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REQUIRING AUTO-ENROLLMENT: LESSONS FROM UK RETIREMENT PLANS

By JONATHAN CRIBB AND CARL EMMERSON*

Introduction

Policymakers around the world are concerned that workers are not saving enough for retirement. One reason is that, in some countries, many workers do not have an employer-based retirement plan. For example, at any given time, around half of private sector employees in the United States do not have a plan¹ and, as recently as 2012, the coverage rate in the United Kingdom had fallen to just one in three. Since relatively few people save for retirement outside of employer plans, those without a plan are at greater risk of being unable to maintain their pre-retirement standard of living in retirement.

To address this coverage gap, one option gaining traction is requiring some or all employers to enroll their workers in a plan automatically, with the worker allowed to opt out. California, Connecticut, Illinois, Maryland, and Oregon have all enacted such policies while Germany, Ireland, and Poland are actively considering them.² So far, however, the United Kingdom is the only country to have completed the nationwide

rollout of a policy that requires all private sector employers to auto-enroll their workers in a retirement plan.

The UK experience provides a unique opportunity to evaluate the effectiveness of such a wide-scale policy on plan participation and saving. This *brief* summarizes the results of two recent studies on the UK reform.³

The discussion proceeds as follows. The first section provides background on the UK reform. The second section assesses the effects of auto-enrollment on participation at medium and large employers and, separately, at small employers. The third section compares UK participation to US participation. The fourth section looks at how auto-enrollment affects UK contribution rates. The fifth section considers how “re-enrolling” workers affects retirement plan participation. The final section concludes that the UK reform has substantially increased participation rates – to about 90 percent at medium and large

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employers and 70 percent at small employers. And, although most of the increase is among employees making minimum default contributions, the share of employees contributing at higher rates has also risen significantly as a result of the policy.

Background

Under an auto-enrollment policy, employers sign up their workers for a retirement plan, with the workers allowed to opt out. The key idea behind auto-enrollment is that it harnesses inertia because, once people are in a plan, they are unlikely to leave it. The UK's policy reform, which was created by the Pensions Act 2008, requires all private sector employers to auto-enroll their workers in a plan. This approach simultaneously addresses two concerns that are often treated separately in the United States – how to boost participation rates at firms that already offer a retirement plan and how to extend coverage to the large number of workers at firms that do not offer a plan.

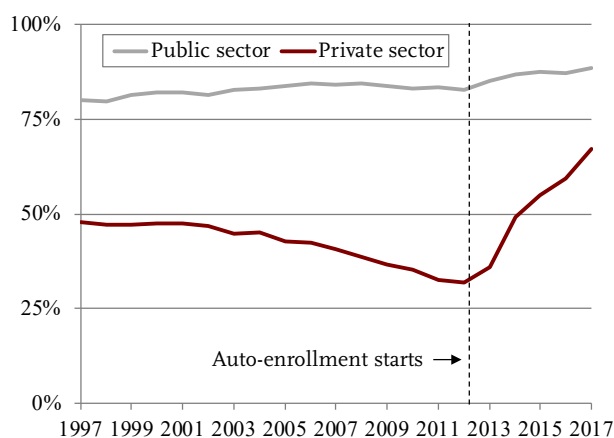
To be eligible for a plan, UK workers must: 1) be age 22 or older, up to the “state pension age” (65 for men and 63 for women in 2016-2017);⁴ 2) earn at least £10,000 (\$13,000) per year; and 3) have worked for their employer for at least three months. Contributions to the plan in the 2016 financial year had to be at least 2 percent of earnings between £5,824 (\$7,600) and £43,000 (\$55,900), of which at least 1 percent had to be an employer contribution. The minimum contribution rates were increased in April 2018 and are rising again in April 2019.

