

AAT RESPONSE TO THE DEPARTMENT FOR WORK & PENSIONS “AUTOMATIC ENROLMENT EARNINGS THRESHOLDS REVIEW AND REVISION 2015/2016”

1 EXECUTIVE SUMMARY AND OVERVIEW

1.1 There have been significant changes within the pension industry over the last decade and there is more to come. This includes:

- Changes to the state pension rules,
- The qualifying scheme charge cap, and
- The new pension freedoms.

There is evidence of both payroll and pension provider I.T issues¹, which are causing problems for key stakeholders. In recognition of this we recommend, whatever decision is taken regarding the earnings trigger, that there is guidance and confirmation of the intentions for future years. This will allow all stakeholders to plan effectively.

1.2 From a payroll perspective this would allow payroll providers to build robust systems for 2015/16 and beyond. From an employer’s perspective this would aid them in budgeting and estimating future pension costs.

1.3 We believe the general consensus is that the automatic enrolment earnings trigger and the qualifying earnings band should be made as simple as possible. This is to aid effective communication to all parties but especially employers and employees. With the increase in the numbers of employers staging in the tax year 2015-16 and beyond, an easily communicated message is paramount.

1.4 When evaluating the advantages and disadvantages of the four options outlined for the 2015/16 earnings trigger, AAT favours Option 3 - increase the trigger to £10,500 in line with the threshold for paying income tax.

1.5 If AAT’s favoured option was discounted, then AAT’s second choice would be Option 1 - to freeze the trigger at its current rate of £10,000. As an alternative (See Q5) pegging the earnings threshold to the lower qualifying earnings, also, has its merits.

1.6 AAT would prefer that Option 2 - raise the Trigger by Indexation and Option 4 - use the Pension Commission’s Benchmark Replacement Rate to determine the trigger, not to be the option(s) selected by the DWP.

1.7 With regard to the qualifying earnings band AAT would suggest ensuring the link between the band earnings and qualifying earnings remains.

¹ The Telegraph, 6 Sept 2014, [“Pensions meltdown threatens savings revolution”](#)

- 1.8 There is still much debate, confusion and even uncertainty with employers and pension experts alike with regards to certain employers' automatic enrolment responsibilities. For example, the effect of automatic enrolment legislation with regards to close companies. AAT recommends that the Pensions Regulator moves to clarify the position.
- 1.9 AAT believes there is scope for further simplification of auto enrolment responsibilities generally. This is especially relevant to ensure smaller businesses who have limited HR and payroll resources remain compliant.

2 RESPONSE TO QUESTIONS FOR RESPONDENTS

Question 1

Are there any other factors that should be taken into account in the review of the automatic enrolment earnings trigger for 2015/2016? If so please explain.

- 2.1 AAT considers that the DWP should maintain consistency with other statutory requirements. Any values they use must be in existence for income tax and National Insurance purposes.
- 2.2 AAT believes simplicity is key to ensure all stakeholders are prepared for 2015/16 changes and beyond.
- 2.3 It is common sense to future proof the earnings trigger and qualifying earnings definition for subsequent tax years.

Question 2

Is it your experience that alignment with an existing payroll threshold reduces complexity? If so, please explain the impact upon you or your clients of

- a) **freezing the trigger or**
- b) **increasing in line with indexation**

- 2.4 AAT strongly believes that alignment with an existing payroll threshold helps to reduce complexity.
- 2.5 For those clients whose payroll system has an automatic enrolment pension module this may result in their facing an increased administrative burden to ensure their systems are fit for purpose. For those clients who may do this

manually, (we envisage some small employers will do this), it represents an even greater burden with the requirement to consider an extra threshold adds further confusion.

- 2.6 Based on our knowledge of key stakeholders, AAT considers that there is enough evidence to suggest that there are I.T. issues facing payroll providers, middle-ware providers and pension providers.

Question 3

Which of the four options do you favour and why?

- 2.7 AAT considers that linking the earnings threshold to the personal allowance is simple and transparent. It is relatively easily communicated rather than having a separate payroll threshold. In this age of huge complexity the average individual does not want another set of guidelines to work towards and this, assuming the current custom and practice is to continue, would give it natural inflation proofing.
- 2.8 If the DWP opted to link the earnings threshold to the personal allowance until further notice the decision would enable stakeholders to plan.
- 2.9 However, it should be noted, if the automatic enrolment threshold was to continue to increase more people will be excluded from benefitting from their employer's contribution. As salaries have not kept up with cost of living increases a greater number of people could be excluded.
- 2.10 Though point 2.9 is correct the workers who earn above the qualifying earnings limit would be allowed to opt in and then receive the employer contribution. The non-eligible job holders would have this message communicated to them by letter or email.
- 2.11 Some political parties have suggested that the personal allowance could increase further². This could result in a greater number of people not being automatically enrolled. Alternatively, if the personal allowance was reduced, due to the need to increase taxes, and it was the link to the automatic enrolment earnings trigger, many employers could be affected by having to pay additional pension contributions for those previously non-eligible job holders.
- 2.12 Linking the automatic earnings trigger to the personal allowance has an attraction because pension contributions will be lower for the next few years and, until the automatic transfer of an individual's pension pot is in place, it could mean people build up numerous small pots which are inefficient and costly to administer.

