New Policy Institute

The self-employed pension savings gap

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Key points

- The proportion of self-employed people contributing to a pension has more than halved in the course of a decade, falling from 36% in 2003/04 to just 17% by 2013/14.
- The self-employed lag far behind employees at all ages in terms of pension participation. Annual pension contribution rates peak at just 26% among the self-employed (at ages 45-54 and 55-59) but reach 65% for 45-54 employees.
- As household incomes rise, there is only a very limited increase in this proportion. Less than a quarter of self-employed adults with the highest household incomes (£1000 or more per week) were contributing to a pension in 2013/14.
- The trend for employees is very different. As household income increases, so does the proportion of employees paying in to a pension. Over 60% of employees with a household income of £1,000 or more were paying in to a pension scheme in 2013/14.
- Among those contributing to a private pension, employees tend to have greater household pension savings than self-employed people.
- The pension savings gap really starts to show among the over 45s. Among 45-54 year olds who have some private pension savings, the median value of employee pension savings is £140,000, more than double that of the self-employed (at £65,000).
- The pattern for cash savings is less clear. At age 55-64, there is no difference in household cash savings between self-employed and employee families – both types of family have average cash savings of around £7,000.
- But, self-employed families do tend to have higher household property wealth than employees. This is particularly apparent for older age groups: the median value of property wealth amongst those households headed by someone aged between 45 and 54 ranged from £225,000 for the self-employed to £145,000 for employee households.
- Turning to pension contribution levels at the household level, 63% of the self-employed (2.4 million) were not paying in to a pension and had no partner contributing to a pension in 2013/14. The share of employees in this situation was much lower, at 39%.
- The share of the self-employed with no pension coverage[1] drops by 20 percentage points when the current pension status of any partner is taken into

[1] I.e. either actively contributing to a pension, or living with someone who is

account. In comparison, the proportion of employees with no pension coverage fell by just 9 percentage points. The self-employed are therefore more reliant on their partner to provide them with some pension coverage than employees.

Introduction

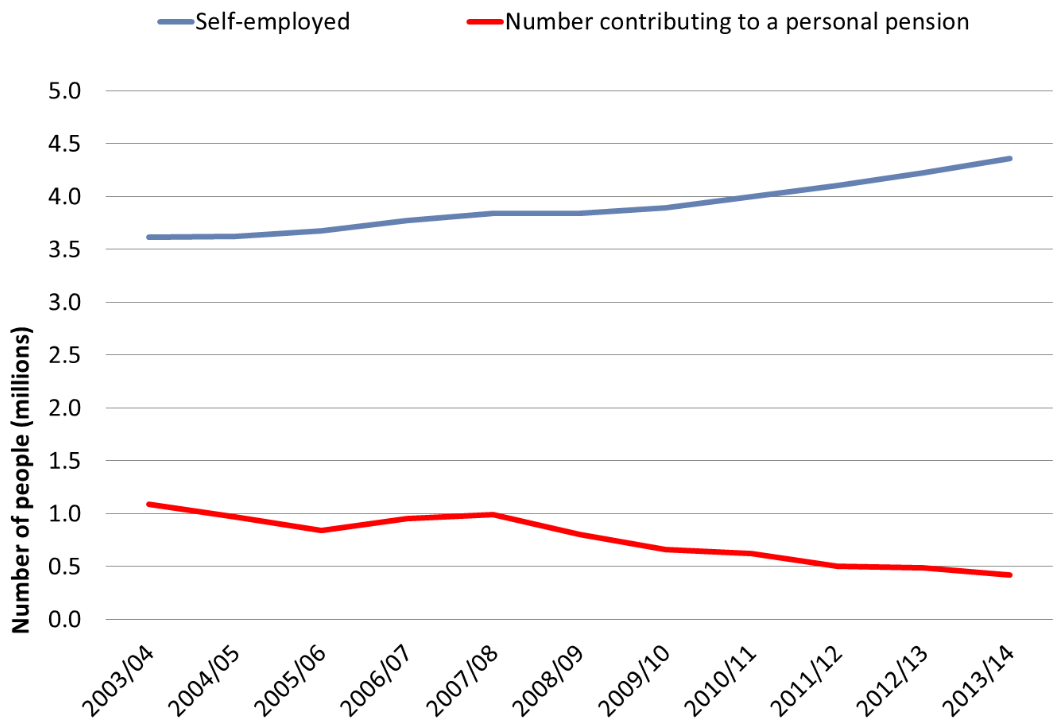
This paper explores current pension contribution levels amongst the self-employed. It provides an overview of the number of self-employed people paying into a pension and how this varies over time, and across different groups of the population.

