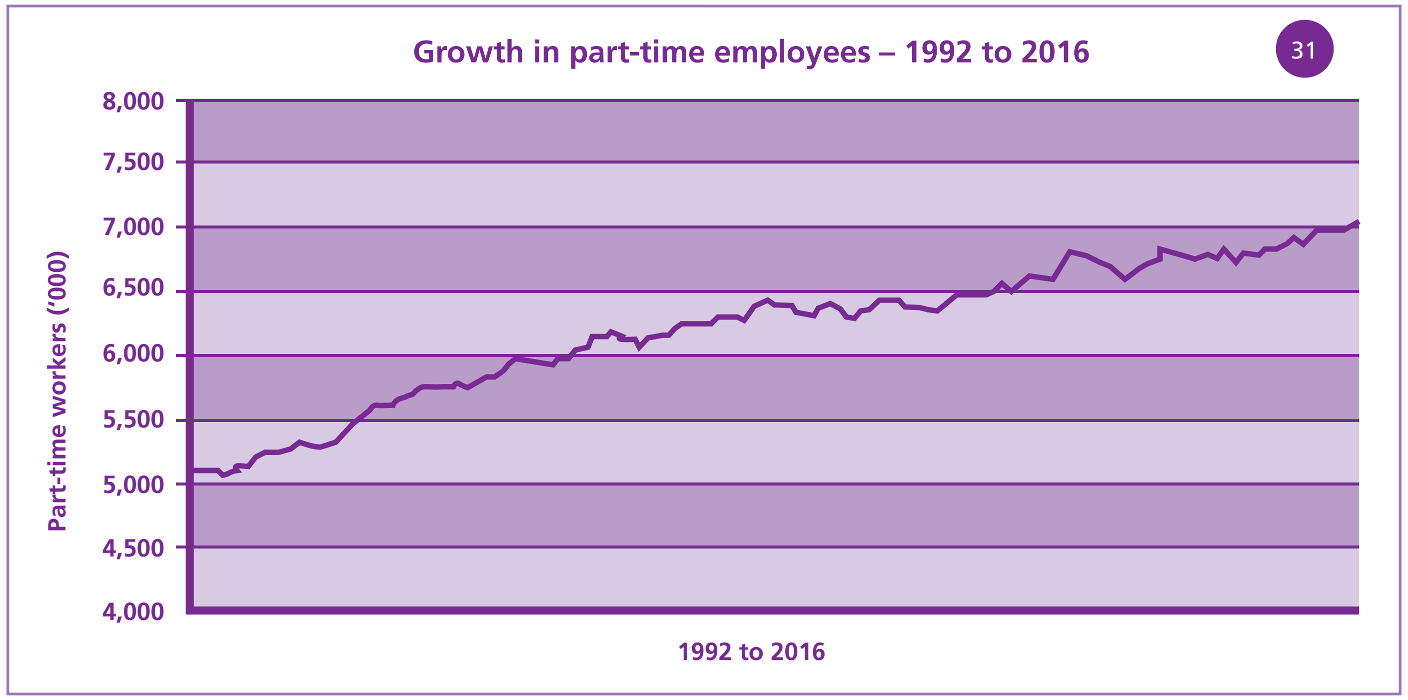
People continue to work more flexibly and having multiple jobs enables people to do this. Others have multiple jobs out of financial necessity or because they can't get full-time work from one employer. There has been a significant growth in part-time employees over recent years.

Source: 28. http://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/employmentandemployeetypes/datasets/summaryoflabourmarketstatistics I 29. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/460867/workplace-pensions-update-analysis-auto-enrolment.pdf I 30. ONS: A01 Summary of labour market statistics

24%

The percentage of workers not eligible for AE

(DWP)



The graph above shows the growth in part-time workers and shows an upward trend in the possible pool of multiple job-holders.

Currently, 29% of multiple job-holders (136,000 out of 470,000 people) are not captured by AE. Whilst 19% (89,000 out of 470,000 people) could voluntarily opt-in, this still leaves 10% fully excluded[32]. This 10% equates to 50,000 employees, of which 40,000 are reported to be female. Their pay from each of these jobs may be below the AE qualifying threshold of £10,000 despite their combined salary potentially exceeding £10,000.

For these employees, the financial shock of living in retirement on just the state pension will be just as great as their full time colleagues. However they do not benefit from AE and, depending upon their earnings, they may not be eligible for an employer pension contribution if they opt in.

The qualifying earnings threshold and the AE threshold perform an important function in ensuring that low paid workers contribute at an appropriate level but when workers have multiple jobs they are disadvantaged as the thresholds are applied to each job individually as opposed to overall earnings.

The world of work has changed over recent years and a system that was right when the original Pensions Commission began its work in 2002 may not be right for today.

If the income from both first and second jobs was taken into account when assessing eligibility for AE, then a further 80,000 people (60,000 women and 20,000 men) would earn enough to meet the qualifying criteria[33].

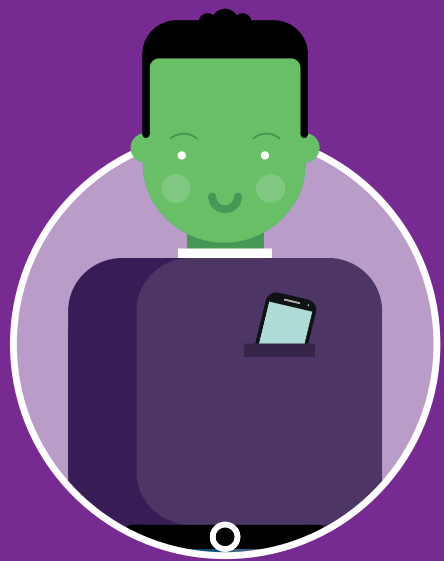
We would propose that DWP and HMRC work together to investigate whether Real Time Information (RTI) data could be used to identify employees with multiple jobs and advise employers that these individuals should be automatically enrolled or eligible for employer contributions.

Implementation timescales will need to factor in the impact on those industries which employ large numbers of part-time workers, but we believe there are sufficient numbers who are disadvantaged by the current system to justify exploring solutions to the issue in detail.

Source: 31. Office for National Statistics: A01 Summary of labour market statistics I 32. https://www.gov.uk/government/news/the-number-of-people-saving-as-a-result-of-automatic-enrolment-to-hit-10-million I 33. PPI Briefing Note 75 – who is ineligible for automatic enrolment?

