EVIDENCE-BASED POLICY MAKING: THE PENSIONS COMMISSION AND BEYOND

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The Pensions Commission first report (2004) set out the evidence base in relation to pension provision in the UK drawing on national surveys, academic and social research, modelling and administrative data. Its recommendations (2005) were similarly evidence-based. Since then the Department for Work and Pensions (DWP) has worked to introduce pension reforms through the 2007 Pension Act, focused on a fairer State Pension system and the 2008 Pensions Act and the Workplace Pensions Reforms Regulations that aim to increase private pension saving in the UK. This paper will focus on the Workplace Pensions Reforms. Evidence-based impact assessments and implementation plans have been published. Discussions are ongoing to develop an Evaluation Strategy. Liaison continues between DWP and other colleagues to build on existing surveys, such as those produced by the Office of National Statistics to develop the evidence base for the future.

INTRODUCTION

Pension policy cannot be considered in isolation and the relevant evidence-base is wide ranging. The policy recommendations published by the Pensions Commission covered a reform to both the State and the Private Pension system; these were largely accepted by Government following the White Paper in 2006. The breadth of analysis, much of it commissioned or carried out by Department of Work and Pensions (DWP) analysts, is so wide that it cannot all be covered in this short paper. This paper will therefore aim to summarise the importance of evidence-based policy making in relation to private pensions reform in the UK. The paper will cover three key areas; firstly the role of the independent Pensions Commission in making recommendations for reform to the Government, secondly the impact of the Workplace Pensions Reform on individuals and finally the plans that are being developed now to evaluate the reforms.

PENSIONS COMMISSION

The Pensions Commission was an independent body established by Government following the pensions Green Paper in December 2002. The Commission had three Commissioners and the following remit: to keep under review the regime for UK private pensions and long-term savings, and to make recommendations to the Secretary of State for Work and Pensions on whether there is a case for moving beyond the current voluntarist approach.

The Commission published an initial work plan in June 2003 outlining the analysis that would be conducted in the period before the First Report. The Commission outlined clearly that the First Report would focus on a detailed description of the present position, but would not make policy recommendations. They deliberately chose this approach as it was essential that the problems facing Britain’s pension system were analysed comprehensively, looking at how all the different facets of the system relate to one another. The Commission wrote that pension reform in the UK has too often in the past proceeded on the basis of analysis of specific isolated issues.

The report was fact-based with a large number of charts, tables, footnotes and appendices tabulated against several characteristics (such as gender, age and sector) and categories. The topics included:

- Demographics data including population projections, fertility, mortality, migration, healthy life-expectancy
- Labour market data including employment rates, average retirement age
- State pension data including pensioner incomes and replacement rates, expenditure by pensioners and public pension expenditure
- Private pensions data including participation in private pension schemes of various types, contributions to pensions, numbers of pension schemes, macro-level contributions

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- Data on other forms of wealth including other forms of savings, housing wealth, inheritance, business assets
- Insight from behavioral economics, data on the public's understanding of and attitudes to pensions, rates of return, tax relief.

The analysis used to inform the development of the Pensions Commissions' recommendations was based on an extensive evidence base, including the Office for National Statistics (ONS) Annual Survey of Hours and Earnings (ASHE), ONS General Household Survey, the Government Actuary demographic data (now published by ONS), social research reports published by government, academics and others, DWP and HMRC administrative data, modelling by analysts in the Commission and the DWP Pensim2 dynamic micro simulation model. ONS data at the macro level from the Blue Book was also used. The Commission analysts liaised with ONS statisticians to gain access to specific datasets, to request specific analysis and outputs, and to understand the interpretation of results.

The Commission outlined the deficiencies in data sources available to help improve the evidence base in this area in the future. They also highlighted where judgments had to be made. This was deliberate as the Commission wanted to make clear the facts on which the analysis had been based, enabling experts and interested parties to point out if key issues had been missed. Getting a common understanding of the evidence-base at the first stage meant that when the Second Report was published the focus could be a policy discussion rather than an argument about the analysis and evidence.

The Commission published a Second Report in November 2005, which proposed a new settlement for UK pension's policy combining two main elements:

- A new policy for earnings-related pension provision relying on the automatic enrolment of employees into either a new National Pensions Savings Scheme or into existing company pension schemes, but with the right to opt-out, and with a modest level of compulsion on employers to make matching contributions.
- A reform of state pension provision to make it simpler to understand and less means-tested than it would become if current indexation arrangements continued. This is essential to provide the clear incentives and the understandable base on which individuals and employers can build additional private provision.

WORKPLACE PENSIONS REFORM

The Commission highlighted the UK pension system would have to be reformed to ensure it could meet several long-term challenges.

- People are living longer and fertility rates are low, meaning the proportion of the population aged 65 or over is rising rapidly. DWP analysis of ONS demographic data suggests the 'dependency ratio' will double between 2005 and 2050, with four working-age people supporting every pensioner in 2005, but only two in 2050.
- A higher dependency ratio means that, unless people have saved enough for their retirement, there is a high cost to those who are working to maintain the pension of the economically dependent.
- DWP modelling of the English Longitudinal Study of Ageing (ELSA) suggested around 7 million people are not saving enough to deliver the income they are likely to want or expect in retirement. This is slightly lower than the estimate produced by the Commission because the DWP estimate is based on household level data, while the Commission's figures are based on individual level data. The DWP estimate also factors in other financial assets, non-owner occupied housing wealth and business assets, whereas the Commission only looked at pension wealth.