We also explore the finding that pension contribution levels are very low amongst self-employed adults, considering whether this is linked to lower income levels, and whether the self-employed are making alternative arrangements to provide for themselves in retirement.

The analysis was commissioned by Citizens Advice, and is referenced in their recent work on self-employment.[2]

Pension contribution levels over time

Figure 1: Number of self-employed contributing to personal pensions (stakeholder and non-stakeholder), 2003/04 to 2013/14



Source: Labour Market Statistics & ONS Personal Pensions Statistics 2015.

In 2003/04 an estimated 1.1 million self-employed people were contributing to a personal pension. Since then there has been a marked decline, with the number

[2] https://www.citizensadvice.org.uk/shy-of-retiring/

more than halving to 450,000 people in 2013/14.[3] What is particularly striking about this decline is that it happened as the overall number self-employed was on the increase, with the result that there has been a fall in the share contributing to a pension.

Comparing the personal pensions data reported in figure 1 to the total number of self-employed people, we find that the proportion contributing to a pension has fallen from 30 per cent in 2003/04 to 10 per cent in 2013/14. This trend is confirmed by survey data, though the estimates for the proportion paying in to a pension start and end at a higher level over the same period. According to the Family Resources Survey (FRS), in 2003/04 36 per cent of the self-employed were contributing to a pension but by 2013/14 this had halved, falling to 17 per cent.

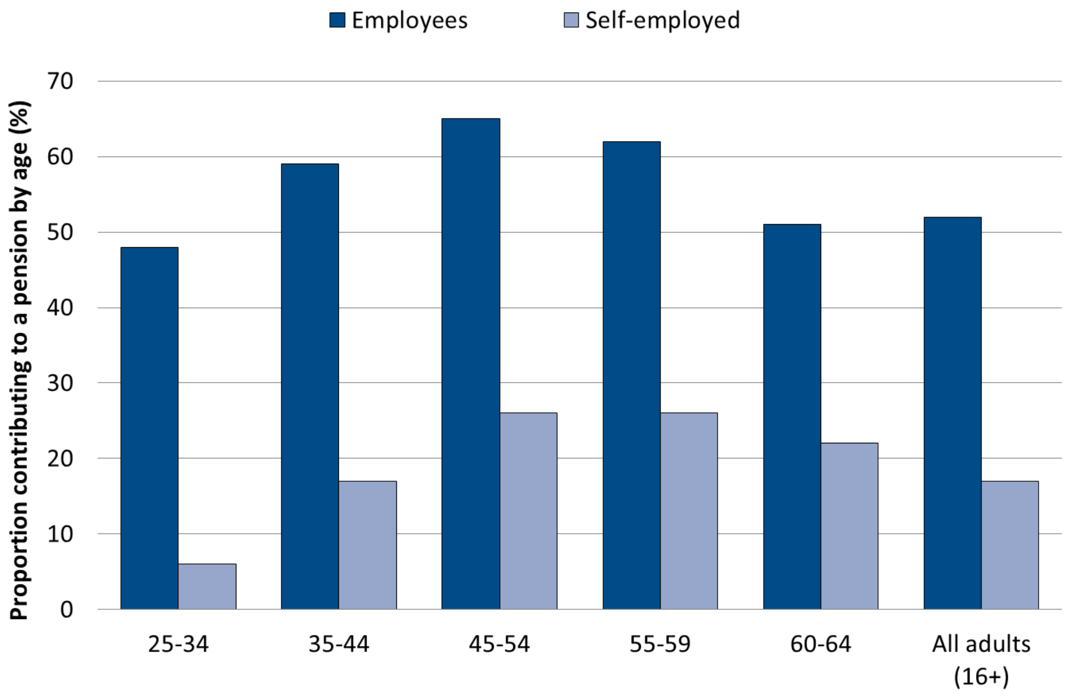
The rest of this paper draws on analysis of the Family Resource Survey (FRS) and the Wealth and Assets survey (2010/12) in order to look at how pension contribution levels vary by age, household income and for employee and self-employed families. The paper finishes by considering some explanations for low pension coverage amongst the self-employed, looking at whether the self-employed live with a partner who contributes to a pension and whether savings and investments might function as an alternative to pensions for some of the self-employed.

