EXPLANATORY MEMORANDUM TO

THE AUTOMATIC ENROLMENT (EARNINGS TRIGGER AND QUALIFYING EARNINGS BAND) ORDER 2012

2012 No. 1506

1. This Explanatory Memorandum has been prepared by the Department for Work and Pensions and is laid before Parliament by Command of Her Majesty.

2. Purpose of the instrument

This instrument sets out revised rates for the 2012/13 tax year for the automatic enrolment and re-enrolment earnings trigger and the qualifying earnings band.

3. Matters of special interest to the Joint Committee on Statutory Instruments

These rates were set initially in the Pensions Act 2008 with a requirement to review them every tax year. Automatic enrolment begins this year and so the Secretary of State is now setting the rates for tax year 2012/13.

4. Legislative Context

4.1 The amounts of the automatic enrolment and re-enrolment earnings trigger and the qualifying earnings band are set out in the Pensions Act 2008.

4.2 The Secretary of State is required to review these amounts each tax year and revise, by Order, if he considers that any of the amounts should be increased or decreased.

4.3 The Secretary of State has discretion to increase or decrease the amounts and may take into account the prevailing personal tax threshold; Class 1 National Insurance contributions limits and thresholds; the rate of basic state pension and the general level of prices and earnings, or any other factors he considers are relevant. He has the power to prescribe annual rates and proportionate amounts to match pay periods. He also has the power, in respect of the rounded figures, to specify the amount as a figure of whole pounds, a figure that is divisible by 10 pence or a figure that includes a whole number of pennies. It is for the Secretary of State to decide whether to round any particular amount up or down.

4.4 Automatic enrolment starts to go live from October 2012 with the largest employers able to bring automatic enrolment forward to July 2012. The Order substitutes the amounts of the automatic enrolment and re-enrolment earnings trigger and the qualifying earnings band in the Pensions Act 2008 with revised rates for 2012/13.

4.5 The Secretary of State has concluded that the prescribed amounts for the automatic enrolment and re-enrolment earnings trigger and the qualifying earnings band should be increased for the tax year 2012/13.

5. Territorial Extent and Application

The Order applies to Great Britain. Separate but corresponding provision will be made for Northern Ireland.

6. European Convention on Human Rights

Steve Webb MP, Minister for Pensions, has made the following statement regarding human rights:

"In my view the provisions of The Automatic Enrolment (Earnings Trigger and Qualifying Earnings Band) Order 2012 are compatible with the Convention Rights".

7. Policy Background

What is being done and why

7.1 The automatic enrolment and re-enrolment earnings trigger is the level of earnings at which employers are obliged to automatically enrol (and re-enrol) eligible jobholders into a qualifying workplace pension scheme. Employers are then obliged to pay contributions at least equal to 8 per cent of a band of qualifying earnings made up of salary, wages, commission, bonuses, overtime and statutory sickness, maternity, paternity and adoption pay.

7.2 The Secretary of State believes that automatic enrolment should be as straightforward as possible for people to understand and employers to administer. He believes that automatic enrolment thresholds should, wherever possible, be aligned with existing payroll thresholds that employers are familiar with.

7.3 The Secretary of State has concluded that it is appropriate to enrol people automatically into workplace pension saving once they earn enough to pay income tax at the prevailing rates for the year 2012/13. The Order provides for the automatic enrolment earnings trigger to be revised to align with the PAYE income tax personal allowance for the tax year 2012/13.

7.4 He has also concluded that private pension saving should build on the foundation of state pension entitlement and that the qualifying earnings band should be as wide as possible to maximise pension saving. Under current rules state pension entitlement accrues from earnings at the National Insurance contributions lower earnings limit. The Secretary of State has, therefore, decided to use the National Insurance contributions lower earnings limit as the most relevant point to begin private savings for retirement. So the Order provides for the lower limit of the qualifying earnings band to be aligned with the lower earnings limit for 2012/13.