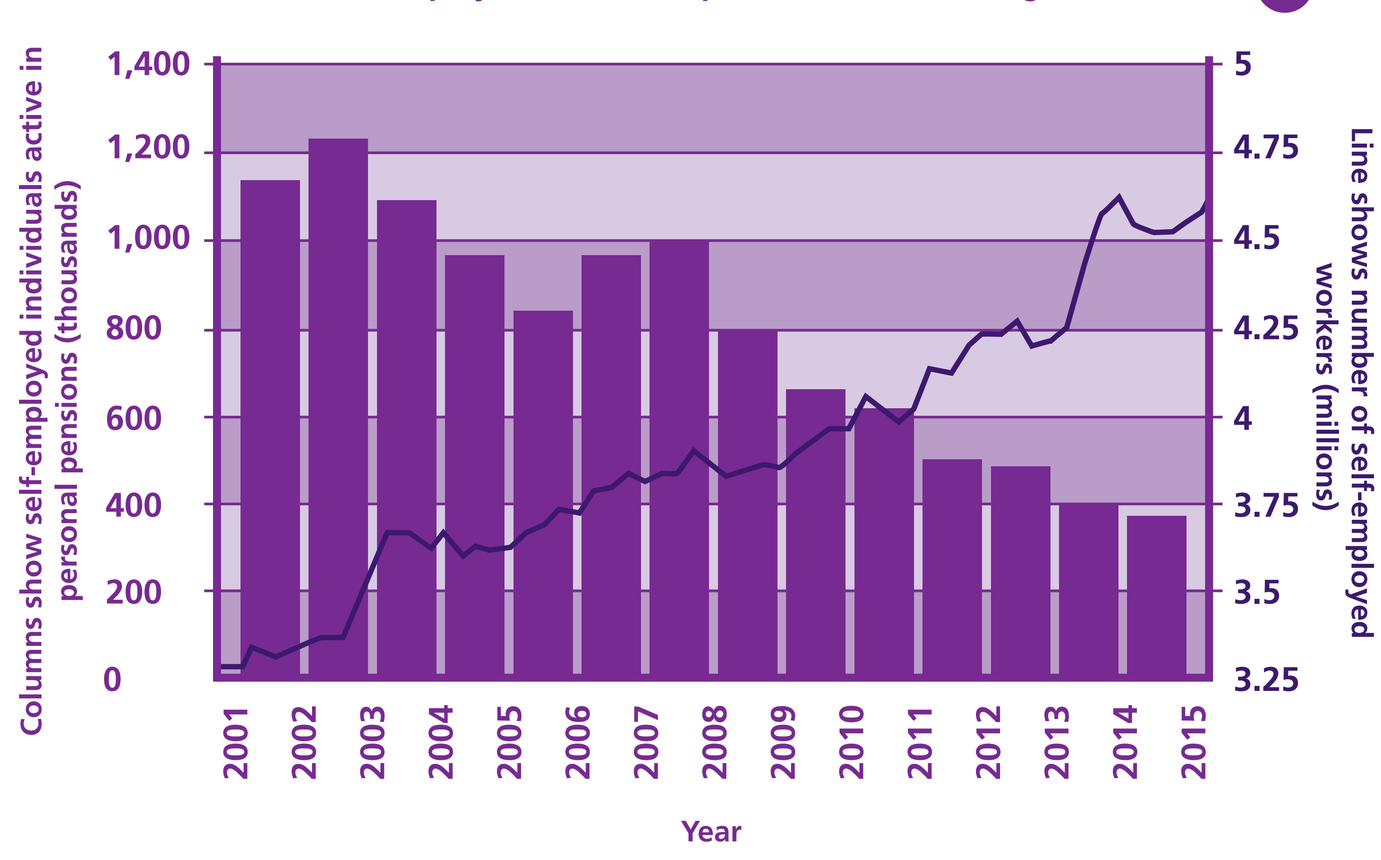
RECOMMENDATION:
Capture multiple job-holders

The self-employed



The fact that AE doesn't capture the self-employed is particularly worrying given the decline in saving amongst this community. The number of self-employed people saving in a personal pension has fallen to 380,000 in 2014-15. This is the lowest number since records began in 2001, and down from a peak of 1.2 million in 2002-03[34].

Self-employed: Numbers up but retirement saving down 35



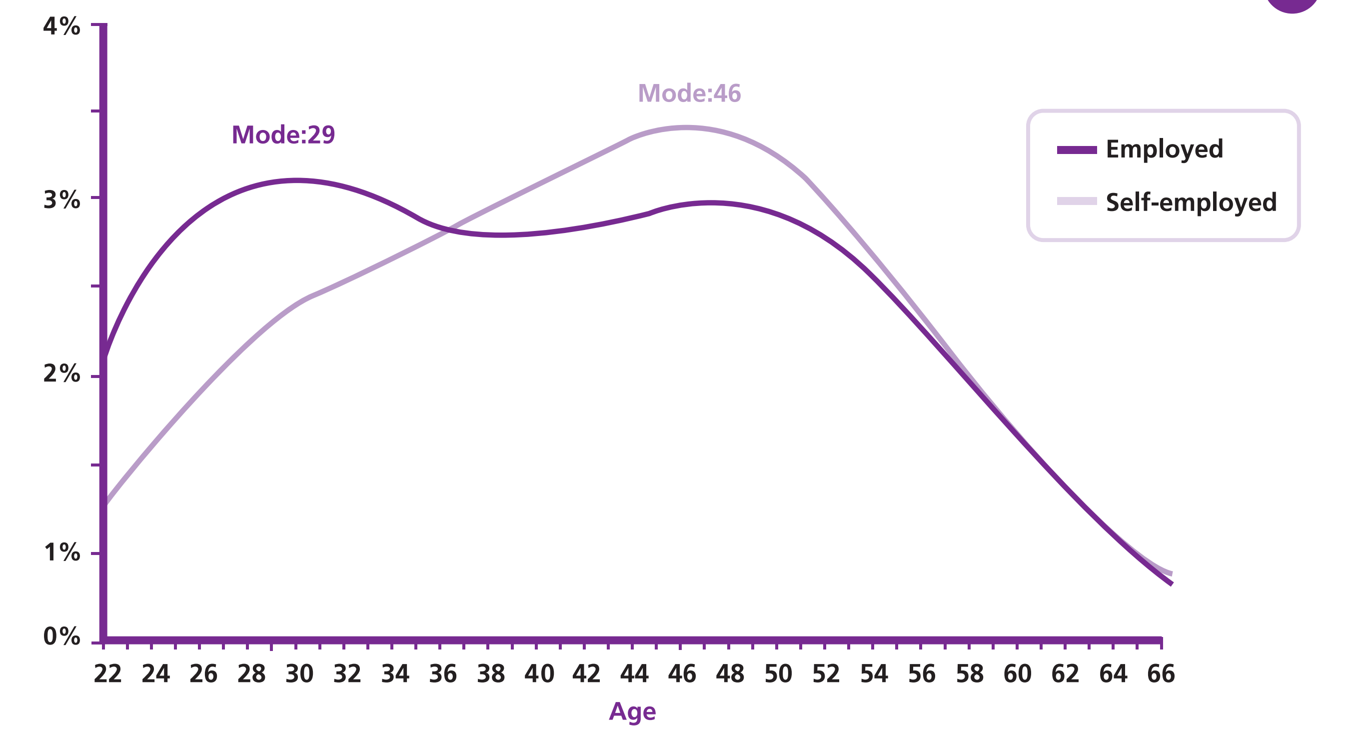
As the number of people who are self-employed continues to increase – reaching 4.7 million in the latest official statistics – it is concerning to see the number of savers in this community continue to fall.

Source: 34. HMRC, Personal pensions statistics introduction, 2014 (last updated 2016) I 35. HMRC, Personal pensions statistics introduction, 2014 (last updated 2016) and ONS Article: Trends in self-employment in the UK: 2001 to 2015.

When the original Pensions Commission began its work there were close to one-and-a-half million fewer self-employed people in the UK.

The age-profile of employed and self-employed workers is also very different. The modal age of an employed worker is 29. The modal age of a self-employed worker is 49. The needs and urgency of retirement provision between the two groups will be very different.

Distribution of employed and self-employed by age 36



As with multiple job-holders, a system that may have been right for then, is not right for today.

RECOMMENDATION: Explore options to capture the self-employed

While the rest of this report focuses on the needs of employed people, we believe the needs of the self-employed also require urgent attention.

We recognise that the Government received an independent report into the world of self-employment in February 2016[37]. Written by Julie Deane OBE, it considered a wide range of issues affecting the self-employed, including saving for the future. The report identified that "around one in five self-employed people have no financial plans for retirement other than relying on the state pension", and "less than a third of the self-employed say they pay into a pension". One of Julie Deane's recommendations addressed this point specifically:

"As the number of self-employed continues to increase, the need for more flexible financial solutions, from mortgages and insurance to pensions, will become more imperative. The financial institutions that choose to address this need stand to benefit enormously. When such flexible financial instruments do begin to appear trade organisations will play a key role in signposting these so that their self-employed members can benefit from them."

This report provides wide-ranging insight on which the industry's response can be built. Aviva will be doing a further piece of work in this area in 2017. In particular, we will consider how tax treatments could be used to support the self-employed.