[3] The employment status that is recorded for people contributing to a pension is based on the information provided in the original pension application. Subsequent changes in employment status are not recorded. This means, for example, that people who start paying in to a pension when they are employed and who then move into self-employment and continue contributing to the same personal pension will not be included in this data.

Pension contribution levels remain low across different groups

Pension contributions by age

Figure 2: Proportion contributing to a pension by age and employment status, 2013/14



Source: Family Resources Survey, DWP.

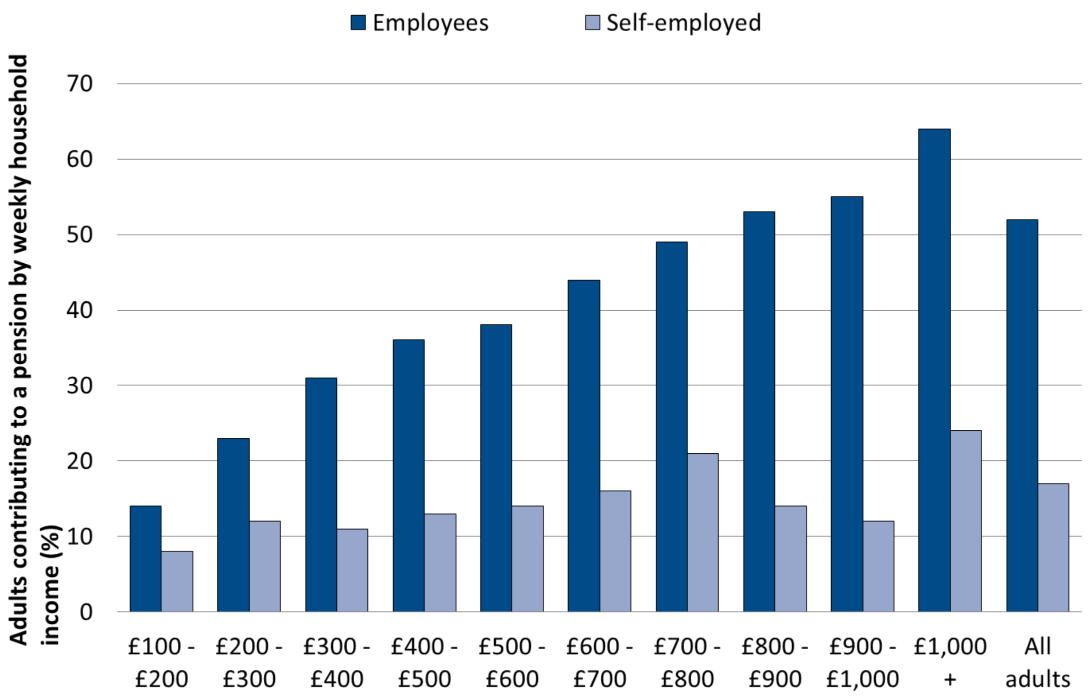
Pension contribution levels among the self-employed are uniformly low in comparison to employees. Focussing on working-age adults, the proportion of self-employed adults paying in to a pension starts as low as 6 per cent among 25-34 year olds and peaks at just 26 per cent (among those aged 45-54 and 55-59).

In contrast, the majority of employees are paying in from the age of 35 and up. Amongst employees aged between 45 and 54 – the age group most likely to be paying in to a pension – 65 per cent were paying in to a pension in 2013/14.

Pension contributions by weekly household income

We have previously highlighted the fact that the self-employed tend to have lower incomes.[4] One potential explanation for poor pension contribution rates amongst the self-employed is that these lower incomes prevent them from contributing to a pension. The graph that follows describes how pension participation rates in 2013/14 vary with weekly household income levels.