7.5 The Secretary of State has also concluded, taking into account the responses to the public consultation on the thresholds for 2012/13 which placed a high priority on alignment with existing thresholds, that the upper limit of the qualifying earnings band should also be aligned with the National Insurance contributions band. The Order therefore provides for the upper limit of the qualifying earnings band to be aligned with the National Insurance contributions upper earnings limit.

7.6 Employers will apply the proportionate amount of the annual figure to determine if a worker has jobholder status, and hence whether they should be enrolled automatically, in line with their usual pay period.

Consolidation

‘Informal consolidation of the instrument will be addressed by up-dating the relevant values in the appropriate statutory instruments in due course in the Department’s “the law relating to Social Security” (the Blue Volumes). This publication is available at no cost to the public on the internet at:
http://www.dwp.gov.uk/publications/specialist-guides/law-volumes/the-law-relating-to-social-security/.’

8. Consultation outcome

8.1 The duty to review the automatic enrolment and re-enrolment trigger and the qualifying earnings band must be discharged in relation to each tax year. The power to substitute new amounts is a flexible power that allows the Secretary of State discretion to set the automatic enrolment thresholds every year.

8.2 To assist the Secretary of State in setting the amounts for the first year of live running, he consulted on the proposed values for 2012/2013 and sought views on the relevancy of each of the revision factors. In arriving at his decision, he has taken the results of the consultation into consideration.

8.3 The consultation ran for 6 weeks from 5 December 2011 to 26 January 2012. The Department received 32 formal written responses from employer organisations, pension providers, accountants, lawyers, trades unions and consumer organisations.

8.4 The majority of the responses favoured alignment with the PAYE threshold for the automatic enrolment trigger and alignment with the National Insurance contributions lower and upper limits for the qualifying earnings band.

8.5 A key message to emerge from the consultation is that simplicity is critical to the success of automatic enrolment and that simplicity is best supported by aligning automatic enrolment triggers and thresholds with existing payroll thresholds.
The challenges of business planning and the need for certainty about the thresholds in advance was a significant theme in the responses. The Government recognised the importance of longer term financial planning in helping employers prepare for automatic enrolment.

8.6 The Government also recognise the advantages of alignment with the tax and National Insurance contributions thresholds. However, a lock-in to any particular approach may not be suitable or sustainable in the event of any future developments in the structure of tax and National Insurance, changes in expected savings patterns or in economic circumstances, so it is important that flexibility to review the thresholds and triggers for future years is retained.

8.7 Some respondents addressed low pay and equality issues and argued in favour of a lower entry point to automatic enrolment. That evidence was reviewed carefully. The group excluded from automatic enrolment by a higher trigger comprises more women than men. However, those with lower earnings are less likely to benefit from pension saving than other groups. In determining the appropriate level for the automatic enrolment trigger, the Government weighed the possible adverse impact on women of a higher trigger, which may exclude lower earners from pension saving, against the risk that a lower trigger may also adversely impact women by bringing lower earners into pension saving inappropriately.

8.8 The Secretary of State has placed a copy of the Government's response to the public consultation *Automatic enrolment earnings thresholds review and revision 2012 / 2013* in the library of both Houses of Parliament.

9. Guidance

The Pensions Regulator will update its on-line guidance for employers and payroll providers with the new rates following the publication of the Order. The new rates will also be published on the DWP website following the publication of the Order.

10. Impact

10.1 The impact of this order on business and civil society organisations is low.

10.2 The impact of this Order on the public sector is low.

10.3 A full impact assessment has not been published for this instrument because it amends an existing regulatory regime and the associated administrative costs are low. Publication of a full impact assessment is not necessary for such legislation. Nevertheless, the Secretary of State has considered the impact of the various options for each of the thresholds and an analysis of volumes and costs was published as part of the formal consultation. The analysis has been updated and is published with the Government's response to the consultation. That updated analysis is attached to this memorandum (Annex A and Annex B) and will be published alongside it on www.legislation.gov.uk.