² City a.m. article, 1 October 2014, [Conservative party conference 2014: We'll raise personal allowance to £12,500 and the 40p tax threshold, says David Cameron](#)

- 2.13 When considering each of the four options it is AAT's opinion that despite potential drawbacks, Option 3 – increase the trigger to £10,500 in line with the threshold for paying income tax is the preferred option.
- 2.14 AAT recommends that the DWP should maintain consistency with other statutory requirements. Any values they use must be in existence for income tax and National Insurance purposes. By pegging the automatic earnings threshold to the personal allowance the threshold does not have to be considered/reviewed again.
- 2.15 Similarly, as suggested in Question 5, if the DWP peg the automatic earnings threshold to the National Insurance level (either the lower earnings threshold or primary threshold) then once again the earnings threshold does not have to be reviewed.

Question 4

What pensions tax relief arrangement do you (or your clients) use and why?

- 2.16 Most existing pension providers who now offer new qualifying schemes and/or auto enrolment schemes are predominantly offering terms as Group Personal Pensions (GPP), with the tax relief given at source.
- 2.17 Whereas, providers who have recently entered the market offering a master trust occupational pension scheme which includes Nest, The People's Pension and Now: Pensions all offer different tax relief arrangements.
- 2.18 Nest offers relief at source (RAS). Therefore employee contributions are paid net and then government tax relief is then added.
- 2.19 Now: Pensions offers the net pay arrangement (NPA). Therefore contributions are collected gross.
- 2.20 The People's Pension offers both options.
- 2.21 Anecdotally we understand employers are making use of salary exchange schemes. This has tax and National Insurance contribution advantages for both the employee and employer contribution. The contributions are paid over gross by the employer.
- 2.22 Both the NPA and RAS arrangement have advantages and disadvantages.
- 2.23 The NPA ensures higher rate tax relief immediately for those eligible.
- 2.24 With the RAS arrangement a higher rate tax payer would have to claim back the extra tax relief through their annual tax return.

- 2.25 Non-tax payers cannot claim the tax relief through NPA schemes.
- 2.26 Non-tax payers benefit from tax relief through RAS schemes.
- 2.27 It is our understanding of the pensions provision market that RAS's are the main type of arrangement being used for new schemes.

Question 5

Are there any other options we should be considering?

- 2.28 There are three potential options which are all worthy of consideration.
- 2.29 "Option 1 Plus". This is as Option 1. Therefore the automatic enrolment earnings trigger is kept at £10,000. However the DWP confirm that this figure will be reviewed on a triennial basis. This would mean all stakeholders would know where they stood for the next three years.
- 2.30 It should be noted that over time inflation would erode the difference between the earnings trigger and the qualifying band which could then be reviewed.
- 2.31 One benefit of this option is that it allows more workers over time to be automatically enrolled. When contributions increase to 8% in October 2018 the pension contributions and their associated pension pots will become more significant.
- 2.32 Option 2, an alternative option to Option 1 plus, could be to link the earnings trigger to the living wage rate. This living wage has been set at £7.85 per hour as of November 2014. (Source: Livingwage.org).
- 2.34 The Living Wage is calculated according to the basic cost of living in the UK The living wage is currently calculated by the Centre for Research in Social Policy at Loughborough University, while the London Wage (£9.15) has been calculated by the Greater London Authority since 2005.
- 2.35 Based on somebody working either a twenty, thirty or forty hour week the earnings thresholds for automatic enrolment purposes could be £8,164; £12,246 and £16,328 based on £7.85 per hour.
- 2.36 Option 3 would be to use the lower earnings limit/lower band of qualifying earnings as the earnings trigger and abolish the current auto enrolment trigger and peg the auto enrolment earnings trigger to the lower earnings limit.
- 2.37 This would mean an employer would have increased costs if they used qualifying earnings rather than the current £10,000 earnings trigger as their pensionable definition. However, this would also result in larger contributions being invested into pensions.
- 2.38 Though this would result in more workers being enrolled and at a lower level of earnings, individuals who felt they could not afford it could still opt out.

- 2.39 Though those earning just over the lower qualifying earnings band would have small pension contributions, the new pension flexibility being introduced in the 2015/16 tax year will encourage more people to save into pensions and even those with small pots would be worthwhile.

Question 6

Would any of the four options have a disproportionate or unreasonable impact upon any particular sectors of the population? Please explain why and how

- 2.40 AAT is concerned that even at the current automatic earnings trigger of £10,000 many of the low earners whom the government would want to save towards a pension are excluded.
- 2.41 Option 2 and Option 3 would mean a number of workers would not be automatically enrolled. Those who were on £10,000 and up to the revised earnings trigger would not be automatically enrolled. However, as previously stated those that could be excluded can opt in if they are a non-eligible job holder.
- 2.42 With the basic state pension age being reviewed regularly with the prospect of a later state pension age than currently stated, it could be argued that it is even more important for low earners to save into a pension if they would like to retire before their state pension age.
- 2.43 Option 1 and Option 4 would result in a greater number of workers being enrolled. (This assumes wage inflation with regard to Option 1). This would result in more workers being automatically enrolled and higher pension contribution costs for employers.