Figure 3: Proportion contributing to a pension by weekly household income and employment status, 2013/14



Source: Family Resources Survey, DWP. Estimates for adults in households with an income of less than £100 are not presented due to small sample sizes.

Pension participation among self-employed people tends to be less than half the figure for employees, whether household income is £200 or £1,000 per week.[5] Moreover, as household incomes rise, overall participation levels increase much more for employees than the self-employed.

In 2013/14 8 per cent of self-employed adults with some of the lowest levels of household income (£100 to just under £200) were paying in to a pension. This is

[4] Tinson, A. (2015) Who are the self-employed? CAB & NPI

[5] Only among households with income of between £100 and £200 does the proportion of self-employed paying in to a pension equal more than half of the share of employees paying in to a pension, at 8 and 14 per cent respectively.

extremely low, though it is understandable given the limited income that this group have to live on. But just 21 per cent of self-employed adults with a combined household income of £700-£800 per week were paying in to a pension in 2013/14. Beyond this income level the proportion dips slightly before it increases again for those with a household income of £1,000 or more, reaching 24 per cent. This is still incredibly low, particularly given the amount of income that is presumably available to adults in this situation.

In contrast, there is a clear household income gradient among employees. As household income increases, so does the proportion of employees paying in to a pension. Only 14 per cent of employees with a combined household income of between £100 and £200 were paying in to a pension in 2013/14, compared to over 60 per cent of employees with a household income of £1,000 or more.

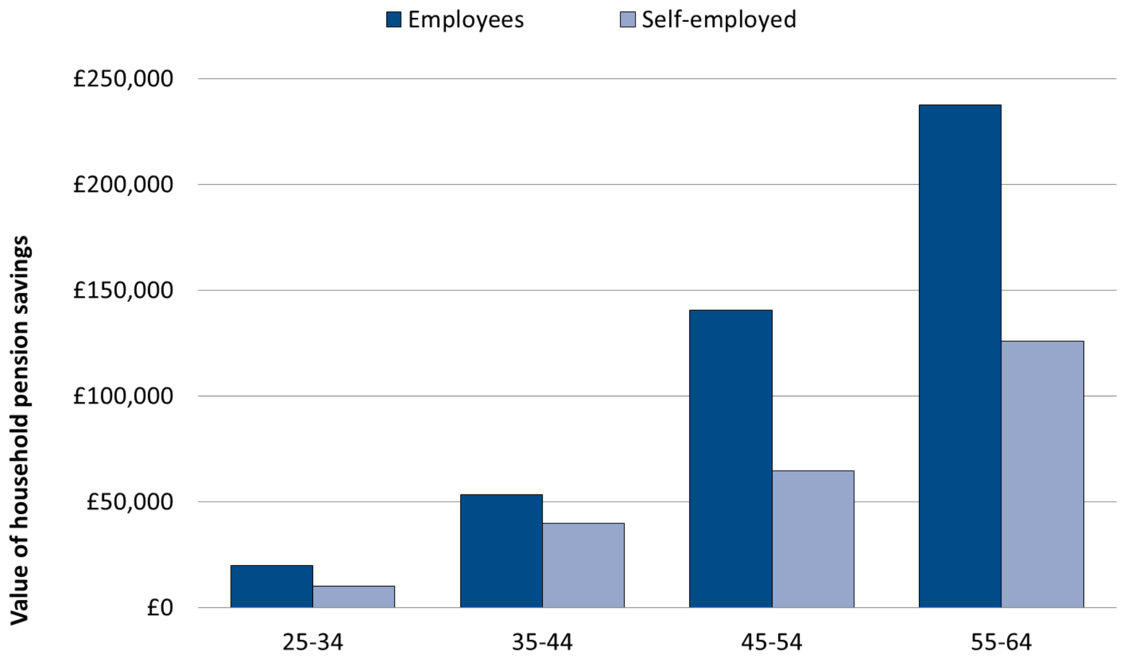
Value of pensions

The graphs above show that self-employed people are less likely to contribute to pensions than employees. Another way of looking at it is by analysing the size of the pension pot that people have saved. The following graph provides this perspective, showing the value of pension savings among households with these savings in 2010/12.

The source is the Wealth and Assets Survey, covering the years 2010-12[6]. Figures are given at a household level, broken down by the employment status of the household reference person. Given that the value of savings increases as retirement approaches, the graph breaks down the results by age group.

