

Pensions Bulletin

Fact Sheet I

Spring 2009 Issue 4

Auto-enrolment and Personal Accounts

I Executive summary

- 1.1 Most of the detail about auto-enrolment and Personal Accounts was contained in a White Paper 'Personal Accounts – a new way to save' published in December 2006, and the Government's response to consultation, published in June 2007.
- 1.2 The measures to implement this new system are contained in the Pensions Act 2008, which received Royal Assent on 26 November 2008.
- 1.3 From 2012, the legislation requires employers to automatically enrol eligible workers into a pension scheme that meets certain criteria or the new Personal Accounts scheme being set up by the Secretary of State for Work and Pensions. Workers who 'opt-out' will have to be automatically re-enrolled at regular intervals.
- 1.4 Subject to transitional provisions, all employers will be required to contribute a minimum of 3% (on a band of earnings) to an eligible worker's pension arrangement. This will supplement the 4% that must be paid by employees and there will be around 1% from the Government in the form of tax relief.
- 1.5 The new employer duty will be enforced by The Pensions Regulator.
- 1.6 From 2012, a new low cost saving vehicle (the Personal Accounts scheme) will be introduced. This will be aimed at employees who don't have access to a good quality work based pension scheme - in the main, median to low earners.

2 Auto-enrolment – employer duties

- 2.1 In the case of a "jobholder", aged at least 22 but under state pension age, an employer must make arrangements by which the jobholder becomes an active member of an "automatic enrolment scheme". This requirement does not, however, apply if the jobholder is already an active member of an occupational or personal pension scheme that meets certain criteria (see section 4 below on "qualifying schemes").
- 2.2 *Definition:* A "jobholder" is a worker:
 - a) who is working or ordinarily works in Great Britain under the worker's contract;
 - b) who is aged at least 16 and under 75; and
 - c) to whom "qualifying earnings" (see section 3 below) are payable by the employer.
- 2.3 *Definition:* An "automatic enrolment scheme" is an occupational or personal pension qualifying scheme which enables an employer to make the auto-enrolment arrangements described elsewhere in section 2 of this Fact Sheet.

- 2.4 Workers who meet parts a) and b) of the definition of jobholder but not part c), because they don't have qualifying earnings, can require their employer, by notice, to arrange for them to become active members of a registered pension scheme.
- 2.5 The Personal Accounts Delivery Authority (PADA), the body responsible for setting up the Personal Accounts scheme, has stated that the start date for auto-enrolment into pension schemes will be October 2012. It was originally thought that the start date would be April 2012.

3 Auto-enrolment - qualifying earnings

- 3.1 A person's "qualifying earnings" in a pay period of 12 months are gross earnings between £5,035 and £33,540. In the case of a pay period of less or more than 12 months, this provision applies as if the amounts were proportionately less or more.
- 3.2 The qualifying earnings band is subject to review each tax year and is expected to rise in-line with increases in the general level of earnings.

4 Auto-enrolment - qualifying schemes

- 4.1 To be a "qualifying scheme", a pension scheme must meet certain requirements. These depend on how the scheme is constituted and, in the case of occupational schemes, whether the scheme is defined contribution (DC) or defined benefit (DB).
- 4.2 For a DC scheme to qualify, contributions must at least match what would be paid into a Personal Account. In particular:
- the employer's contribution must be equal to or more than 3% of the jobholder's qualifying earnings; and
 - the total amount of contributions paid by the jobholder and the employer must be equal to or more than 8% of qualifying earnings.
- 4.3 A DB scheme will qualify automatically if it is contracted-out of the state pension. If a DB scheme is not contracted-out, it must provide an accrual rate of at least 1/120th of the member's average qualifying earnings in their last three tax years for each year of scheme membership.
- 4.4 For personal pensions (which includes stakeholder pensions), four conditions must be satisfied:
- all of the benefits provided must be money purchase benefits;
 - there must be an agreement between the scheme provider and the employer under which the employer will pay contributions equal to or more than 3% of the jobholder's qualifying earnings;
 - if there is a shortfall between the employer's contribution and 8% of the jobholder's qualifying earnings, there must be an agreement between the provider and the jobholder under which the jobholder will pay contributions which are equal to or more than the shortfall;
 - there must be direct payment arrangements providing for the employer to pass on contributions to the provider.
- 4.5 For DC and personal pension schemes, the legislation will allow employers to "self certify" that their pension scheme meets the requirements to be a qualifying scheme. This self-certification will be based on the expected value of pension contributions to be made over the course of each coming year. Once certified, employers will not have to make retrospective reconciliation payments if contributions unexpectedly fall short, unless the detriment to a jobholder exceeds certain minimum levels. These levels will be set in such a way to protect jobholders from significant, systematic or persistent detriment.