Source: 36. ONS Article: Trends in self-employment in the UK: 2001 to 2015 I 37. Self-employment review: an independent report, Julie Deane

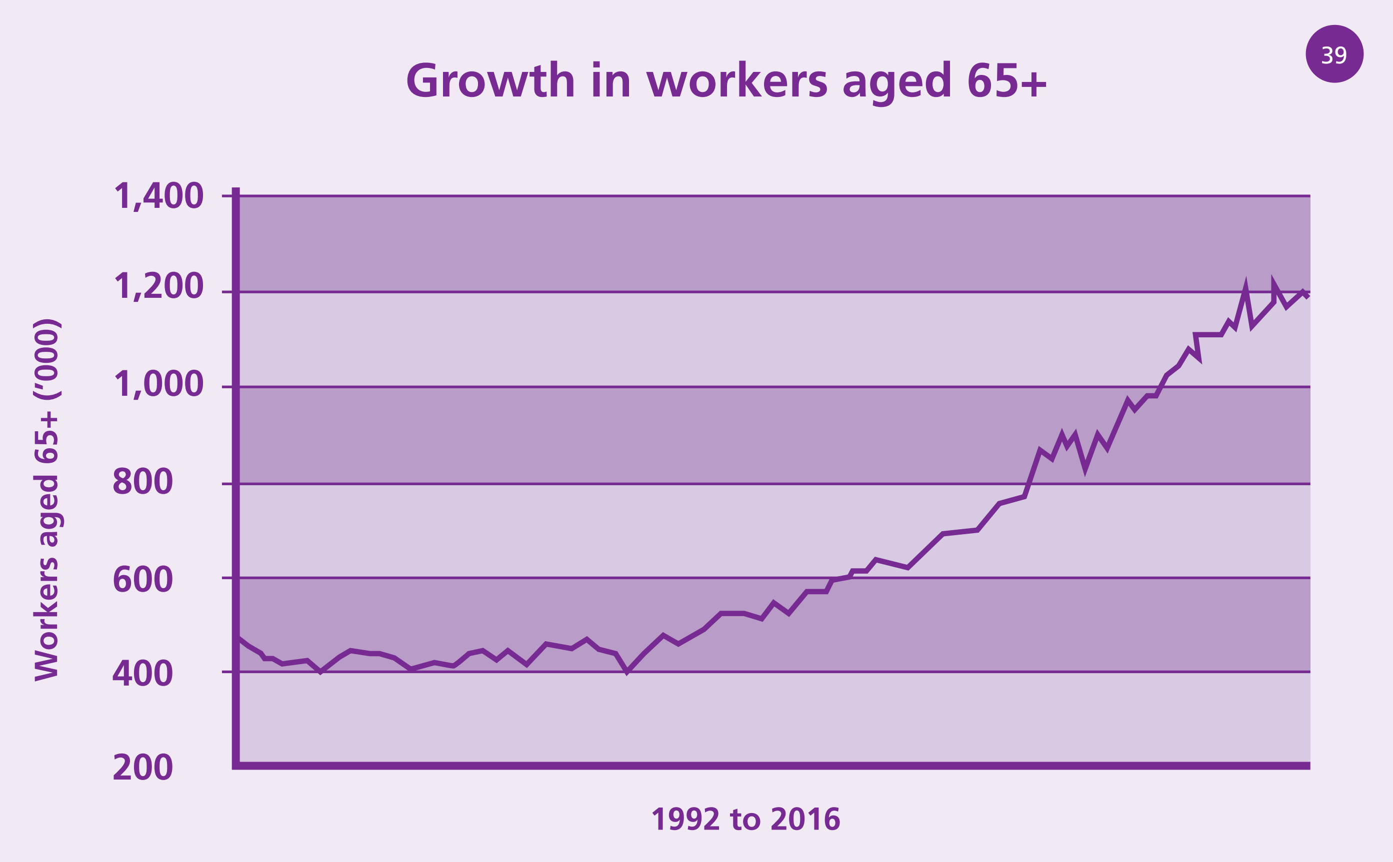
Older workers

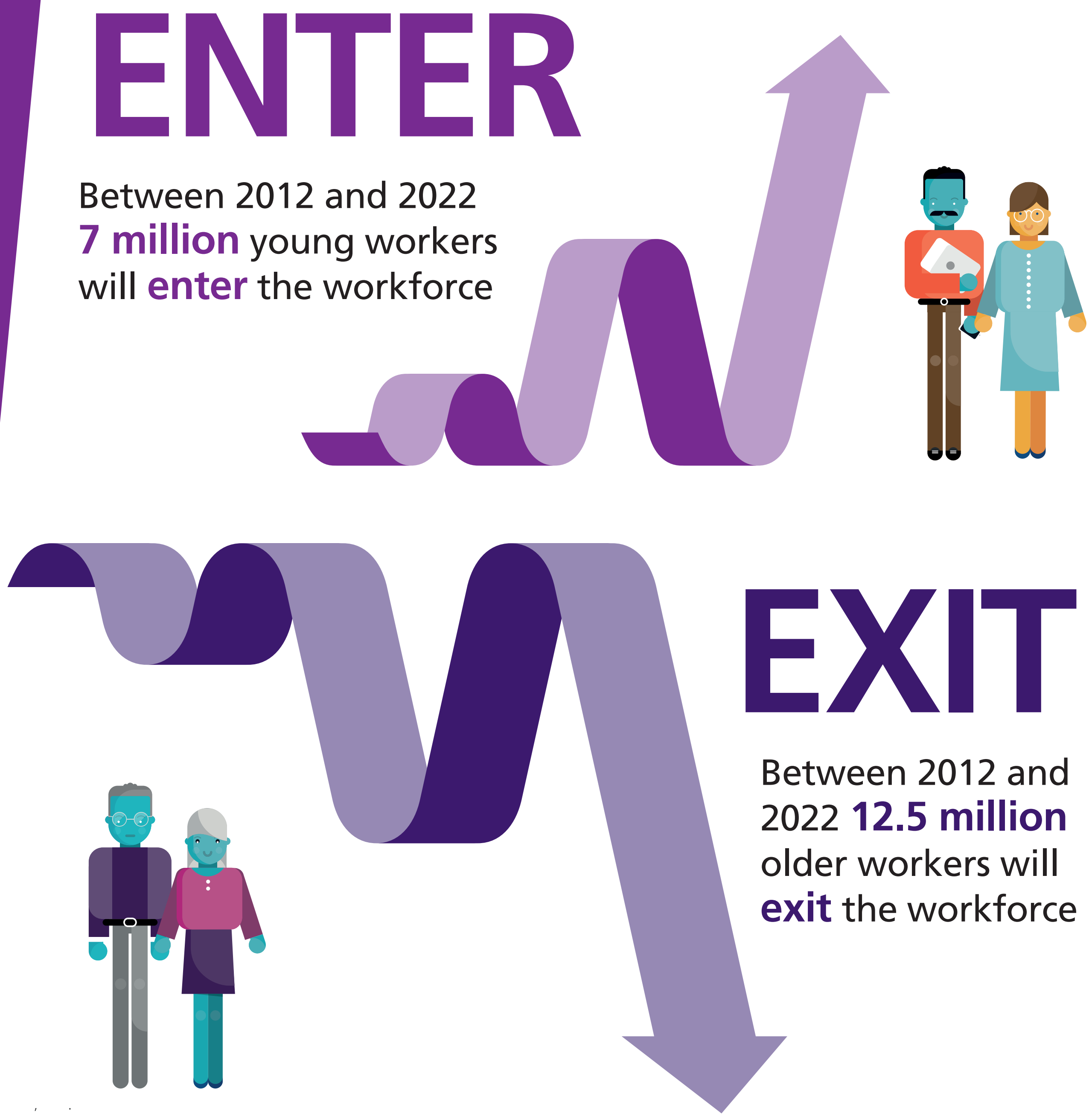
The number of workers aged 65+ has more than doubled over the past twenty years. This comes at the same time as life expectancy continues to rise.

The business case and benefits of employing older workers are clear for both the employer and employees. Having a diverse and representative workforce can be a real advantage to any business. Making organisations aware of the opportunities around retaining an ageing workforce can improve the overall contribution of older workers to economic growth and productivity, as well as making the best use of peoples' skills and experience.

For the UK as a whole, there is also a need to encourage a longer working life. Recent research from Business in the Community[38] reported that between 2012 and 2022 seven million new workers will enter the UK workforce. This comes at the same time as more than 12 million older workers will exit. We need more workers, and the older generation carry skills that can be of unique value.

Current AE policy means that if you're over the State Pension age, you won't be automatically enrolled by your employer into a workplace pension. Whilst you have the right to opt in up to age 74 – depending on your earnings – we believe removing the upper ceiling of state pension age will encourage a longer working life.





Given the specific pressures on younger savers – including managing student debt, getting on the property ladder and beginning a career – and the principles of other employment laws - such as the national living wage – we believe it makes sense for the minimum age of AE to be held at 22.

The evidence above, however, supports our belief that the current upper ceiling for AE should be abolished and replaced with 75 when the tax benefits of pension savings stop.