Auto-enrollment was introduced gradually beginning in 2012, with the timing determined by the number of employees working for each employer. Based on this information, employers were given a date to introduce their auto-enrollment plan – though the date could be postponed by up to three months – a feature that is accounted for in this research. The largest employers were required to introduce auto-enrollment in October 2012, and progressively smaller employers were affected over time. By April 2015, all employers with 58 or more employees had introduced auto-enrollment. Between June 2015 and February 2018, the enrollment deadline for the smallest companies (those with fewer than 30 employees) was determined by the last two digits of the employer's payroll tax number.

Effect of Auto-Enrollment on Participation

The UK's policy reform has led to an enormous increase in the share of private sector employees who are saving in a workplace retirement plan. The participation rate more than doubled: from 32 percent in 2012 to 67 percent in 2017. It still remains lower, however, than the participation rate in the public sector (see Figure 1), where workers are generally enrolled automatically in (typically more generous) defined benefit pensions, as opposed to the private sector, where defined contribution (“401(k)-style”) retirement plans are much more common.

FIGURE 1. PARTICIPATION RATES IN EMPLOYER RETIREMENT PLANS BY SECTOR, 1997-2017



Note: Participation rates were measured in April of each year. Sources: Office for National Statistics, Pension Tables (2011-2017); and Cribb and Emmerson (2016) calculations from *Annual Survey of Hours and Earnings* (ASHE) (1997-2010).

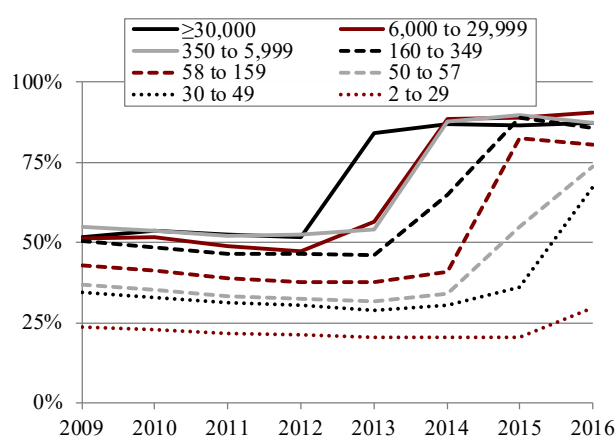
Participation by Employer Size

Just examining trends in participation does not prove that the increases were due to auto-enrollment. To achieve this aim, our analysis exploits the gradual roll-out of auto-enrollment from the largest to the smallest employers.⁵ This approach allows for an estimation of the effectiveness of auto-enrollment because different employers were affected by the policy

at different times. The analysis requires two assumptions to hold: 1) that the trends in plan participation would otherwise have been similar among employers of different sizes; and 2) that auto-enrollment only affects employer and employee behavior once the requirement goes into effect.

Looking at participation rates by employer size shows that rates jumped for employers of all sizes when their auto-enrollment deadline was reached (see Figure 2). For medium and large employers (those with 58+ workers), auto-enrollment increased participation rates by 37 percentage points, to a level of 88 percent in 2015 – very similar to the experience of large US firms that adopted auto-enrollment.⁶

FIGURE 2. PARTICIPATION RATES BY EMPLOYER SIZE (NUMBER OF EMPLOYEES), 2009-2016



Notes: Participation rates were measured in April of each year and exclude workers who were not eligible for auto-enrollment. Employer size is from 2012.

Source: Authors' calculations using ASHE (2009-2016).

As noted, the auto-enrollment mandate kicked in later for smaller employers. Similar to large firms though, employers with 50-57 and 30-49 workers saw substantial increases in participation. However, it is notable that participation rates reached 74 percent and 67 percent among these two groups, significantly below the rates reached by larger employers.