Question 7

Are there any other factor that should be taken into account in the review of the qualifying earnings band lower limit for 2015-2016? If so please explain why.

- 2.44 AAT believes if the qualifying earnings band lower limit is to be kept then ensuring it is pegged to National Insurance lower earnings limit is appropriate.

Question 8

Has alignment with the National Insurance lower earnings limit caused any problems? If so please explain.

- 2.45 There have been some communication issues with employee engagement. Low earners particularly have said it is not worth opting in on a qualifying earnings scheme. Individuals understand what basic pay means.
- 2.46 If banded earnings are still to be used AAT considers they should remain being aligned with the lower earnings limit in order to avoid confusion and error. In particular, now that auto enrolment is moving into a period where smaller entities are affected, they in particular will need consistency of values otherwise such business owners will simply not be able to comply.

Question 9

Are there any other factors that should be taken into account in the review of the qualifying earnings band upper limit to 2015/2016? If so please explain why.

- 2.47 AAT considers if there is to be an upper limit to the qualifying earnings band upper limit to 2015/2016 then it should remain aligned to the upper limit for National Insurance contribution purposes.
- 2.48 Further simplification could be achieved by changing the definition of qualifying earnings, by removing the qualifying upper and lower band earnings option and using the basic pay and total pay definitions. As Individuals understand what basic pay is whereas communicating banded earnings can cause some confusion.
- 2.49 However, if our suggestion was to be taken forward that would lead to larger pension contributions for employers.
- 2.50 A consequence of the above (2.47 - 2.49) would be the receipt of greater pension contributions being paid on behalf of individuals and as a result individuals would benefit from higher pension contributions and therefore can expect to benefit from larger pension pots.

Question 10

Has alignment with the National Insurance upper earnings limit caused any problems? If so please explain.

- 2.51 AAT is pleased to report that in general our response to question 10 is, no.
- 2.52 However, AAT is aware of a recruitment company which pays its employees a low basic salary linked to a high bonus. In this scenario the employer concerned did not want to use qualifying earnings definition³ as the costs were quite high. The employer opted for a basic pay definition but they then failed the 85% of earnings rule which resulted in them having to pay an additional employer contribution.

3 CONCLUSIONS

- 3.1 With the proposed new pension freedoms being introduced, people will have more choices as to how to take their retirement income when they get to age 55 and saving for retirement is likely to become more attractive.
- 3.2 AAT considers that as employer's automatic enrolment responsibilities can be complex, a vital component to the success of auto enrolment is ensuring rules and definitions and earnings triggers are kept as simple as possible for all stakeholders (1.1 above). Simplicity will have a disproportionately higher impact and will be particularly significant for smaller employers and their employees.
- 3.3 AAT also believes that it is vital for employers to be informed as soon as possible with regard to any proposed changes. The more notice that the key stakeholders have the better it will be in terms of successful planning and implementation (1.1 and 2.3 above).
- 3.4 Band earnings can significantly diminish savers' pension pots and disadvantages people on low income particularly. Low earners were/are a segment of the population which the workplace pension was designed for. Someone earning £10,000 only receives a total contribution of 3.4% (based on qualifying earnings band salary definition).
- 3.5 AAT believes there is scope for a wider consultation with regards to auto enrolment focusing on further simplification, definition of earnings, the actual minimum contribution rates moving forward from October 2018.

³ <http://www.nestpensions.org.uk/schemeweb/NestWeb/public/helpcentre/contents/qualifying-earnings.html>

4 ABOUT THE AAT

- 4.1 The Association of Accounting Technicians (AAT) is pleased to take part in this opportunity to comment on the DWP's consultation on revision proposals for the automatic earnings trigger and the qualifying earnings band.
- 4.2 AAT has over 49,800 Members and 80,000 Students worldwide (correct as at 30 Sept 2014).
- 4.3 AAT has over 4,100 Members in Practice who provide accounts and tax services, including assisting companies to meet their statutory filing obligations to circa 350,000 sole traders, partnerships and limited companies, covering a full range of businesses, particularly small and medium-sized enterprises and owner-managed entities.
- 4.4 AAT is a registered charity whose objectives are to advance public education and promote the study of the practice, theory and techniques of accountancy and the prevention of crime and promotion of the sound administration of the law.
- 4.5 In pursuance of those objectives AAT provides a membership body. AAT are participating in this consultation not only on behalf of our membership but also from the wider public benefit perspective of achieving sound, effective and transparent information with regards to workplace pension reform.
- 4.6 AAT has consulted with a few key stakeholders with regards to this consultation. These include employers, pension providers, some AAT members, and payroll managers, accountants, financial advisers and employee benefit consultants.

Further engagement

If you have any questions or would like to consult further on this issue then please contact:
email: consultation@aat.org.uk and aat@palmerco.co.uk

telephone: 020 7397 3088

Aleem Islan
Association of Accounting Technicians
140 Aldersgate Street
London
EC1A 4HY