In 2011 we saw the abolition of the default retirement age[40]. This change in law made it illegal to make someone redundant based on their age alone. This was a positive reaction to the increasing trend in life expectancy, and we believe now is the time for AE rules to catch up.

RECOMMENDATION: Remove the upper enrolment ceiling of the state pension age to encourage a longer working life

Consolidation

Multiple jobs, multiple pensions

The number of small pots is increasing under AE. Younger workers in particular are likely to be mobile between jobs as they establish their careers and would benefit from new rules allowing the easy transfer of small pots. We know from consumer research that people want to be able to take their pension pots with them as they move jobs.

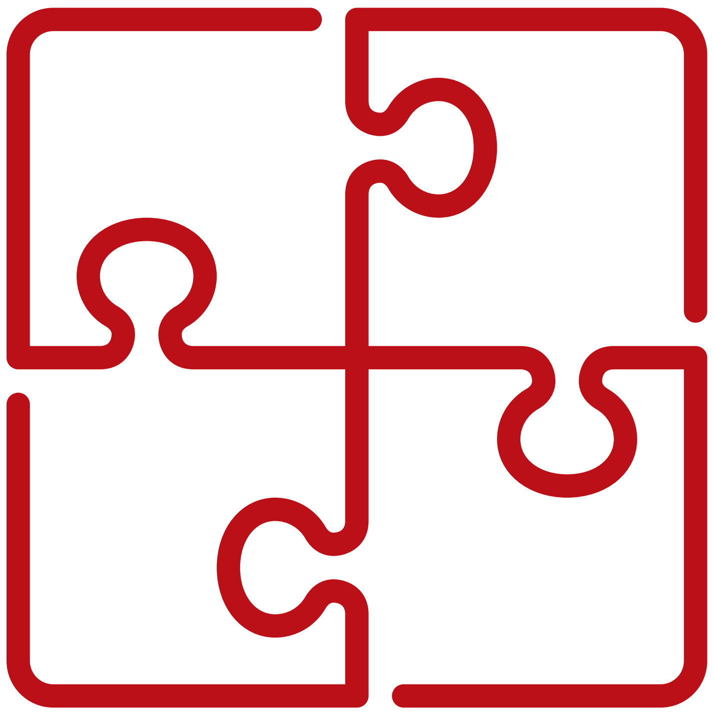
It is well reported that, on average, a person can have 11 employers over their working life[41], which means that they could end up with multiple private pensions by the time they retire. In some industry sectors this average number of employers will be much higher.

At the moment there is no way for people to see the value of all of their pensions in one place and research has shown that two-thirds (63%) of UK workers said they did not understand what happened to their pension fund once they left their employer[42]. The growing number of small pension pots will bring with it a growing number of problems:

- Difficulty for the individual in administering their pensions – e.g. updating address
- Difficultly in retirement planning - e.g. projecting retirement incomes
- Difficulty in making decisions at retirement - e.g. different pension freedoms on different products
- Inefficiency in administration on the part of the provider – e.g. higher costs restricting a provider's ability to invest in new services

The new Pensions Dashboard will be a key means of addressing these challenges in the market.

The Dashboard aims to provide a link to "lost" pension pots with previous employers and could help release the £400 million worth of pensions savings that the Department for Work and Pension estimate are currently unclaimed[43].



"On average, a person can have 11 employers over their working life"

Source: 41. https://www.gov.uk/government/news/pensions-dashboard-prototype-to-be-ready-by-spring-2017 I 42. http://www.aviva.co.uk/media-centre/story/15435/aviva-calls-for-automatic-transfer-of-small-pensio/ I 43. https://www.gov.uk/government/news/new-pension-tracing-service-website-launched

Aviva is one of the 17 leading providers committed to the development of the Dashboard, and we encourage all others to join this important initiative.

As reported in September[44], the leading providers are currently focused on delivering a prototype by March 2017, with the goal of having a full solution by 2019.

Some have suggested that, in addition to the Dashboard, there should be the legislative implementation of automatic transfers. We don't agree: the "pot-follows-member" debate was significant and robust, but it failed to deliver. We believe energies should now be focused on the implementation of the Dashboard. However the Dashboard won't be a panacea for the problem of small pension pots. We therefore recommend two additional actions to build on the momentum of the Dashboard.

We do not advocate automatic pension consolidation at the individual level. We believe the risks of financial detriment are too high. However we do believe that a clear signal needs to be sent to employees to encourage their own action. We recommend that a "rule of thumb" be agreed, adopted and promoted by all, stating that:

> "It is good to consolidate pots worth £10,000 or less – the engagement benefits of having these smaller pensions in one place, helping you appreciate what savings you have, will likely outweigh any potential losses."

We are supported in our belief by the position held by the DWP in its consultation, "Automatic transfers: consolidating pension savings[45]". The consultation document makes the case for the £10,000 pot size well:

"There are trade-offs that we considered in deciding a pot size limit for automatic transfers. We aim to achieve sufficient consolidation to encourage individuals to take note of, and engage with, their pension saving and to give them enough visibility of their savings to help them plan for retirement. We also need to sufficiently mitigate the risk that individuals lose track of pots and miss out on retirement income. This might point us towards higher pot size limits."

"On the other hand, a higher pot size has a greater potential risk of detriment where an individual moves between schemes with different features, though we might expect a range of potentially offsetting detrimental and beneficial impacts over an individual's working lifetime. Our proposed standards for automatic transfer, discussed in the next section, would help mitigate this risk."

"Balancing all these factors, we therefore propose that initially the pot size limit should be £10,000. We estimate that this would achieve reasonable consolidation for individuals by leaving only around 1 in 30 (or less than 4 per cent) of those retiring between 2050 and 2060 with five or more dormant pots."

As also recommended by the DWP, we recommend the £10,000 level be reviewed at least every five years to ensure it remains appropriate.

RECOMMENDATION: Officially encourage consolidation of small pension pots of £10,000 or less

Source: 44. https://www.gov.uk/government/news/pensions-dashboard-prototype-to-be-ready-by-spring-2017 I 45. DWP, Automatic transfers: consolidating pension savings, April 2013

Contract-based pension transfers

The workplace pensions arena is made up of broadly two worlds of governance – the trust-based world and the contract-based world. It would be misguided to state that one is better than the other, but it would also be misguided to state that both are the same.

As at March 2016, the Pension Policy Institute reports that over 3 million of the 6.1 million who have been automatically enrolled have been enrolled into trust-based schemes, and over 2 million have been enrolled into contract-based schemes[46]. The rest have been enrolled in hybrid or defined benefit schemes.

There is a significant difference between the worlds of trust-based and contract-based pensions in the area of transfers. Trust-based pensions have the authority to transfer their members' benefits from one scheme to another if they are professionally advised that the new scheme is at least equal. This authority does not exist in the contract-based world. A bulk transfer can be proposed, but individual member consent must be sought and secured prior to any transfer taking place.

Aviva's experience of seeking and securing individual member consent is that it can often result in more than one-in-three members failing to respond. This means that a significant proportion of members remain in their original scheme, often a poorer value scheme.