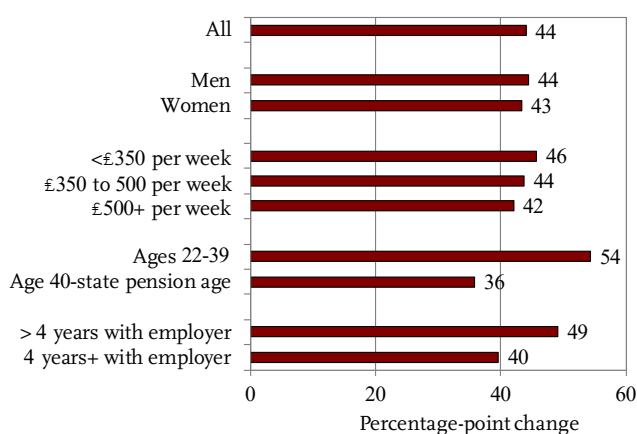
A Closer Look at the Smallest Employers

Looking at the smallest employers (2-29 employees) provides the best information on the effects of the auto-enrollment mandate because of the ability to

exploit the second feature of the roll-out explained above: that the timing of auto-enrollment for this group was determined by employer payroll tax number. Based on the date associated with this number, the analysis compares the participation rates at the smallest employers who had introduced auto-enrollment by April 2016 to those who had not yet done so.⁷

The results show that auto-enrollment increased participation for workers at the smallest employers by about 44 percentage points on average (see Figure 3). The effects were similar for women and men, but much larger for some other groups that previously had lower participation – lower earners, those under age 40, and those who had worked for their employer for less than four years.⁸

FIGURE 3. EFFECT OF AUTO-ENROLLMENT ON PARTICIPATION RATES AT EMPLOYERS WITH 2-29 EMPLOYEES, PERCENTAGE-POINT CHANGE, 2016

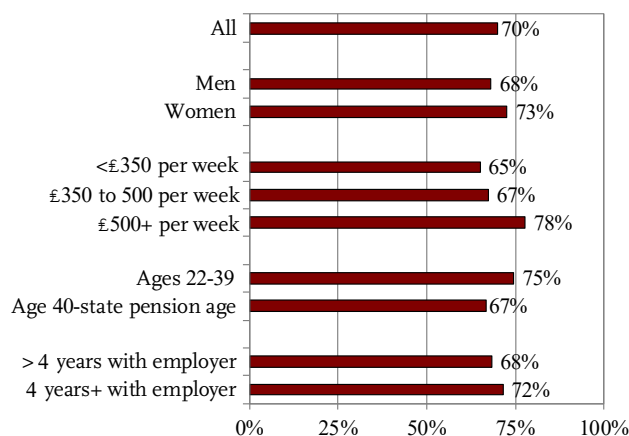


Note: Excludes workers who were not eligible.

Source: Cribb and Emmerson (2019).

Figure 4 (on the next page) shows the overall participation rate for the smallest employers that had introduced auto-enrollment, and how participation varied by worker characteristics. The participation rate for this group was 70 percent. This figure is high but not as high as the levels for medium and large employers, where it was about 90 percent. It also shows that participation under auto-enrollment was slightly higher for women, higher earners, workers under age 40, and those who had worked for their employer longer. However, none of these groups approached 90-percent plan participation.

FIGURE 4. PARTICIPATION RATES AT EMPLOYERS WITH 2-29 EMPLOYEES, 2016



Notes: Excludes workers at employers that were not yet subject to auto-enrollment and workers who were not eligible.
Source: Cribb and Emmerson (2019).

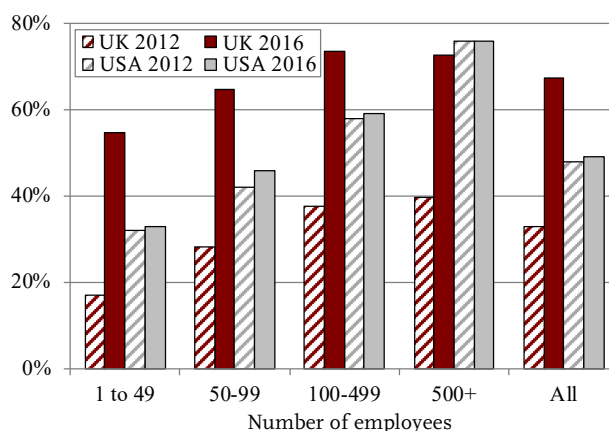
A key takeaway is that while auto-enrollment substantially increased participation rates at small employers, these rates are still much lower than those at larger employers. This gap is not explained by differences in the age, earnings, and job tenure of workers at smaller employers (all of which are predictive of lower participation). Some evidence indicates that, at least in part, the lower participation rates at smaller employers are due to less generous employer contributions, which appear to increase the likelihood of opting out.

