

Workplace Pension Reform (WPR)



ifs Financial Management

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The purpose of this article is to explain to employers what changes the Government is introducing with regard to the compulsory provision of pensions in the workplace.

The information is based on draft legislation and may be subject to change.

What is WPR?

The Government is concerned that as average life expectancy increases, many people are not saving enough to adequately provide an income in their old age.

Consequently, beginning in 2012, workplace pensions reforms (WPR) will be introduced which will impose new duties on employers to make mandatory pension provision for their employees.

Employers will have to automatically include certain employees in a pension scheme within a strict timescale. This process will be referred to as 'auto-enrolment'.

The pension scheme chosen by the employer must pass a quality test in that there must be a minimum level of contributions to be classed a qualifying scheme.

When will WPR happen?

It would not be practical for all employers to implement the new rules on the same day so the new employer duties will apply to largest employers first with effect from 1 October 2012. The gradual phasing in of WPR is known as staging.

Each employer's staging date will be based on PAYE records and the smallest employers (businesses employing fewer than 50 people) will be gradually phased in between March 2014 and February 2016. The actual date depends on the employer's PAYE reference.



What is a 'Qualifying Pension Scheme'?

A UK pension scheme is a qualifying scheme if it is registered and meets certain requirements and quality standards allowing it to be used for auto-enrolment (see below)

If a qualifying scheme is to be used for auto-enrolment then it must:

- Be able to accept members by auto-enrolment
- Have a default contribution basis
- Have a default investment option

Some pension schemes which are already in force will meet the qualification criteria and others will have to be amended to comply.

How much will employers have to pay?

When the new legislation is fully implemented, the minimum amount an employer must contribute will be 3% of qualifying earnings. However, the minimum contributions will be gradually stepped up from 1% in September 2016 to 3% in October 2017.

How much will employees have to pay?

When the scheme is fully implemented the minimum level of employee contribution will be 5% of earnings. Employee contributions will qualify for basic rate income tax relief at source so the figure of 5% will effectively reduce to 4%.



What are qualifying earnings?

Contributions will be made on a band of earnings, called the “Personal Accounts Earnings Band”. This was aligned with the Primary Threshold and Upper Earnings Limit for National Insurance contributions when it was launched, when the amounts were £ 5,035 and £ 33,540 respectively. These amounts will be increased each year in line with earnings.

Earnings from employment will include:

- Salary or wages
- Overtime payments
- Bonuses
- Commission
- Statutory sick pay, statutory maternity and paternity pay

What is automatic enrolment?

At the core of WPR is a requirement for employers to automatically enrol certain employees within a strict timescale without the employee having to:

- Apply to join the scheme
- Provide any information
- Make any choices with regard to the level of their contribution or how their contribution will be invested

Employees may opt out of the scheme after having been auto-enrolled but if they do they will have to go through an automatic re-enrolment process every three years.

Pension legislation is rarely straightforward so to complicate matters, an employer’s pension obligations will be different depending on which of two categories an employee falls into i.e.

Eligible jobholders must be auto-enrolled into a qualifying pension scheme unless they are already a member of one. An eligible jobholder is someone who:

- Is aged between 22 and State pension age
- Works in the UK
- Has earnings in excess of £7,475 per annum

Non-eligible jobholders do not have to be auto-enrolled unless they voluntarily opt in. A non-eligible jobholder is someone who:

- s aged between 16 and 21 or between State pension age and 74
- Works in the UK
- Has qualifying earnings

There are other classes of employee but the vast majority of UK employees will be classed as either eligible or non-eligible jobholders.

It is important to note that employers will be able to deduct contributions due from an eligible jobholder as a result of their membership of the pension scheme without the need to obtain their explicit consent



NEST

Under the WPR reforms, employers must auto-enrol certain employees into a qualifying pension scheme within a strict timescale.

If an employer does not have a pension scheme or the scheme they have is unsuitable they can elect to use the National Employment Savings Trust (NEST).

NEST is a centralised registered occupational pension and is open to any employer. It is a simple low cost scheme aimed at earners with low to moderate incomes.

NEST is an alternative to the employers own scheme. It is subject to certain rules and restrictions which make it less flexible than most other pension schemes:

- There is a cap on the level of contributions which can be made for or by any employee in any tax year. This is expected to be £3,600 (in 2005 terms, increased by the change in average earnings).

- The choice of investment funds will be limited.
- At retirement, the only way in which the pension fund can be used to provide a lifetime income will be to purchase an annuity.
- The charges will be capped. It is likely that there will be a 1.8% initial charge taken from each contribution and that the annual management charge will be limited to 0.3% of the fund value.
- Members of NEST will not be able to transfer their benefits out of NEST unless they have reached the normal minimum pension age of 55 or they are ill.

With the exception of pension sharing benefits from a divorce settlement, members of NEST will not be able to transfer funds into the scheme.



Who will check that employers are meeting their obligations under the new regime?

The Pensions Regulator is responsible for regulating WPR compliance and penalties will be imposed on employers who do not comply with the rules.

- Employers must prepare in advance of the new legislation by:
- Ensuring that if they have an existing pension scheme it will qualify
- Choosing between a new pension scheme and NEST if they do not already have a qualifying scheme
- Identifying which job category their employees fall into

- Once the WPR rules have been implemented, the employer must:
- Have a record keeping system which must be retained for six years
- Periodically register information about the company, the employees and the pension scheme
- Ensure that payroll systems can make the necessary salary deductions at the correct level

WPR will impose quite onerous responsibilities on the small employer who does not have the time or the relevant expertise. It is expected that in many cases, small employers will employ the services of a professional payroll adviser (often their accountant) who will be able to ensure that all the relevant systems are in place.

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