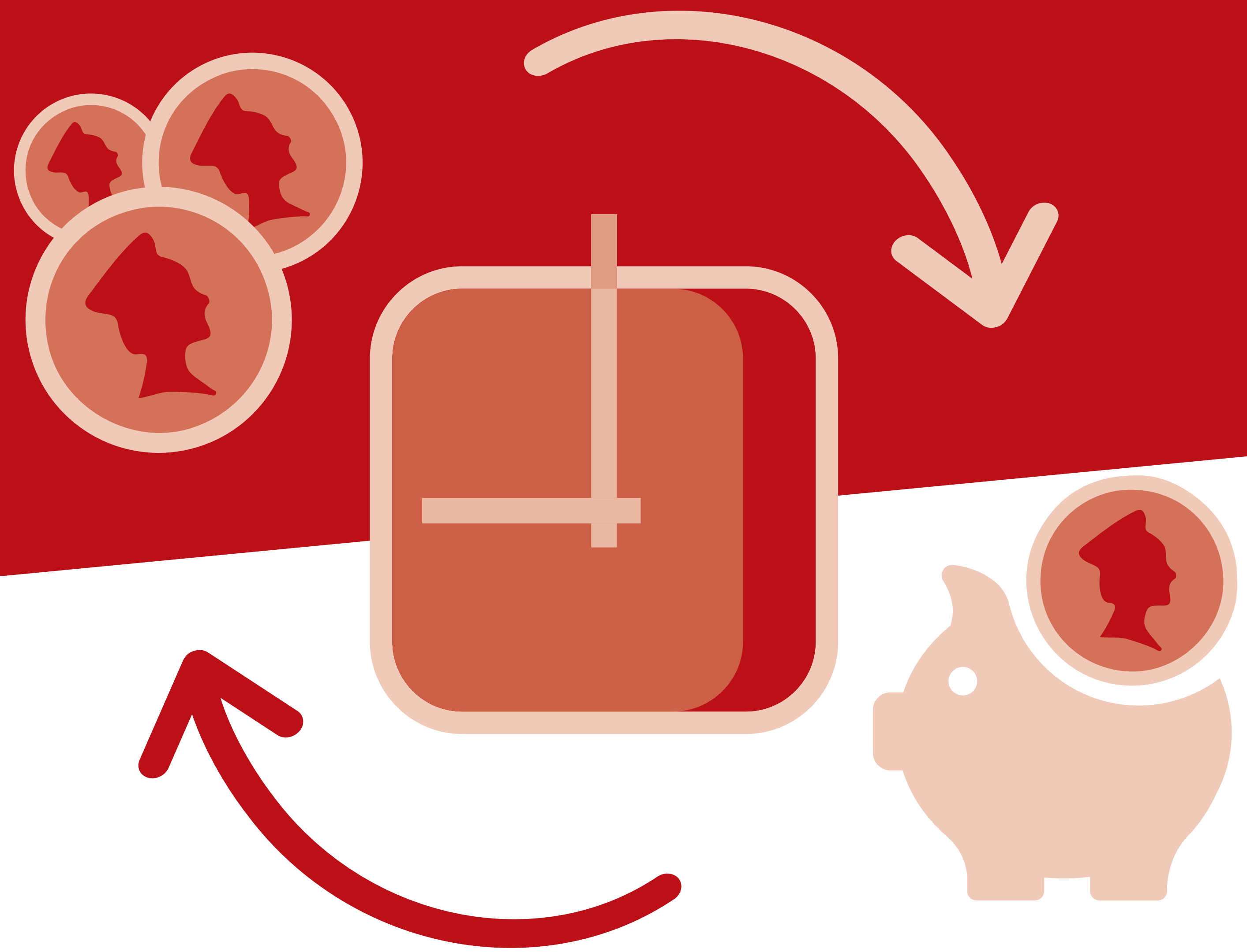
Pensions are, by their nature, long term products. As with all products, the services, options, and charges they offer develop over time. Savers benefit from these new developments, if they continually switch to the most modern products. The one-in-three who fail to transfer to modern pension schemes are less likely to benefit from these new developments on more modern pension platforms. That same one-in-three who fail to respond to offers to facilitate a transfer will not benefit from pension consolidation and the confusion of multiple small pension pots will continue.

In short, the one-in-three who fail to respond are likely losing access to a better and cheaper pension and the higher level of personal engagement that larger pension pots engender.

To solve this, we recommend that providers of contract-based pension schemes be given regulatory consent to implement bulk transfers of member benefits where it can be demonstrated by the provider to be in member interests. These bulk transfers, however, could only progress with the consent of the sponsoring employer and the provider's Independent Governance Committee. Both parties would have to agree that a bulk transfer is in the members' best interests. This governance "double lock" will ensure that the interests of scheme members are protected. As a final protection, disclosure requirements should ensure that all members are informed of the proposed transfer, and that they retain the right to opt-out, as they do with AE.

RECOMMENDATION: Permit "without consent" transfers of contract-based workplace pensions, so long as savers are no worse off

"Pensions are, by their nature, long term products. As with all products, the services, options, and charges they offer develop over time."



Source: 46. PPI The Future Book: unravelling workplace pensions, second edition 2016

Engagement

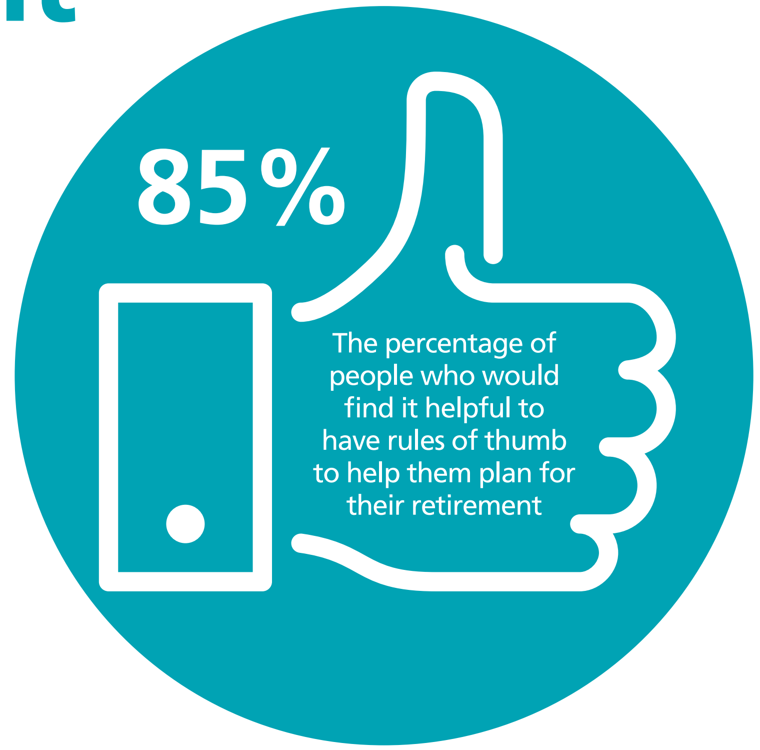
Do you speak pension?

Current AE reforms were designed around the expectation that inertia would lead many people to remain automatically enrolled, but that same inertia appears to be an important barrier to people improving their own rate of pension saving.

Whilst AE has been a success so far, there continues to be strong evidence of a lack of saver engagement:

- One in six employees are not aware of the workplace benefits available to them [47]
- The British Public would rather vacuum or change their bed-sheets than review their pension[48].

As contributions increase in 2018 and 2019 it will become increasingly important for individuals to understand where this money is going and to engage with their future retirement in order to avoid a rise in opt-out rates.



Case study: Aviva Good Thinking campaign – helping the UK face their future

As part of Aviva's mission to get the nation saving smarter, we recently launched a new campaign designed to spark a transformation in how people approach their finances.

At Aviva, we want to get to the crux of why people aren't saving enough, demystify the ways in which they can prepare for their futures, and inspire a new generation of savers in ways that resonate with their lives and aspirations.

Millions of people have now seen the outcome of our social experiment in documentary-style ads, shown on TV and online. In the experiment, we aged two people in prosthetics and challenged them to live off an amount of money that turns out to be their projected pension income.

The campaign brings to life – in an engaging-yet-thought-provoking way – the savings gap that many people face. The Shape My Future tool is central to the campaign and helps people to address what they want their future to be and whether they are on track to achieve it. This new tool received over 50,000 visits in its first two weeks and offers a solution based on deep customer insight around barriers to long term saving. It is accompanied by helpful content across a range of media – video, infographics, articles and other tools to help people take action. We're using social channels to specifically engage with SMEs in the AE space, driving them to related AE content.

In the next phase of the campaign we will be looking to the workplace: to engage advisers, trustees, employers and their employees, and encourage them to take action using workplace channels to deliver the campaign activity. All of the campaign activity for the workplace has been designed with this in mind, and is informed by our in-depth knowledge of financial education and engagement with some of the UK's leading brands through their pension schemes.

Source: 47. Survey of 11,428 UK employed people carried out by YouGov (Jan-Dec2015) on behalf of Friends Life, now part of the Aviva Group I 48. http://www.aviva.com/media/news/item/uk-brits-would-rather-vacuum-than-review-their-pensions-17666/ I 49. http://www.aviva.com/media/news/item/uk-30-million-adults-fear-their-money-wont-last-in-retirement-yet-one-in-four-worry-more-about-their-looks-than-their-pension-17689/ I 50. 15% of today's 31.8 million working people equates to 4.7 million people I 51. Financial Advice Market Review, March 2016 I 52. PPI Transitions to Retirement: Myths and rules of thumb in retirement income

Aviva research found that a majority of people (59%) worry about having sufficient savings to last them in retirement, but a minority (44%) feel they are taking sufficient action[49]. There is a risk people are being paralysed by fear into inaction. This 15% worry/action gap could be said to equate to nearly five million working people in the UK[50].