[6] In the Wealth and Assets survey, private pension wealth is the sum of the value of current occupational pension wealth, retained rights in occupational pensions, current personal pension wealth, retained rights in personal pensions, Additional Voluntary Contributions (AVCs), value of pensions expected from former spouse or partner and value of pensions in payment.

Figure 4: Median value of pension savings by age and employment status of household head, 2010/12



Source: Wealth and Assets Survey. Medians are reported for employee and self-employed households with pension savings

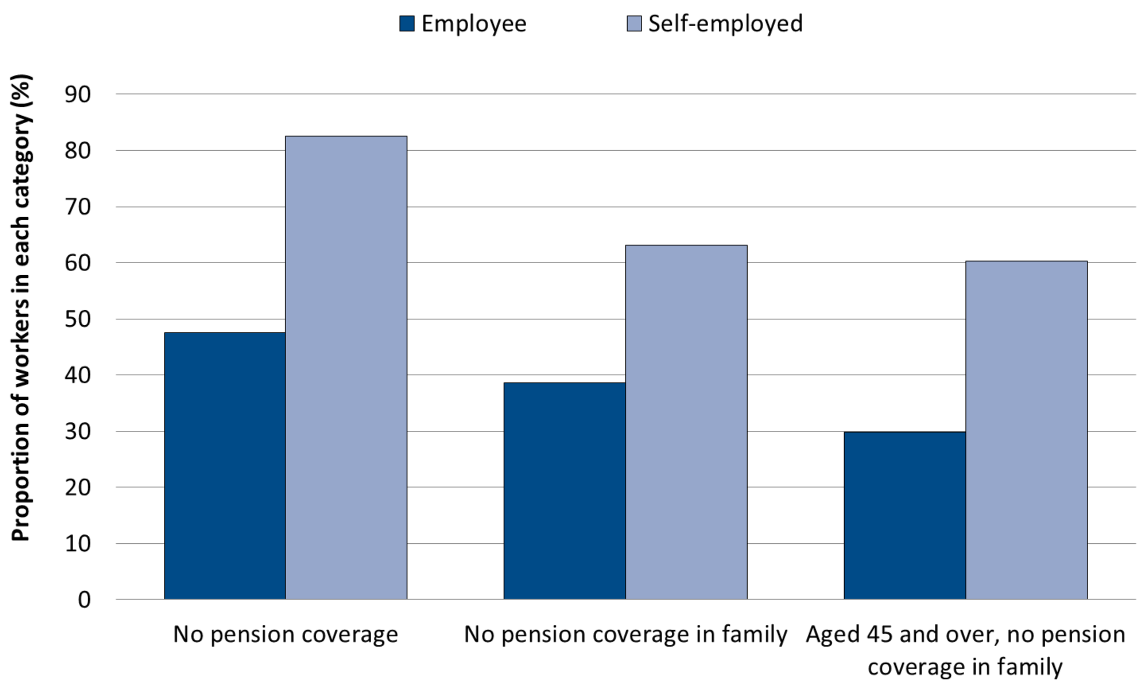
From the age of 25 onwards, among those with some pension savings, employees tend to have greater household pension savings than self-employed people. This gap really starts to show among the over 45s. Among those aged 45-54 who have some private pension savings, the median value of employee pension savings is £140,000, more than double that of the self-employed (£65,000).

Among those closest to retirement, median pension savings among the self-employed are around £125,000, just over half that of employees (£235,000). So not only are contribution rates low, but among those who do contribute, the level of contribution among self-employed people is lower than employees.

Pension contributions at a household-level

We now turn to consider whether the self-employed live with a partner who is contributing to a pension.

Figure 5: People lacking pension coverage within family, 2013/14



Source: FRS 2013/14

Figure 5 presents data on the proportion of people who are not currently contributing to a pension and who have no other person actively contributing to a pension in their family.[7] This is of interest because it may be that people with no pension may intend to share their retirement finances with other people who do, though relying on someone else's future pension income is a risky approach.

