EXPLANATORY MEMORANDUM TO

THE AUTOMATIC ENROLMENT
(EARNINGS TRIGGER AND QUALIFYING EARNINGS BAND)
ORDER (NORTHERN IRELAND) 2017

S.R. 2017 No. 54

1. Introduction

1.1 This Explanatory Memorandum has been prepared by the Department for Communities to accompany the Statutory Rule (details above) which is laid before the Northern Ireland Assembly.

1.2 The Statutory Rule is made under sections 14 and 15A(1) of the Pensions (No. 2) Act (Northern Ireland) 2008 and is subject to the negative resolution procedure.

2. Purpose

2.1 This Order sets the amounts of the automatic enrolment qualifying earnings band for the 2017/18 year in line with the lower and upper National Insurance contributions earnings limits for that year. It also specifies rounded figures for the earnings trigger and qualifying earnings band for that year.

3. Background

3.1 The amounts of the automatic enrolment and re-enrolment earnings trigger (the earnings level at which an employee must be automatically enrolled) and the qualifying earnings band (the earnings on which contributions must be paid) are set out in the Pensions (No. 2) Act (Northern Ireland) 2008 and the Pensions Act 2008.

3.2 Whenever the Secretary of State for Work and Pensions makes an order to substitute amounts and specify rounded figures for the earnings trigger and qualifying earnings band, the Department may make a corresponding order. The Department has no power to specify different amounts for Northern Ireland.

3.3 This year's order provides for the amounts of the lower and upper limits of the qualifying earnings band to be aligned with the lower (£5,876) and upper (£45,000) National Insurance contributions earnings limits for the 2017/18 tax year. It also specifies rounded figures for the earnings trigger and qualifying earnings band (where the pay reference period is not more than 12 months) so that 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.

4. Consultation

4.1 There is no requirement to consult on this Order.

5. Equality Impact

5.1 In accordance with its duty under section 75 of the Northern Ireland Act 1998, the Department has conducted a screening exercise on the legislative proposals and as they merely discharge the Department’s statutory duty to substitute the amounts of the lower and upper limits of the automatic enrolment qualifying earnings band and do not alter policy, has concluded that they do not have significant implications for equality of opportunity. In light of this, the Department considers that an Equality Impact Assessment is not necessary.

6. Regulatory Impact

6.1 A Regulatory Impact Assessment is attached as an Annex to this Explanatory Memorandum.

7. Financial Implications

7.1 None for the Department.

8. Section 24 of the Northern Ireland Act 1998

8.1 The Department has considered section 24 of the Northern Ireland Act 1998 and is satisfied that this Order –

(a) is not incompatible with any of the Convention rights,

(b) is not incompatible with Community law,

(c) does not discriminate against a person or class of person on the ground of religious belief or political opinion, and

(d) does not modify an enactment in breach of section 7 of the Northern Ireland Act 1998.

9. EU Implications

9.1 Not applicable.

10. Parity or Replicatory Measure

10.1 The corresponding Great Britain Order is the Automatic Enrolment (Earnings Trigger and Qualifying Earnings Band) Order 2017 (S.I. 2017/394) which was made on 14th March 2017 and comes into force on 6th April 2017. Parity of timing and substance is an integral part of the maintenance of single systems of social security, child support and pensions in line with section 87 of the Northern Ireland Act 1998. It was, therefore necessary to make the Order during the period of interregnum.

ANNEX

REGULATORY IMPACT ASSESSMENT

THE AUTOMATIC ENROLMENT (EARNINGS TRIGGER AND QUALIFYING EARNINGS BAND) ORDER (NORTHERN IRELAND) 2017

AUTOMATIC ENROLMENT: REVIEW OF THE EARNINGS TRIGGER AND QUALIFYING EARNINGS BAND FOR 2017/18

The costs and savings outlined in this Regulatory Impact Assessment are calculated on a United Kingdom-wide basis.