Our customer research has shown that people will not engage with things they do not understand – what we describe as a black box. We think we should make it easier for people to understand when they will be enrolled and how much their contributions will be. We recommend increasing the £10,000 earnings threshold to £10,400, and lowering the contributions threshold to £5,200. This means if you earn more than £200 a week you will be automatically enrolled and your contributions will be based on your earnings above £100 a week. We believe levels should be set so that people find it easier to understand, not at levels that make payroll easier.

RECOMMENDATION: Increase the eligibility threshold to £10,400 and lower the contribution threshold to £5,200 so that individuals can easily understand when they will be enrolled (once they earn more than £200 per week) and how much they will pay (contributions due on earnings over £100 per week)

Rules of thumb

We believe rules of thumb can give people a sense of saving required to achieve a desired retirement. Our consumer research tells us that an overwhelming majority (85%) of people would find it helpful to have rules of thumb to help them plan for their retirement – something akin to the healthy eating "five-a-day".

In developing rules of thumb, we agree with the FCA that these should be "simple principles which are generally reliable in the absence of full advice, such as broad steers on how to achieve a certain financial goal"[51].

We have used the Pensions Policy Institute's recently stated criteria for a valid rule of thumb to guide our thinking[52]:

a. Addresses a specific situation

b. Relatively easy to understand, apply, and mass-communicate

c. Can be used as a guide or a target

d. Offers a better course of action than not following it (i.e. it is in the individual's general best interests)

We also note the limitations of rules of thumb as set out by the Pensions Policy Institute:

a. Accept that rules of thumb will not provide "optimum" advice

b. Accept that rules of thumb are not intended to replace professional advice

c. Accept that rules of thumb do not represent "once and done" actions for savers

d. Accept that rules of thumb need regular review to reflect changes in the personal finance environment (e.g. changes in rules and/or tax rates)

People understand that rules of thumb are only guides, not strict rules to abide. Our consumer research shows that the majority (54%) describe a rule of thumb to be "a broad statement that is based on science, but it is not accurate for all people". Only 21% saw a rule of thumb as "an accurate statement on which all should base their decisions".

We strongly believe that rules of thumb could be of value in all areas of personal finances. At this time, we have focused our thinking on the retirement accumulation process.

RECOMMENDATION: Adopt Aviva's three rules of thumb

- **40 year rule:** Aim to begin saving at least 40 years before your target retirement date
- **12.5% rule:** Aim to save at least 12.5% of your monthly salary towards your retirement
- **10 times rule:** Aim to have saved at least 10 times your annual salary by the time you reach retirement age

Our three proposed retirement saving rules of thumb are [53]:

The retirement rules of thumb

When planning your retirement savings, aim to meet at least two of the following three rules:

- **40 year rule:** Aim to begin saving at least 40 years before your target retirement date
- **12.5% rule:** Aim to save at least 12.5% of your monthly salary towards your retirement
- **10 times rule:** Aim to have saved at least 10 times your annual salary by the time you reach retirement age

We tested consumer attitudes to rules of thumb[54]:

84% of people said a rule about how many years you should save for would be a helpful guide to help them plan for their retirement

85% of people found a percentage of salary a helpful guide

76% of people found a rule about target pension pot using salary multipliers useful

The common adoption and promotion of these rules of thumb by all in the retirement saving arena – providers, government, regulators, employers and advisers - will help embed them in the minds of savers.

Case study: The success of 'five-a-day'

'Five-a-day' is the best known and most successful health message. The advice encourages people to eat five portions of fruit and vegetables a day. Having originated in the U.S., the UK government introduced its 'five-a-day' campaign in 2003 following evidence showing that eating at least five portions of fruit and vegetables each day could prevent up to 20% of deaths from illness including heart disease and some cancers.

Research showed that the public was confused as to what constituted a portion so the campaign set out how much of a particular fruit or vegetable you needed to eat as part of a healthy diet. The 'five-a-day' logo also aimed to prevent the food industry from using misleading labelling about the nutritional value of their products.

The 'five-a-day' message is now ingrained in people's minds due to continued promotion from both government and the food industry.

Aviva's retirement saving rules of thumb aim to help people identify their saving goals in the same way that 'five-a-day' has helped people understand what constitutes a healthy diet.

We would propose that rules of thumb are endorsed by the FCA and the Pensions Regulator so that they can be used in member communication without the need for lengthy caveats which could detract from the effectiveness in promoting positive outcomes for savers at retirement.

Source: 53. Methodology explained in Annex 2 I 54. Recommendations tested with 2,311 consumers through private research conducted for Aviva by Censuswide

The digitisation of pensions

We see a clear role for government and regulators to create the right environment and the right incentives so that the pensions industry is encouraged to digitise the customer experience.

Aviva is on record as saying that our industry is "in the stone age" when it comes to digital technology[55]. We have a lot of catching up to do, and we must rise to this challenge.

The responsibility for retirement well-being increasingly sits on the shoulders of the individual – driven by the decline of final salary pensions and the introduction of pension freedom and choice. Digital technology has the potential to support individuals to make the right decisions as they rise to this new responsibility.

There is strong evidence of people's willingness to engage with their pensions via technology. Over 400,000 people have requested a state pension forecast online over the past year – a year-on-year rise of 40%[56]; the Pension Wise website has had over 3 million visits[57]; and Aviva's own online Retirement Planner has been used over 200,000 times by customers planning their retirement in the past 12 months.

The appetite for technology is understandably strongest amongst the young; and the young is a market we cannot ignore[58]. There are over two billion under-30s in the world today, and by 2025 they will represent 75% of the global workforce[59].

Aviva's research has found 75% of people would like to manage their pension savings online and that one-in-two under 35s would prefer to buy their savings products online. Google has probably replaced friends and family as the go-to place for help and information[60].

When we've asked younger savers what they look for in a product or service they say three things:

Convenience I Pace I Personalisation

Digital technology has the ability to address all three. Aviva therefore proposes action.

RECOMMENDATION: Encourage the digitisation of pensions through government policy and regulation and a minimum level of digital functionality

Source: 55. http://www.wsj.com/articles/aviva-boss-slams-insurance-industrys-tech-progress-1446122760 I 56. https://www.gov.uk/government/news/demand-increases-for-new-state-pension-statements 57. I https://www.gov.uk/performance/pension-wise I 58. Aviva Consumer Attitudes Survey 2016 I 59. GfK Evolving Consumer Trends, 2016 I 60. Aviva Consumer Attitudes Survey 2016

As a first step, the provision of data to the Pensions Dashboard should be a condition of qualification as an AE scheme. We would also encourage policy makers to consider setting a minimum standard of digital functionality including online statements and standard data export/import capability to support future IT development.

This will ensure that more than six million savers who have been introduced to pensions via AE will continue to benefit from the latest digital developments; will have guaranteed access to the Pensions Dashboard; and will enjoy a pensions online user-experience in line with virtually every other service they experience.

Case study: Aviva "Shape my future" tool

To encourage people across the UK to make sure they are saving enough into their pension Aviva designed the "shape my future" tool. Our goal was simple: reframe pensions to make them want to engage.

Just telling people about pensions is not enough as many are deliberately avoiding the subject – it is not a high priority issue for many people and they find it hard to empathise with their future, older, selves.

Our solution was to focus on "retirement lifestyle" and get rid of as many figures and graphs as possible. The tool is accessible online and helps people daydream about the lifestyle they might like to have in the future.

First we encourage people to build an approximate budget of what they might have to spend in their later life, then we take a light-hearted, look at how much the lifestyle they want could cost. As they do this they can see their lifestyle budget being spent and can rebalance their budget, either by increasing their contributions or reducing their lifestyle budget.

Users told us they found it much easier to understand what a pension is and why it is important to save now.

The new tool received over 50,000 visits in its first two weeks.