The Pensions Act 2008 and Workplace Pension Reform Regulations 2010 aim to increase private pension saving in the UK. They form part of a wider reform package designed to ensure the UK has a pension system fit for the twenty first century and provides dignity and security for tomorrow's pensioners. The policies in the Act met requirements that the Government set out in the May 2006 White paper.

One of the key aims of the reform was to slow down and eventually reverse the anticipated decline in retirement saving, whilst minimising the burden on employers and impacts on the pension industry. Certain regulations designed to improve the operational viability of the reforms or minimise burdens on employers can potentially reduce contributions to pension saving in the short-term. The Impact Assessments associated with the Workplace Pension Regulations outline the macro-economy impact, and the impact on individuals, employers, the pension industry and government. This paper will mainly focus on the effect on individuals; by getting more people to save more for their retirement.

Automatic enrolment is one of the most effective joining techniques to overcome people's tendency not to act when faced with difficult financial decisions. Inertia and lack of confidence in making financial decisions appear to be more significant barriers for women than men in saving in a pension scheme. Research on the 401(k) experience in the United States shows that amongst employers that chose to use automatic enrolment it had the greatest effect among people on low incomes, people from minority ethnic groups and women.

For those individuals that choose not to save because it does not suit their personal circumstances, *the opt-out process* is designed to support the individual's decision not to save (DWP research report 434, 550 and 551). Changes in income, employment and domestic arrangements may drive some individuals who have opted out to want to save at a later point. Re-enrolment will help maximise savings and harness decision-making inertia by providing individuals with an opportunity to reconsider their savings decision. The number of individuals who are re-enrolled is likely to decline as reforms to workplace pensions saving become embedded over time.

As a result of these reforms, our latest working assumptions suggest that around 10 to 11 million people (4 to 5 million women) will be eligible for automatic enrolment into a workplace pension. After accounting for people who opt-out, we expect this will result in *5 to 9 million people (2 to 3 million women) newly saving or saving more in all forms of workplace pensions*. This analysis uses DWP modelling based on a range of data sources, such as the ONS ASHE, DWP employer and individual research reports (545, 546, 550) to name a few.

The reform will enable individuals to transfer income from their working life to increase their income in retirement. As a result, many individuals are likely to enjoy increased well-being over their lifetime by *smoothing their income between work and retirement*. Based on the methodology outlined in the DWP technical working paper 562 the impact of 'consumption smoothing' will be to increase social welfare by around £40 to 60 billion for the period up to 2050.

The reform will increase private pension incomes by around £11 to 14 billion a year (in 2009/10 prices), or £5 to 7 billion in 2009/10 earnings terms by 2050. The projections are based on the DWP Pensim2 dynamic micro simulation model which simulates the future life course of a current population to estimate their future pension income. It enables aggregate and distributional analysis of alternative policy, demographic and economic scenarios, and is based on data from the DWP Family Resources Survey, British Household Panel Survey and the DWP Lifetime Labour Market Data Base.

Most individuals, at the point of automatic enrolment, can expect to get back more in real terms than they put in. Analysis shows that for the vast majority (over 95 per cent) of individuals, the improvement in their retirement incomes is greater than the cost of contributions. Most get back more than twice the amount they put in, after taking inflation into account and there is no group identifiable in advance who would be better off not saving (DWP research report 558).

CONCLUSION

The reform will be staged from October 2012. The programme intends to fully evaluate the effects of the reforms against the policy objective of getting more people to save more for retirement. The Evaluation Strategy will assess the impacts of the reforms on individuals, employers and the pensions industry, to evaluate the extent to which we meet this policy objective whilst putting minimal burden on employers and maintaining current good pension provision.

Given the decentralised nature of the UK statistical system; each UK government department and each of the devolved administrations retain operational responsibility for the collection and production of statistics which relate to their own areas of responsibility. The ONS is the largest producer of official statistics in the UK; analysts in other government departments are therefore key users of ONS statistics and use those statistics in evidence-based policy-making in their own area.

The effects of the reforms will be evaluated through analysing a range of data, including Management Information from the Pensions Regulator and the National Employment Saving Trust (a new universal occupational pension provider established for the implementation of the reforms), existing continuous surveys of individuals and employers run by DWP and research from other Government Departments such as the ONS, and where appropriate, discrete research commissioned by DWP.

As such, the evaluation will be conducted by a combination of external research organisations and academics and DWP analysts. The evaluation will be carried out on an on-going basis to gauge progress throughout the implementation of the reforms and beyond. For example, the Department is currently carrying out an extensive feasibility study using the longitudinal ONS ASHE data to help evaluate the number of employees in the target group who are participating in pension saving, the amount of saving, the persistency of saving and to determine if employer contribution into pension provision remains stable or improves in light of the reform. Findings will be available publicly at key stages.

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DWP Workplace Pensions Regulations are a package of regulations which includes: *the Occupational and Personal Pension Schemes (Automatic Enrolment) Regulations 2010, the Employers' Duties (Implementation) Regulations 2010 and the Employers' Duties (Registration and Compliance) Regulations 2010*.