UK to US Comparison

To understand the impact of the reform, it is also instructive to compare participation rates in the United Kingdom to those in the United States over the same period. US retirement plan participation rates were flat between 2012 and 2016 (see Figure 5), hovering just under 50 percent overall, which is not surprising given the lack of any significant policy changes during the period. In contrast, due largely to the new auto-enrollment policy, participation in the United Kingdom soared from 33 percent to 67 percent. The differences by employer size are striking, however. For large employers (500+ workers), the UK participation rate was still slightly lower than the US rate in 2016 while, for employers with fewer than 500 workers, the UK participation rate flipped from being much lower

than the US rate to much higher. This pattern suggests that an equivalent reform in the United States could generate a sizeable increase in retirement plan participation, primarily among employers with fewer than 500 workers.

FIGURE 5. PARTICIPATION RATES AT UK AND US EMPLOYERS BY EMPLOYER SIZE, 2012 AND 2016



Note: UK data for 2016 exclude small employers that were not yet subject to auto-enrollment.

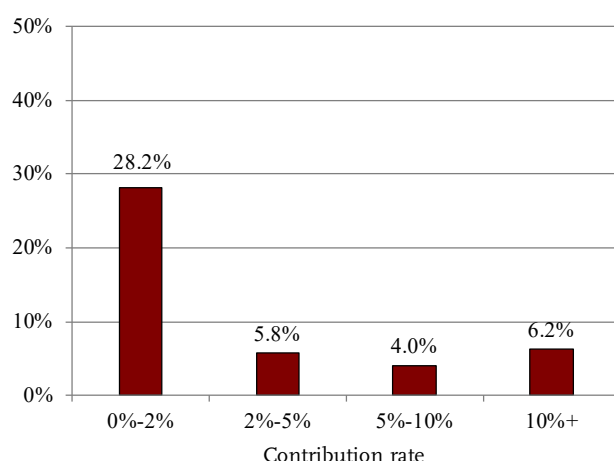
Sources: UK: Authors' calculations using the ASHE (2012, 2016). US: Bureau of Labor Statistics, *National Compensation Survey* (2012, 2016).

Effect of Auto-Enrollment on Contributions

The adequacy of retirement saving will ultimately depend on how much is saved – not just whether employees are participating in a plan. The analysis therefore looked at how auto-enrollment affected the total contribution rate (employee and employer combined).⁹ Figure 6 (on the next page) shows the results for the smallest employers (2-29 workers). The biggest effect is on the probability of having very low contribution rates – consistent with people making and receiving only the minimum default contributions set by the government. However, the results also show an increasing probability of significantly higher rates of contributions as well. For example, the share of employees contributing 5-10 percent of earnings rose by 4 percentage points, while the share contributing more than 10 percent rose by 6 percentage points.

These findings also apply to medium and large firms.¹⁰ The exact mechanism behind the increase in the share of workers contributing at higher levels is not clear. But one strong possibility is that some firms are enrolling their employees automatically in plans with contributions that are much higher than the minimums, potentially in plans that were already available before the auto-enrollment mandate went into effect but had low participation rates.

FIGURE 6. EFFECT OF AUTO-ENROLLMENT ON DISTRIBUTION OF TOTAL CONTRIBUTION RATES AT EMPLOYERS WITH 2-29 EMPLOYEES, 2016, PERCENTAGE-POINT CHANGE



Note: Excludes workers who were not eligible.
Source: Cribb and Emmerson (2019).