"Aviva's new 'Shape my future' tool received 50,000 visits in its first two weeks"

Food for thought

This report highlights Aviva's ten priority recommendations to ensure the continued success of AE. However our thinking continues. Our consumer research shows that less than one in four (22%) employees say they understand AE very well. As contribution rates increase towards 12.5% however it can be expected that more and more employees will want to know where their money is invested and may want to exert greater personal control. We would encourage government and industry to continue to review engagement levels and how these can be increased.

One way to increase engagement levels may be to allow employees to select their own pension provider. Employers would still select a default provider for all but employees could, if they wish, choose a different provider.

Greater ownership may encourage engagement levels and lower opt-out rates. Indeed, our consumer research shows one in four (24%) would like the freedom to choose their own pension product and 44% would be open to the possibility.

We recognise that this concept may raise operational and financial challenges. This proposal could be complex and costly for providers and employers to administer, potentially adding to costs and straining the AE charge cap. Additional costs could be detrimental to savers.

Having said that, we think the cost to savers could be kept to a minimum because AE software is now capable of facilitating employer payments to multiple schemes without creating any additional payroll administration.

We must also consider the risks for the employee. Some may get a better deal by choosing an alternative pension provider whilst others may lose out. There would also be a need to consider how the governance framework which currently oversees employer-sponsored pensions could be enhanced to cover individually-selected pensions.

Additionally, employers would need to maintain a default scheme for new workers without an existing account or whose previous employer is not prepared to allow them continued membership.

It's clear that there are a range of issues which would need to be examined here and government and regulators would need to consult on these issues and risks to test the practicalities and the benefits.

Enabling employees to select a pension provider if they want to is just one further example of how government and industry could help drive engagement levels. We don't yet have the solution to every single problem but we have tried to show that in addition to our 10 steps to AE success, there are plenty of other options worth examining.

We believe our 10 steps to AE success provide a strong platform for reforms that will help the British public, and particularly people like Sue, secure a more prosperous retirement.

Conclusion

Recent government initiatives are moving people in the right direction and AE has made a demonstrable difference to the future pension health of the nation. But there is more work to be done.

As the reforms progress, the focus should be on consumer needs, and long term policy making. AE policy was successful because it emerged in a de-politicised environment and it has been supported by successive governments - the policy was born under a Labour government via the Pensions Commission, it was rolled out in 2012 under a Coalition government and its review is now taking place under a Conservative government. We hope that this support continues.

Our vision for savers is that every person can enjoy the retirement that they aspire to. Their aspiration, whatever that may be, should be their reality.

To achieve that vision, we need to continue to ensure the link to workplace and employer contributions, retain a sustainable incentive to upfront savings and not disrupt the roll out of AE through other policy interventions. The system needs to work for as many people as possible, provide people with an adequate income in retirement and use technology to solve tomorrow's problems.

Above all, we need to engage people and help them understand how to plan for their retirement. We believe our 10 steps to AE success help make this a reality and we look forward to working with government in its review of AE.

About Aviva UK

We have strong businesses in selected markets: UK, Europe, Asia and Canada. Across our 16 businesses, we protect our 29m+ customers and the things that are important to them. Aviva Life is the UK's leading life and pensions business, providing award-winning retirement, savings and protection business to 12 million customers.

Our purpose is to free people from fear of uncertainty and to support our customers at some of the most significant moments in their lives. Our ambition is to be the company that customers turn to first, to help them enjoy a secure and prosperous retirement and to protect them and their loved ones should they die or fall ill.

We help make life easier for over 12m customers in the UK. We're the largest corporate pension provider in the market with £47 billion of assets, a market set to triple in the next decade. We help retirees navigate new pensions freedoms and offering innovative investment solutions. We have an extensive protection product range, with the broadest distribution footprint, providing life insurance, critical illness cover and income protection. We have a multi-distribution network, providing our products and services directly to customers, online and via independent financial adviser, strategic partners and joint ventures. Aviva's asset management business, Aviva Investors, provides asset management services to both Aviva and external clients, and currently manages over £289 billion in assets. Aviva helps people save for the future and manage the risks of everyday life; we paid out £30.7 billion in benefits and claims in 2015. This means £2.3 million was paid every day to life, critical illness and income protection customers and their families in 2015 – that's £1,600 every minute. By serving our customers well, we are building a business which is strong and sustainable, which our people are proud to work for, and which makes a positive contribution to society.

For further information please contact:

Media relations enquiries:
Ben Moss
+44 (0) 117 928 5843
+44 (0) 7827 832 395
Ben.moss@aviva.com

Public policy enquiries:
Roisin Watson
+44 (0) 207 662 0429
Roisin.watson@aviva.com

Annex 1: Methodology

We've worked to ensure our report uses recent, established sources and a robust methodology, where necessary, to explain our recommendations.

The research shared in this report includes:

- Consumer polling: we surveyed employed people through two rounds of consumer polling. The first round of polling was conducted with Onepoll and we received a total of 2,000 responses. The second round was conducted with Censuswide and we received a total of 2,311 responses. Both surveys were conducted online and the sample targeted ensured a comprehensive cross-section of the UK working population.
- Large business polling: we surveyed a sample of our own large business customers and received a total of 277 responses. For the purpose of this report, a 'large business' is a company ranging from 50 to 20,000+ employees.
- Small and medium business polling: we surveyed a sample of our own small and medium business customers and received a total of 182 responses. For the purposes of this report, a 'small and medium business' is a company with 0-49 employees.

In addition we also made reference to previous consumer polling conducted by Aviva. This has been referenced throughout the report.

Annex 2: Rules of thumb calculations

We base our rules of thumb on four principles:

1. Broad guidance only; and people understand this

"Rules of thumb" are intended to provide useful guidance. They are not intended to provide specific direction or advice. Aviva's research suggests consumers understand this.

People understand that rules of thumb are only guides, not strict rules to abide. Our consumer research shows that the majority (54%) describe a rule of thumb to be "a broad statement that is based on science, but it is not accurate for all people". Only 21% saw a rule of thumb as "an accurate statement on which all should base their decisions".

2. Focusing on the majority

We believe it is appropriate to base this analysis on scenarios that are relevant for the majority of people. We have therefore based our analysis up to incomes of £40,000 (before tax). This covers 80% of the UK working population[61]. We believe that those who earn above £40,000 each year (i.e. broadly higher-rate taxpayers) are better placed to pay for personal financial advice to guide their actions.

3. Cautious assumptions

Our analysis is based on cautious assumptions. For example, we assume a median level of investment growth and assume use of low risk, inflation-linked annuities at retirement. It is possible that higher investment growth could be achieved and a retirement plan involving greater risk could be adopted. It is also possible the individual would have access to other assets at retirement, beyond their defined contribution pension.

4. A high bar

We have however consciously set a high bar for savers. At a time of recognised under saving, our belief is that positive use of ambitious rules of thumb could be used to "jolt" savers into positive action. At this time of chronic under-saving, positive jolts are needed.

With these principles in mind, we propose the following three rules of thumb:

- The 12.5% rule: Aim to save at least 12.5% of your salary towards your retirement, and this can include any money from your employer and the tax man, in the form of tax relief
- 40 year rule: Aim to begin saving at least 40 years before your target retirement date
- The 10 times rule: Aim to have saved at least 10 times your salary by the time you reach retirement.

Source: 61 https://www.gov.uk/government/statistics/percentile-points-from-1-to-99-for-total-income-before-and-after-tax

12.5% rule: Aim to save at least 12.5% of your salary towards your retirement, and this can include any money from your employer and the tax man, in the form of tax relief.

The table below shows the range of percentages that an individual would need to save to achieve the noted target replacement rates.

For the 2% of working people who are reported to earn £10,000, they do not need to save beyond their state pension to achieve their target replacement rate. However many of these individuals may have multiple jobs or may find themselves earning more as they get older. For the others in our analysis there is a need to save. For all others, our guidance of "at least 12.5% of your salary" is relevant.