Introduction

1. This Regulatory Impact Assessment sets out the policy objectives of the review of the automatic enrolment earnings trigger and qualifying earnings band for the 2017/18 year and the impact on, for example, individuals, employers and the pensions industry.

Background

2. The Pensions (No. 2) Act (Northern Ireland) 2008 and corresponding provision in the Westminster Pensions Act 2008 introduced a duty on employers to enrol eligible jobholders into a qualifying workplace pension and to make minimum contributions into it. Under the legislation, employers are able to choose the qualifying workplace pension scheme they adopt to discharge this duty. A qualifying scheme is a scheme which meets specific criteria, for example, an occupational pension scheme (including the National Employment Savings Trust (NEST) established on a UK-wide basis under the Pensions Act 2008) or a workplace personal pension scheme.

3. Automatic enrolment mandates employers to enrol all eligible workers into a qualifying workplace pension. Roll out began in July 2012 with largest employers and automatic enrolment has now been successfully extended to medium sized employers. Small and micro employers started to stage[1] from June 2015. It is estimated that around 11 million people are in the eligible target group[2] for automatic enrolment and 10 million people will be newly saving or saving more into a workplace pension by 2018.[3]

4. The legislation also mandates employers to pay a minimum contribution for eligible workers who remain automatically enrolled. To help reduce burdens on employers, the implementation timetable gradually phases in rises in minimum contribution rates to a defined contribution workplace pension.[4] The minimum contribution rate is currently at or

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[1] An employer has to meet its automatic enrolment duties (or stage) and begin enrolling its eligible workers into a workplace pension at a pre-defined (by its PAYE records at 1st April 2012) staging dates.

[2] The eligible target group is defined as workers who are aged between 22 and State Pension age, earning over £10,000 in 2016/17 and either (i) not currently saving in a pension scheme; or (ii) saving in a pension scheme where the employer contributions are less than 3% of the worker's salary, and is not a defined benefit scheme.

[3] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/560356/workplace-pensions-update-analysis-auto-enrolment-2016.pdf

[4] Under automatic enrolment legislation contributions are made into a workplace pension by individuals, their employers and the Exchequer via tax relief applied to individual cash contributions.

equivalent to 2 per cent. of a band of qualifying earnings[5] (of which at least 1 per cent. must be paid by the employer). This is due to rise to 5 per cent. in April 2018 (with a minimum employer contribution of 2 per cent.) and by April 2019 it will rise to 8 per cent. (with a minimum employer contribution of 3 per cent.).

5. The automatic enrolment and re-enrolment earnings trigger determines who is eligible to be automatically enrolled by their employer into a workplace pension. The intent behind the earnings trigger is that it should be set at a level that ensures as many people as possible are eligible for automatic enrolment without disproportionately capturing those lowest earners for whom it makes little sense to save for retirement and who are likely to opt-out. This is currently set at £10,000 of gross annual earnings for 2016/17.

6. The qualifying earnings band sets minimum contribution levels for money purchase schemes. The minimum of the band is intended to ensure that those who are automatically enrolled pay contributions on a meaningful level of their earnings. The lower limit is also relevant to defining who can opt-in to a workplace pension if their take-home pay is under the earnings trigger and still be eligible for employer contributions. Having an upper limit helps manage burdens on employers by capping the amount of contributions they are legally required to pay. The qualifying earnings band is currently aligned with the Upper and Lower Earnings Limits for National Insurance contributions at £5,824 - £43,000 for 2016/17.

7. The Pensions Act 2011 initially aligned the earnings trigger with the Personal Income Tax Threshold. The Government consulted on the thresholds for the first two years (2012/13 and 2013/14) of automatic enrolment to test the approach to the annual review, the relevant revision factors for each threshold and the balance between targeting, administrative simplicity and employer costs.

8. After considering all the relevant factors, it was decided in the third year (2014/15) of automatic enrolment that it was right to continue to align with the personal tax allowance of £10,000 and so a consultation was considered unnecessary.