5 Auto-enrolment – phasing in of contributions

- 5.1 The requirements outlined in sections 2 to 4 above are to be phased in over transitional periods. The arrangements for these transitional periods operate differently for different types of pension schemes.
- 5.2 For DC and personal pension arrangements, contributions will be phased in. In the first transitional period, which will last at least one year, the minimum employer contribution will be 1% and the minimum overall contribution 2%. In the second transitional period, which will also last at least one year, the minimum contributions are 2% and 5%, respectively. Thereafter, contributions revert to the minimum employer contribution of 3% and minimum overall contribution of 8%.
- 5.3 For DB schemes, there is just one transitional period, which only affects existing jobholders who have previously been and remain able to join the scheme. For such jobholders, the employer does not have to make arrangements for them to become active members until the end of a period prescribed in regulations. In practice, given the number of closed schemes, this transitional period will not be relevant to many employers.

6 Auto-enrolment – compliance

- 6.1 Under the regulations, trustees of occupational pension schemes are given the power to modify their schemes by resolution to ensure compliance with provisions relating to automatic enrolment or to increase contributions to the required levels. It should be noted that no modification can be made without employer consent.
- 6.2 Employer duties will be enforced by The Pensions Regulator, which is given a new statutory duty of maximising compliance with the duties. A whole chapter of the 2008 Pensions Act is devoted to the subject of “compliance” and key provisions include the following:
- Powers for the Regulator to issue “compliance notices” and/or “unpaid contributions notices” if employers contravene their new duties.
 - A power for the Regulator to issue “fixed penalty notices” if an employer fails to comply with a compliance notice or unpaid contributions notice. Fixed penalty notices can also be issued for contravention of employer duties. The penalty cannot exceed £50,000, but provision exists for “escalating penalty notices” if there is continued non-compliance with a notice issued by the Regulator.
 - The creation of new offences for employers that wilfully fail to comply with their duties relating to automatic enrolment, re-enrolment and jobholder’s right to opt-in.
- 6.3 Other provisions that employers need to be aware of are the rules on “prohibited recruitment conduct” and “inducements”, as follows:
- An example of prohibited recruitment conduct would be where a job advertisement indicated that the applicant might stand more chance of success if he was prepared to opt-out of pension scheme auto-enrolment.
 - Inducement is considered to be any action taken by an employer for the sole or main purpose of trying to force or encourage an individual to opt-out of, or cease, pension scheme membership.

7 Personal Accounts

- 7.1 To help employers comply with their new duties, the 2008 Pensions Act provides that the Secretary of State for Work and Pensions must set up a new pension scheme. This scheme will be treated as being established under irrevocable trust (and run by trustees), will be tax registered (so tax relief is given on contributions), will provide DC benefits and will enable employers, by participating in the scheme, to comply with the pension scheme enrolment requirements described above.

- 7.2 A lot of the detail for the administration and management of the new scheme, which has become known as the “Personal Accounts” scheme, will be set out in secondary legislation and rules made by the trustees or Secretary of State, but some of the key features are detailed below:
- To ensure members and employers are consulted about the operation, development and amendment of the Personal Accounts scheme, there will be a “members’ panel” and an “employers panel”.
 - Secondary legislation must set out a maximum amount of contribution that may be made by or in respect of a member in any tax year (of £3,600 per annum, based on 2005 earnings levels).
 - It is expected that there will be restrictions on rights to transfer in and out of the Personal Accounts scheme.
 - Provision in respect of the last two bullet points above will be subject to review (probably in 2017).
 - A trustee corporation will be appointed as a trustee of the Personal Accounts scheme as soon as it comes into force. (The members’ panel could be allowed to propose people for appointment as members of the trustee corporation. This would be in the spirit of the provisions for member nominated trustees and directors in the Pensions Act 2004).
- 7.3 To assist and advise the Secretary of State in connection with establishment and operation of the Personal Accounts scheme, a new non-departmental public body – the Personal Accounts Delivery Authority (PADA) – has been created. PADA may also give assistance and advice to the trustees of the scheme and, in connection with the employer duties, to The Pensions Regulator.
- 7.4 PADA, however, is a transitory body and will cease to be operational once the Personal Accounts scheme is up and running. Provisions for its constitution were set out in the Pensions Act 2007, as amended by the 2008 Act.
- 7.5 PADA has said that the introduction of the Personal Accounts scheme will be phased in over at least two years. In addition, the scheme is likely to undergo a soft launch because of the size of the task. The first employers will be enrolled in 2011, on a volunteer basis, in order to test the system. After that, it is expected that all employers will be included by 2014.