In light of the low pension contribution rates noted previously, it is not surprising to find that the self-employed are more reliant on their partner to provide them with some pension coverage than employees. The share of the self-employed with no pension coverage drops by 20 percentage points when the current pension status of any partner is taken into account. In comparison, the proportion of employees with no pension coverage falls by just 9 percentage points when partner contributions are taken into account. Overall 63 per cent of the self-employed (2.4 million) were not paying in to a pension and had no partner contributing to a pension in 2013/14.[8] The share of employees in this situation was much lower, at 39 per cent.

[7] The analysis is at the level of a 'benefit unit', which means that the 'family' may consist of a single adult or a couple, and any children.
[8] Some reported that they did not have a partner, others had a partner who was also not contributing to a pension

Perhaps of even greater concern is the high proportion of older self-employed people who are not contributing to a pension and have no other person in their family contributing to a pension: some 1.3 million self-employed people aged 45 and over (60 per cent) were in this precarious situation in 2013/14, compared to 30 per cent of employees.

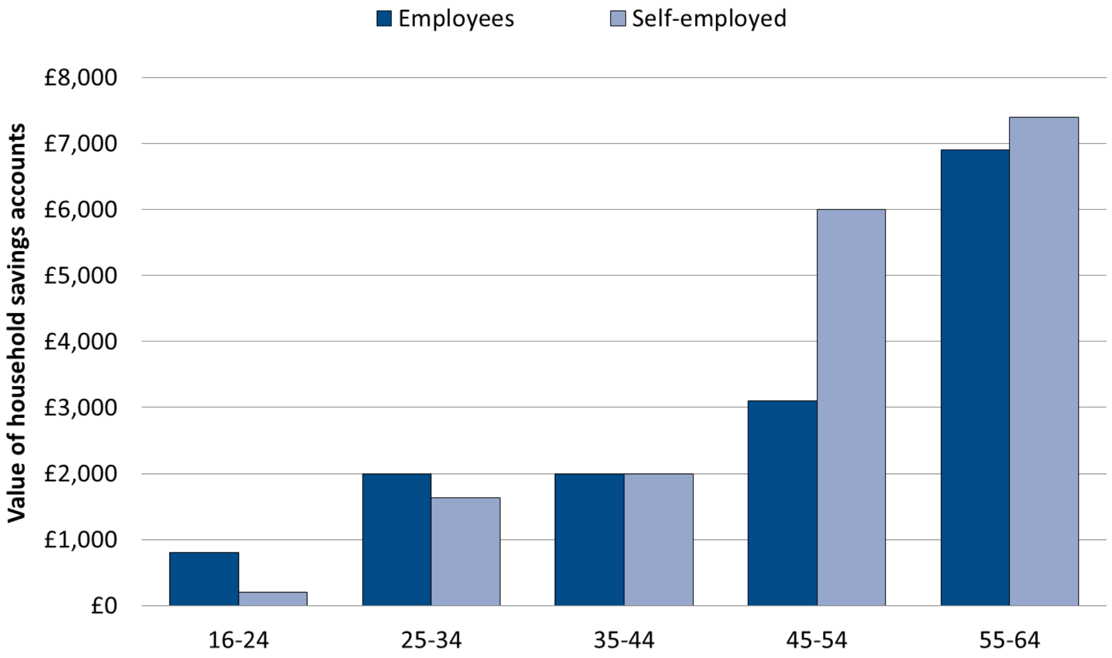
Alternative savings options

The graphs in this section consider whether the self-employed have more household savings or property wealth, which might support them in retirement.

Cash savings by age

The next graph describes the value of household savings by age group, amongst those households that have savings. The figure given is the median level of savings for each household type, for 2010/12.

Figure 6: Median value of household savings by age and employment status of household head, 2010/12



Source: Wealth and Assets Survey. Medians are reported for employee and self-employed households with money in household savings accounts