Gross salary	Net salary today	Target replacement rate (% of net income)	Target Net income in retirement	Gross income required in retirement (assuming all income is taxable)
£10,000	£9,767	80%	£7,814	£7,814
£20,000	£16,767	70%	£11,737	£11,921
£25,000	£20,167	67%	£13,512	£14,140
£30,000	£23,567	67%	£15,790	£16,988
£40,000	£30,367	60%	£18,220	£20,025

Percentage of banded earnings needed to hit replacement rate at age 67, at noted starting age below				
Gross salary	Age 22	Age 30	Age 40	Age 50
£10,000	0.00%	0.00%	0.00%	0.00%
£20,000	10.75%	14.50%	22.75%	41.00%
£25,000	12.50%	17.00%	26.50%	47.75%
£30,000	14.75%	19.75%	31.00%	55.75%
£40,000	14.00%	18.75%	29.50%	53.00%

Our analysis is based on the following methodology and assumptions:

- Our analysis models the percentage of banded earnings that would have to be invested to achieve a set target replacement rate at retirement. These percentages are the totals. They could include tax relief and/or any employer contributions within these totals, if relevant.
- Our replacement rates vary around a core target of 67% for those on median earnings (c£25,000 pa). Given an unavoidable core of basic costs (e.g. housing and utility bills), we have set a higher replacement rate for those on lower levels of income, and vice versa for those on higher levels of income.

- We have based our analysis on net replacement rates, to avoid the payment of National Insurance before retirement exaggerating the replacement income needed in retirement.
- We have based our analysis on defined contribution pension savings only. We give no consideration to potential access to other assets or defined benefit pensions. We believe this will be the case for a large number of AE savers.
- We have assumed the individual will be in receipt of a state pension of £8,093 per year.
- We have assumed the individual retires at the state pension age.
- We have assumed median investment growth (after inflation and charges) of 2.4%.
- We have assumed the individual will use 100% of their pension to purchase a low-risk, single-life, inflation linked annuity, with five year guarantee at retirement. For this, we have used a guidance annuity rate of c3%.

40 year rule: Aim to begin saving at least 40 years before your target retirement date

This rule is based on the same analysis shown in the "12.5% rule". The table below shows the replacement rates that could be achieved if those on set incomes begin saving at set ages.

Gross salary	Net salary today	Target replacement rate (% of net income)	Target Net income in retirement	Gross income required in retirement (assuming all income is taxable)
£10,000	£9,767	80%	£7,814	£7,814
£20,000	£16,767	70%	£11,737	£11,921
£25,000	£20,167	67%	£13,512	£14,140
£30,000	£23,567	67%	£15,790	£16,988
£40,000	£30,367	60%	£18,220	£20,025

Percentage of banded earnings needed to hit replacement rate at age 67, at noted starting age below				
Gross salary	Age 22	Age 30	Age 40	Age 50
£10,000	0.00%	0.00%	0.00%	0.00%
£20,000	10.75%	14.50%	22.75%	41.00%
£25,000	12.50%	17.00%	26.50%	47.75%
£30,000	14.75%	19.75%	31.00%	55.75%
£40,000	14.00%	18.75%	29.50%	53.00%

It is clear that the earlier we begin saving, the lower the percentage we will need to save. Delaying will only make the hurdle higher. Age 30 will be an indication of "40 years before retirement" for many people. At this age, the saving percentages range between 14.50% and 19.75%. For many, these will be daunting savings rates. It was recently reported that the average saving rate in a defined contribution occupational pension is only 4% today[62].

For many, there can be an expectation of pay progression as they move through their career. This should ease the financial burden on these people. However the message needs to be clear that it pays to begin early.

It must also not be interpreted that it is too late for those with less than 40 years to go. This population can focus on our third "10 times" rule. The climb will be steeper, but the summit can still be reached.

10 times rule: Aim to have saved at least 10 times your salary by the time you reach retirement

The multiple of 10 is based on the objective of securing a target net replacement rate in retirement. Our target rates vary around a core target of 67% for those on median earnings (c£25,000 pa). Given an unavoidable core of basic costs (e.g. housing and utility bills), we have set a higher replacement rate for those on lower levels of income, and vice versa for those on higher levels of income.

The multiple of 10 is deliberately based on a "cautious" approach to financial planning. It assumes the individual has no access to other assets at retirement and no defined benefit pension, and it assumes a single-life, inflation linked annuity is purchased at retirement. It is very possible that the individual will have access to these other assets, and the individual could choose an alternative drawdown strategy at retirement.

The tables below show the net replacement rates that could be achieved at retirement by having various multiples of your salary in a defined contribution pension at retirement. The multiples are 10x, 11x, 12x, 13x, 14x and 15x.

				Net replacement rate			
				Level	RPI-linked	Level	RPI-linked
Gross salary	Multiple	Net salary	Target replace. rate	0% TFC	0% TFC	25% TFC	25% TFC
£10,000	x10	9,767.2	80%	130%	112%	119%	105%
£20,000	x10	18,200	70%	97%	77%	84%	69%
£25,000	x10	22,200	67%	90%	69%	77%	61%
£30,000	x10	26,200	60%	86%	64%	72%	56%
£40,000	x10	34,200	50%	80%	58%	66%	49%
Average replacement rate				97%	76%	83%	68%
£10,000	x11	9,767.2	80%	135%	115%	122%	107%
£20,000	x11	18,200	70%	102%	80%	88%	71%
£25,000	x11	22,200	67%	96%	73%	81%	64%
£30,000	x11	26,200	60%	92%	68%	76%	58%
£40,000	x11	34,200	50%	86%	61%	70%	52%
Average replacement rate				**102%**	**79%**	**87%**	**70%**

Source: 62 ONS Occupational Pension Schemes Survey, UK: 2015

				Net replacement rate			
				Level	RPI-linked	Level	RPI-linked
Gross salary	Multiple	Net salary	Target replace. Rate	0% TFC	0% TFC	25% TFC	25% TFC
£10,000	x12	9,767.2	80%	139%	117%	126%	109%
£20,000	x12	18,200	70%	108%	83%	92%	74%
£25,000	x12	22,200	67%	101%	76%	85%	66%
£30,000	x12	26,200	60%	97%	71%	80%	61%
£40,000	x12	34,200	50%	92%	65%	74%	54%
Average replacement rate				107%	82%	91%	73%
£10,000	x13	9,767.2	80%	144%	120%	129%	111%
£20,000	x13	18,200	70%	113%	86%	96%	76%
£25,000	x13	22,200	67%	107%	79%	89%	69%
£30,000	x13	26,200	60%	103%	74%	85%	63%
£40,000	x13	34,200	50%	97%	68%	79%	57%
Average replacement rate				113%	86%	95%	75%
£10,000	x14	9,767.2	80%	149%	123%	132%	113%
£20,000	x14	18,200	70%	118%	89%	100%	78%
£25,000	x14	22,200	67%	113%	83%	93%	71%
£30,000	x14	26,200	60%	108%	78%	89%	66%
£40,000	x14	34,200	50%	102%	71%	83%	60%
Average replacement rate				118%	89%	99%	78%
£10,000	x15	9,767.2	80%	153%	126%	136%	115%
£20,000	x15	18,200	70%	124%	93%	104%	81%
£25,000	x15	22,200	67%	118%	86%	97%	73%
£30,000	x15	26,200	60%	114%	81%	93%	69%
£40,000	x15	34,200	50%	107%	74%	87%	62%
Average replacement rate				123%	92%	103%	80%

At "10 times", the target replacement rates are achieved across the vast majority of segments analysed. Only if the individual limits their annuity purchase to 75% of their fund do they fail to achieve their target. As indicated in our analysis of the "12.5% rule", the results show no need for those earning £10,000 each year to save beyond their state pension. To do so would result in an income in retirement greater than that secured in employment.

At any multiple greater than ten our belief is that there is a risk of "over-saving" amongst the target group. The quality of life while working could be excessively damaged in an attempt to secure a set level of income in retirement.

Assumptions:

- Retires at state pension age.
- Our replacement rates vary around a core target of 67% for those on median earnings (c£25,000 pa). Given an unavoidable core of basic costs (e.g. housing and utility bills), we have set a higher replacement rate for those on lower levels of income, and vice versa for those on higher levels of income.
- We have based our analysis on net replacement rates, to avoid the payment of National Insurance before retirement exaggerating the replacement income needed in retirement.
- We have based our analysis on defined contribution pension savings only. We give no consideration to potential access to other assets or defined benefit pensions. We believe this will be the case for a large number of AE savers.
- We have assumed the individual will be in receipt of a state pension of c£8,093 per year.
- We have assumed a single-life, inflation linked annuity, with five year guarantee at retirement. For this, we have used a guidance annuity rate of c3%.

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