11. Regulating small business

This Order does not apply to small business. The automatic enrolment legislation places a duty on all employers, whatever their size, to enrol automatically eligible workers into a workplace pension arrangement. However, automatic enrolment during the first year of implementation (2012/2013 tax year) applies only to employers with 10,000 workers or more. Smaller employers do not become subject to the automatic enrolment duty until the 2015/2016 tax year.

12. Monitoring & review
The automatic enrolment rates are subject to review each tax year.

13. Contact
For any queries regarding this instrument, please contact Jane Stewart
Telephone number: 020 7449 7230 or e-mail: jane.stewart4@dwp.gsi.gov.uk

Annex A: Costs and benefits of final proposals

Estimates of the impact of changing the earnings trigger and upper and lower limits of the qualifying earnings band on employers, individuals and government (£ million, in 2012/2013)

	Earnings Trigger	Qualifying Earnings Band – Lower Limit	Qualifying Earnings Band – Upper Limit	Employer Contributions	Individual Contributions	Individual Tax Relief	Level of Pension Saving	Employer Tax Relief
Baseline	£7,692 terms (baseline of PAYE threshold of £7,475 in 2011/12 revalued by average earnings)	£5,983	£39,853	£23m	£18m	£5m	£46m	£6m
Proposal	£8,105 (2012/13 PAYE Personal Tax threshold)	£5,564 (2012/13 Lower Earnings Limit)	£42,475 (2012/13 Upper Earnings Limit)	£24m	£19m	£5m	£48m	£6m
Difference	-	-	-	+£0.9m	+£0.7m	+£0.2m	+£1.9m	+£0.2m

Notes:
Source: DWP modelling.
Figures are expressed in 2012/13 earnings terms.
Figures are rounded to the nearest £10 million and 100,000 as appropriate.
Pension saving is the sum of tax relief, employer contribution and individual contribution costs

Annex B Equality implications of changes to the earnings trigger

It is estimated that there are 9 to 10 million workers eligible for automatic enrolment, of whom just under two in five (39 per cent) are women.

Raising the 2011/12 value of the automatic enrolment trigger from £5,035 (in 2006/07 terms) to £7,475 excluded 600,000 individuals (78 per cent of whom are women). As women are more likely to work part-time, or earn less than men, they will be disproportionately represented in the group excluded from automatic enrolment by an upward revision of the trigger and conversely in any group brought into pension saving by a decrease in the trigger. For example:

- of the 20,000 individuals brought into pension saving on a trigger of £7,605, around 17,000 are women;

- of the 40,000 individuals who would not be eligible for automatic enrolment if the earnings trigger was revised to £7,864 from £7,692 (in 2012/13 terms), around 34,000 are women;

- if the earnings trigger was revised to £8,105, the equivalent figures are around 75,000 women excluded from a total of around 90,000.

Persistent low earners tend to find that the State, through pensions and benefits, provides them with an income in retirement similar to that in working life without the need for additional saving. For these individuals, it may not be beneficial to direct income from working life into pension saving. Furthermore, anyone who is not enrolled automatically because of an increase in the earnings trigger will retain the right to opt in with an employer contribution. Employers will be required to provide information about this.

Revising the current earnings trigger to the PAYE threshold (£8,105 in 2012/13 terms) does not affect the proportion of minority ethnic groups in the total number of persons to be enrolled automatically. The composition of the revised eligible group remains the same at 12 per cent black and minority ethnic groups (BME).

The evidence also suggests that revising the earnings trigger would not particularly affect people with a disability. It is estimated that 17 per cent of the revised eligible group will comprise workers with a disability if the earnings trigger is revised to £7,864 or £8,105 (in 2012/13 terms). This is the same proportion as is included in the current eligible group (£7,684 in 2012/13.)

The median age of those eligible for automatic enrolment on the current earnings trigger is 40 years which indicates that there is a slightly higher proportion of younger workers in the eligible group. However specific age groups are not particularly affected by changing the value of the earnings trigger.

The changes under consideration are not expected to particularly affect individuals according to their sexual orientation, religion or belief.