9. However, after four years of automatic enrolment (2015/16), given the number of employers who had gone through the staging process, a further consultation was conducted to gain valuable insight on the experiences of live running and to test whether maintaining the alignment between the earnings trigger and the personal tax allowance remained right, in light of proposed increases to the personal tax allowance and suppressed earnings growth. Following the consultation, it was decided to again freeze the earnings trigger at £10,000 in 2015/16 and to retain the link with National Insurance for the upper and lower limits for qualifying band earnings. This position was maintained in 2016/17.

Problem under consideration

10. It is a statutory requirement that the automatic enrolment earnings thresholds must be reviewed each year. This allows the automatic enrolment thresholds to be kept up to date and relevant in light of changing economic and fiscal circumstances.

[5] The qualifying earnings band is defined as the upper earnings limit (£43,000 in 2016/17) minus the lower earnings limit (£5,824 in 2016/17) for individuals with gross annual earnings at or above the upper earnings limit; and an individual's gross annual earnings minus the lower earnings limit for individuals earning below the upper earnings limit.

11. Section 14 of the Pensions Act 2008 specifies a number of factors which may be taken into account, but also allows any other relevant factors to be considered. The specified factors are: price and earnings inflation; tax and National Insurance thresholds; and the prevailing rate of the basic state pension. Amendments to legislation, proposed as a result of the introduction of the new State Pension, mean its prevailing rate would also be included in the list.

12. As well as considering these types of factors, the first four reviews have been underpinned by a set of key policy considerations:
    - Will the right people be brought in to pension saving?
    - What is the appropriate minimum level of saving for people who are automatically enrolled?
    - Are the costs and benefits to individuals and employers appropriately balanced?

13. The pension's landscape has changed considerably over the past few years and automatic enrolment has been a step-change for individuals, employers and the industry alike. The programme is now in its most challenging phase with roll-out to small and micro employers well underway. This year's annual review of the automatic enrolment thresholds has therefore recognised the importance of stability against a backdrop of substantial change.

14. A commitment was made to review the scope and operation of automatic enrolment in 2017, mindful of the changes in the labour market and economic landscape. This will take stock of where things are now, what has been achieved over the past four years and ensure it continues to work for individuals and employers alike into the future.

15. The wider review will look at the existing coverage of the policy and consider the needs of those groups currently under-represented in pension saving, for example employees with multiple jobs who do not meet the criteria for automatic enrolment in any individual job. For the 2017/18 tax year it is considered important that the annual automatic enrolment thresholds review does not pre-empt the outcome of the wider review in 2017.

Rationale for intervention

16. It is a statutory requirement that the automatic enrolment earnings thresholds must be reviewed each year. This allows the Government to keep the automatic enrolment thresholds up to date and relevant in light of changing economic and fiscal circumstances. For this reason, the policy appraisal period in this impact assessment is only one year but it is important to recognise that saving into a workplace pension will have significant long term benefits in providing a welfare gain to society through people enjoying a more financially secure later life.

Policy objective

17. The policy objectives are to make automatic enrolment as simple and low cost as possible for employers, particularly small and micro employers. The Government aims to balance this consideration with maximising the opportunity and incentives for individuals, particularly low to moderate earners, to save and continue saving into a workplace pension.

Description of final proposal

<u>Freezing the earnings trigger at £10,000 and maintain the link between qualifying band earnings and the Upper and Lower Earnings Limits for National Insurance Contributions</u>

18. The Government remains sensitive to issues around the affordability of contributions for both individuals and employers. Indeed maintaining the affordability of automatic enrolment is a key function of the earnings trigger and earnings band. However, the considered view remains that the overriding factor should be ensuring that people have sufficient retirement income savings and while it is recognised that there are costs for employers, including one-off administrative costs, this also needs to be viewed against the long term benefits of the policy.

19. In light of the timing of this year's review preceding a broader review of automatic enrolment policy in 2017, the need for stability in this crucial stage of the programme's roll out, and the principle aim of affordability, the review factors have been re-considered against the latest analytical evidence and policy objectives and it has been decided that the current threshold of £10,000 remains the right level and therefore will not change for 2017/18. This strikes the right balance between administrative simplicity and consistency for the employers implementing automatic enrolment up to 2018. It also helps to ensure that the people brought into pensions saving are likely to benefit.