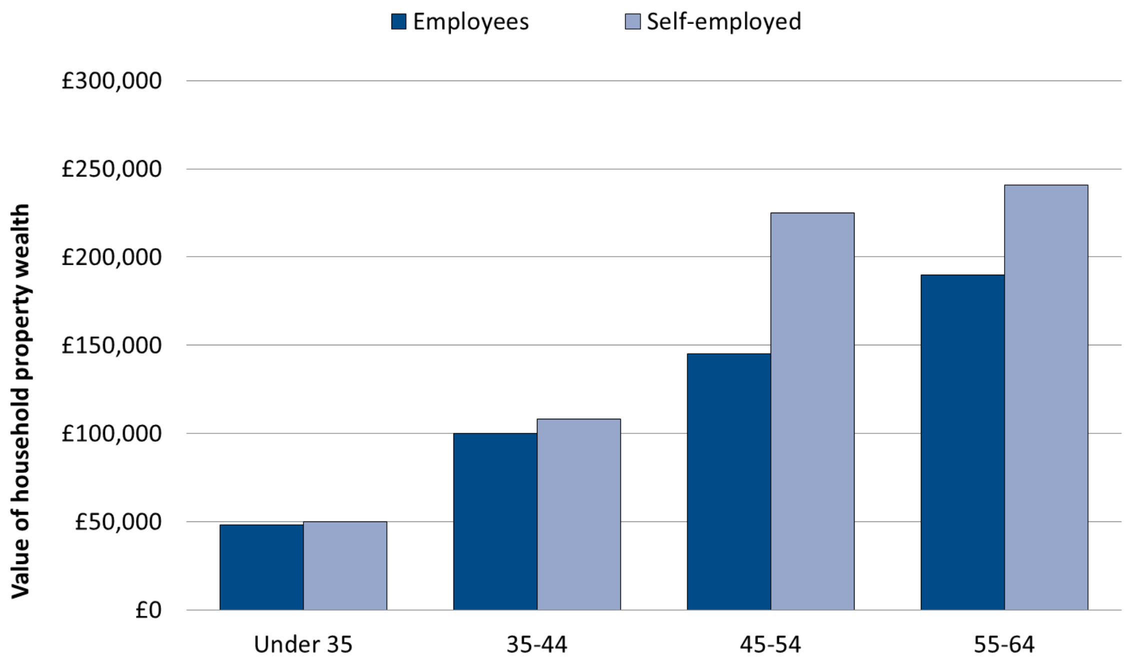
The difference between self-employed and employee family types is much less clear for cash savings than it was for pension savings. Among younger age groups, savings are low and there is no difference between employment statuses. Among those aged 45-54, savings in self-employed families are, at £6,000, twice as high as among employee families. But at age 55-64, there is no difference – both types of family have average savings of around £7,000.

It is hard, then, to discern a pattern or consistent difference between the groups. But there is certainly no evidence to support the idea that the reason pension savings are so low among self-employed people is that they use cash savings instead. The value of cash savings is no higher among self-employed people than among employees.

Property wealth

The next graph shows levels of property wealth. It gives the median value of household net property wealth amongst those who owned property in 2010-12[9]. To frame these figures, it is worth noting that households headed by a self-employed person were slightly more likely to have some property wealth (81 per cent of households) than households headed by an employee (74 per cent).

Figure 7: Household property wealth 2010/12



Source: Wealth and Assets Survey. Data for employee and self-employed households with property wealth greater than zero, values are rounded

Self-employed households tend to have higher property wealth than employee households. This is particularly apparent for older age groups: the median value of

[9] People with negative total property wealth at a household level are excluded from the estimates (comprising approximately 1% of the self-employed and 2% of employees), as well as those reporting property wealth to be zero. The figures are for net values.

property wealth amongst those households headed by someone aged between 45 and 54 ranged from £225,000 for the self-employed to £145,000 for employee households.

Yet self-employed people aged under 45 have no more property wealth than employees. What we cannot tell from the graph is whether the additional property wealth of older self-employed people compared to employees is due to additional investment in older working age or a simple cohort effect that will fade over time.

Conclusion

This paper has shown that there is a clear pension savings gap among the self-employed. The proportion of self-employed adults who are paying in to a pension each year has been declining, falling to just 17 per cent in 2013/14.

Pension participation levels among self-employed people are consistently lower than employees. This is true across different age groups and at different levels of income. The pension pots of self-employed households are also worth less than employee pension pots, so self-employed people are less likely to save than employees and tend to save less when they do.

Though some self-employed people could be compensating by investing in property, it is not clear that any accumulated wealth will be sufficient to offer security in retirement, with implications for the future living standards of the self-employed.