8 Personal Accounts – retirement options

- 8.1 PADA issued a consultation on 2 December 2008 which sets out its initial thinking on retirement options from the Personal Accounts scheme. The consultation covers issues such as the financial choices available to members, as well as how the scheme will help members to access retirement products. Details are available from www.padeliveryauthority.org.uk/securing-income.asp

9 Personal Accounts – scheme administration

- 9.1 On 15 January 2009, PADA announced the launch of its procurement process for the Personal Account Scheme Administration services.
- 9.2 As a public body, PADA is procuring services for the Personal Accounts scheme through the public sector procurement process. This means services are bought through fair and open competition in accordance with European Union procurement directives. PADA expects to make an announcement on the award in the summer of 2010.
- 9.3 The scope of services being procured through Scheme Administration is:
- Employer Participation – provision of scheme information; receipt of employer data; agreement of payment schedules.
 - Enrolment – automatic enrolment; opt-in; enrolment of the self-employed.

- Collection and Reconciliation – contributions from employers and members; contributions limit; handling late payments.
- Cash Management – refunds; aggregating contributions; updating unit prices to member records.
- Accessing Pension Savings – retirement options; purchasing annuity; trivial commutation.
- Administration of Account – updating member and employer records; complaint handling; divorce and dissolution of civil partnership.

9.4 Full details are available at www.padeliveryauthority.org.uk

10 Personal Accounts – investment

10.1 PADA hosted a one-day seminar on the important issues of Responsible Investment and Socially Responsible Investment (RI and SRI) on Tuesday 27 January 2009. The seminar marked the beginning of PADA's investment consultation process. The purpose was to engage stakeholders with the question of what is the appropriate approach the Personal Accounts scheme should take to RI and SRI.

10.2 The feedback from the day will be fed into an investment discussion paper that PADA are currently writing and there will be a chapter on RI. The discussion paper will be published in the Spring and will discuss the investment functions of the Personal Accounts scheme, covering such issues as the design of the default fund, lifecycle asset allocation, governance, and wider investment choices, including SRI.

10.3 Further details are available at www.padeliveryauthority.org.uk/investment.asp

11 Personal Accounts – charging structure

11.1 Charging (the annual costs of running the scheme) will be decided by the proposed trustee board. 30 basis points continues to be controversial. Financing is not decided either, though there is a commitment that set-up and operational costs should not be subsidised by the taxpayer.

11.2 The choice of charging structure is a key decision in the design of the Personal Accounts scheme. It will affect participation, members' pension pots and, ultimately, sustainability of the scheme itself. PADA has been seeking views on the most suitable charging structure for the scheme.

11.3 A consultation from PADA in 2008, "Building personal accounts, choosing a charging structure" explored the options, and invited feedback from interested individuals and groups.

11.4 Further details are available at www.padeliveryauthority.org.uk/charging-structure.asp

12 Means-testing

12.1 In February 2009, the Government published its research into the effect of means-testing on auto-enrolled pensions savings. The research concluded that 95% of people will be better off saving – and 70% can expect to get back twice what they put in – when Personal Accounts and auto-enrolment are introduced.

12.2 The research report – "Saving for Retirement" – indicated that there was no "readily identifiable group in the working-age population" who would not, on average, get back more than they put into a pension.

12.3 The Pension Policy Institute (PPI) has acknowledged that the findings from the Government's paper were broadly consistent with the PPI's own research and that the interaction with means-tested benefits should not be a barrier to saving. However, the PPI noted that a minority of people will not get back the value of their own contributions after taking account of inflation due to the interaction of their saving with means-tested benefits.

12.4 The full report from the Department of Work and Pensions is available at www.dwp.gov.uk/asd/asd5/reports2009-2010/rrep558.pdf

13 The Pensions Trust's view

13.1 The Pensions Trust has some concerns about Personal Accounts. They are intended to “complement, and not replace” existing pension schemes. However, the criteria for exemption from the requirement to offer Personal Accounts include auto-enrolment. Employers who offer a good scheme but after a waiting period of more than three months will either have to reduce the waiting period or auto-enrol new employees into a Personal Account after three months – so Personal Accounts may well compete with existing schemes.

13.2 Most importantly, The Pensions Trust shares the pensions industry's concerns that Personal Accounts could lead to “levelling down” – employers presently providing good quality pensions may well decide that they need only pay the Personal Accounts minimum contribution of 3% of band earnings.

Further updates about Personal Accounts will be included in future issues of the Pensions Bulletin and also via supplementary, more detailed, fact sheets.

While every effort has been made to ensure the accuracy of the information contained in this fact sheet, it should not be treated or relied upon as a statement of law. Readers should contact their regular Account Manager at The Pensions Trust in relation to their own circumstances and / or refer to the original source material as appropriate.

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