20. The current (2016/17) and proposed (2017/18) automatic enrolment thresholds are displayed in Table 1.

<u>Table 1 – Current and proposed automatic enrolment thresholds</u>

	Trigger	**Lower limit qualifying earnings band**	**Upper limit qualifying earnings band**
Current (2016/17 terms)	£10,000	£5,824	£43,000
Proposed (2017/18 terms)	£10,000	£5,876	£45,000

21. Although the absolute values of the Upper and Lower Earnings Limit have changed, they have remained aligned with the Upper and Lower Earnings Limit for National Insurance contributions for 2017/18. The changes are therefore automatic in nature as they simply reflect the uprating of the NIC figures. They do not therefore fall within the definition of 'amendment' for the purposes of the Business Impact Target and are not considered to be regulatory provisions.

22. However, the decision to retain the departure from Income Tax figures in the earnings trigger does not represent such an automatic decision and therefore represents a new regulatory provision. The earnings trigger has been fixed at £10,000 for 3 consecutive years in order to maintain administrative simplicity and to increase the number of people automatically enrolled.

23. To estimate the impact associated only with changing the earnings trigger for 2017/18, it is assumed that under both scenarios, retaining the 2016/17 automatic enrolment earnings trigger in 2017/18 taking into account earnings growth (the baseline) and freezing the earnings trigger at £10,000 (final proposal), the qualifying earnings band is

set at £5,876 - £45,000 for 2017/18. Table 2 shows the level of the earnings trigger, under both scenarios, used to estimate the costs and benefits of the proposed change.

Table 2 – Current and proposed automatic enrolment thresholds used to estimate the costs and benefits of the proposed change to the earnings trigger in 2017/18

	Trigger	Lower limit qualifying earnings band	Upper limit qualifying earnings band
Baseline	£10,255 (2016/17 trigger in 2017/18 terms)	£5,876	£45,000
Proposed	£10,000	£5,876	£45,000

Note: The OBR's Autumn Statement 2016 forecast for private sector earnings growth was used to uprate the baseline trigger to 2017/18 terms.

24. This approach means the estimated impacts from the proposed policy change will differ to the recently published supporting analysis for the 2017/18 review of the Automatic Enrolment earnings trigger and qualifying earnings band[6]. Additionally, since this publication the estimates of the impact on total pension savings of the proposed change have improved. More details on the methodology can be found in Annex A.

Monetised and non-monetised costs and benefits of each option (including administrative burden)

25. This section covers the changes in the estimated costs and benefits to individuals, employers, the Exchequer, pension providers and social welfare from the proposed policy change in 2017/18.

Impact on individuals

Increase in total savings into pensions

26. Freezing the value of the automatic enrolment trigger at £10,000 in 2017/18 results in a real terms decrease in the trigger, which brings an additional 70,000 individuals into the target population[7] (of whom around 50,000 (75 per cent.) are women) in 2017/18 compared to the 2016/17 earnings trigger (baseline). This will result in an associated **increase in total pension saving of £4.3 million in 2017/18 (2017/18 price terms)** (composed of individual contributions, employer contributions and tax relief from the Exchequer on individual contributions), as displayed in Table 3.

[6] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/576423/review-of-ae-earnings-trigger-2017-2018.pdf

[7] The 'target population' covers eligible individuals who are either (i) not saving in a pension scheme; or (ii) saving in a pension scheme where the employer contributes less than 3 per cent of the individual's salary, and is not a defined benefit scheme . More details in Annex A.

