

Focusing on the outcomes

With the increase in minimum contribution rates under automatic enrolment to 8%, Aon head of DC Sophia Singleton asks what is needed to enable members to retire when they, and their employer, want

There will be much excitement within the pension world around the increase in minimum contribution levels from 6 April this year, including the important questions:

- will this lead to significant increases in opt-out rates?
- is 8% enough? and, assuming it's not,
- how can we encourage employees to save more towards their retirement?

Will there be an increase in opt-outs?

Aon's experience with schemes that have flipped their approach to default contribution on its head demonstrates why I believe opt-outs will not increase. This 'flip' defaults employees to maximum company matching levels and then allows them to 'opt-down' to lower levels, rather than the traditional approach of defaulting at the lowest level and trying to encourage members to save more. In all cases we have seen, the outcome is that more than 70% have remained at the maximum level, while those who have elected to reduce contributions have generally not reduced them to the lowest level. Extrapolating this behaviour, people generally accept that they should be

5%

Of surveyed employees said they consulted an adviser on how much to save into their pension

saving more, so if we 'do it for them', it is unlikely that most will actively decide to reduce or cease contributions.

Is 8% enough?

Well perhaps it is, if you are a 22-year-old earning national median salary and looking forward to 45 years of pension saving and a full State pension (on today's rules). This was the scenario modelled by the Pension Commission when designing auto-enrolment. How do employees decide if they need to save more than this?

Aon's recent *DC and Financial Wellbeing Member Survey* asked employees how they decided how much to save and found that only 5% of employees consulted an adviser, with only 3% saying that they used an online tool. Over 60% based their pension savings level on the employer contribution design, either the default or maximum matching levels. This underlines the importance of considering pension outcomes when designing contribution structures.

Our 2017 *DC Scheme Survey* found over 50% of those

60%

Of staff chose their savings level based on their employers' contribution design

responsible for running company pensions did not know how much a typical member might expect to receive from their scheme at retirement, never mind how much a member might need.

We know that many will not be saving enough to be able to retire when they want to – our calculations show that a 25 year old would need to save 18% of his salary per annum to achieve a reasonable outcome.

And our research found that less than half of those with DC pensions expect to retire by age 67, and 70% of people expect to go on working full- or part-time into retirement. This is fine if it is a personal choice, and from an employer's perspective older workers can help retain valuable experience within a business. What is not so positive is if people go on working simply because they cannot afford to retire.


Encouraging employees to save more

One successful approach is to be more holistic when talking to employees about pensions, helping people to put their pension saving in the context of their overall financial situation. For example, providing a simple budgeting tool can enable people to see the costs of their day-to-day outgoings, as well their expenditure on leisure activities. This could be online, part of a workshop, or simply

a sheet of paper, but thinking about spending today is the best way to start setting a retirement income target for the future.

The next step is to help individuals understand their likely retirement income based not just on the projected value of their company pension but also taking into account the state pension and any other savings they expect to have in retirement. Comparing the expected income and outgoings in retirement makes it simple to see where there is a potential shortfall. Employees then have a clear choice about whether to retire later, cut back on their spending in retirement, or save more into the company pension now.

We have worked with schemes taking this type of approach to help them produce communications around the changes, either delivered via face-to-face sessions, by using our online financial aggregation tool, by issuing a short flyer, or via a combination of different methods.

Rather than focusing first on what is being paid in, trustees, employers and most importantly members themselves would be better concentrating on the target outcome first. If we want people to make informed decisions about pension saving, we should be talking to them about setting pension targets in the context of their overall financial position, not just quoting percentages. 

To request a full copy of our DC Pensions and Financial Wellbeing research email talktous@aon.com

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Example	Member contribution	Company contribution
Default		
Current rate	3%	3%
Normal approach	4%	4%
	5%	5%
The flip	6%	6%

Allow trade down