Effect of Re-Enrollment on Participation

Auto-enrollment can be either a “single shot” policy or involve automatically re-enrolling workers who opt out initially, which means that a worker who leaves their retirement plan will be re-enrolled at certain points, though they can always choose to leave again. The United Kingdom chose to require re-enrollment every three years, in addition to whenever an employee moves to a new employer. Given the gradual phase-in of the UK policy, in April 2016 all workers at firms with 30,000+ employees who opted out of the initial auto-enrollment were re-enrolled. Participation rates at these firms can be compared to firms that had not yet (in 2016) re-enrolled anyone – firms with 1,000-2,999 employees.¹¹

Figure 7 shows that, in 2016, the employers that had already gone through re-enrollment experienced no significant uptick in participation rates. Instead, their rates remained essentially the same as those of the comparison group, which had not yet been through re-enrollment. Re-enrollment – at least to date – does not seem to have boosted participation any further. This finding suggests that workers who choose to opt out when first enrolled also choose to opt out when re-enrolled three years later.

FIGURE 7. PARTICIPATION RATES AT FIRMS WITH AND WITHOUT RE-ENROLLMENT IMPLEMENTED, 2010-2016



Notes: Participation rates are measured in April of each year and exclude workers who were not eligible.
Source: Authors' calculations using ASHE (2010-2016).

Conclusion

Since 2012, the United Kingdom has gradually required all private sector employers to enroll most of their employees in a retirement savings plan automatically with at least a low level of contributions. This policy – the first-ever nationwide introduction of auto-enrollment – provides important lessons to policymakers around the world considering whether to introduce such schemes. In particular, it is useful for policymakers in the United States who are either implementing or considering similar policies.

In the United Kingdom, auto-enrollment has substantially increased retirement plan participation rates – to around 90 percent for workers at medium and large employers and 70 percent at small employers. Although most of the increase is among employees making minimum default contributions, the share of employees contributing at higher rates has also risen significantly.

Endnotes

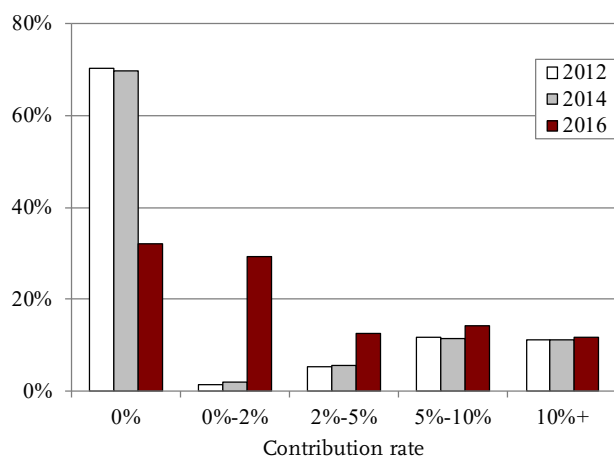
- 1 See Munnell, Belbase, and Sanzenbacher (2018).
- 2 See Ghilarducci and Fisher (2017).
- 3 Cribb and Emmerson (2016, 2019).
- 4 These ages are equivalent to the Earliest Eligibility Age in the U.S. Social Security system, which is 62 for both men and women.
- 5 See Cribb and Emmerson (2016).
- 6 See, for example, Choi et al. (2004).
- 7 See Cribb and Emmerson (2019).
- 8 See Cribb and Emmerson (2019).
- 9 See Cribb and Emmerson (2016).
- 10 Appendix Figure A1 shows the pattern for firms with 30-58 employees. See Cribb and Emmerson (2019) for more details.
- 11 Those working for employers with 3,000 to 29,999 employees may or may not have been re-enrolled – it is not possible to know without proprietary data on these plans. They are therefore excluded from the analysis.

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APPENDIX

FIGURE A1. DISTRIBUTION OF TOTAL CONTRIBUTION RATES AT EMPLOYERS WITH 30-58 EMPLOYEES, 2012, 2014, AND 2016



Note: Firm size is as of 2012.

Source: Cribb and Emmerson (2019).

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