Table 3: Estimated increase in total pension saving in 2017/18 under the proposed earnings trigger when compared to the current earnings trigger (baseline) and resulting demographic effects

	Earnings Trigger	**Total pension saving (£million, 2017/18)**	**Demographic Effects**
Baseline	£10,255 (2016/17 trigger in 2017/18 terms)	6,476.5	Target Population: 11m Of which Women: 37% BME: 9% Disabled:10%
Increase with proposed earnings trigger	£10,000	+4.3	Included Group: +0.07m Of which women: 75%

Source: DWP modelling.
The OBR's Autumn Statement 2016 forecast for private sector earnings growth was used to uprate the baseline trigger to 2017/18 terms.
Pension saving is the sum of individual tax relief, employer contribution and individual contribution costs.
Scenarios after the baseline present the additional impact when compared to the baseline
Costs are presented as negative numbers, benefits as positive numbers.
Demographic effects are rounded to the nearest 0.01m and 1 per cent, as appropriate.
Demographic effects for women are estimated from the latest Annual Survey of Hours and Earnings for the year 2012/13 and from the 2012/13 ONS Labour Force Survey for ethnicity and disability. More detail on in Annex A.

27. For individuals earning below the earnings trigger it may not be beneficial to direct their income from working life into workplace pension saving. Furthermore, anyone who is not automatically enrolled into a workplace pension because their earnings are below the trigger will retain the right to opt-in and will receive an employer contribution as long as they earn above the lower limit of the qualifying earnings band. Recent research published by the Institute for Fiscal Studies shows that automatic enrolment has increased workplace pension membership by 28 percentage points among those earning under £10,000 per year (compared to a baseline of 18 per cent. prior to the reform). This could be as a result of individuals opting-in or employers offering provision to these workers in addition to their eligible workforce.

28. An assessment of the equality implications of the proposed earnings trigger can be found in Annex B.

Impact on employers

Increase in employer contribution costs

29. Increasing the number of individuals automatically enrolled as a result of freezing the earnings threshold leads to additional contribution costs. Employers will make more contributions into workplace pensions between April 2017 and March 2018 than under the current policy. Table 4 shows that the proposed change when compared with the current approach will **cost employers an estimated additional £2.2 million in minimum total pension contributions above the baseline estimate in 2017/18** (in 2017/18 price terms).

Table 4: Estimated increase in contribution costs to employers in 2017/18 under the proposed earnings trigger when compared to the current earnings trigger (baseline)

	Earnings Trigger	Contribution costs (£ million, 2017/18)
Baseline	£10,255 (2016/17 trigger in 2017/18 terms)	-2,750.9
Increase with proposed earnings trigger	£10,000	-2.2

Source: DWP modelling.
The OBR's Autumn Statement 2016 forecast for private sector earnings growth was used to uprate the baseline trigger to 2017/18 terms.
Costs are presented as negative numbers, benefits as positive numbers.
Scenarios after the baseline present the additional impact when compared to the baseline

Increase in employer administrative costs

30. Increasing the number of individuals automatically enrolled as a result of freezing the earnings threshold will lead to administrative costs for those employers who now have additional eligible jobholders. These employers will have to:

- Enrol the additional eligible jobholders, providing them with the required information and providing their details to the pension scheme;
- Deal with opt-outs and refunding any contributions deducted by the employer before the opt out was received;
- Carry out collection and administration of contributions to the pension scheme and deal with queries relating to this process.

31. The model[8] used to estimate administration costs in the Workplace Pension Reform Regulations Impact Assessment (2010) disaggregates the costs of these processes[9]. The section relevant to our proposed changes can be seen in Table 5 below.

[8] An 'administrative cost model' initially developed in 2006 for the White 'Paper Personal accounts: a new way to save', thoroughly scrutinised by a cross government working group and included in subsequent Workplace Pension Reform Impact Assessments used a range of published data sources and specially commissioned research to estimate the administrative cost to employers of the processes required under the employer automatic enrolment duties by firm size. Due to the level of scrutiny during development and cross government agreement, DWP believe the model is still fit for purpose.

[9] http://webarchive.nationalarchives.gov.uk/20100304151554/http://dwp.gov.uk/docs/wpr-ia.pdf

Table 5: Breakdown of administration costs to employers in year 1 in (2009/10 price terms)

Year 1 Cost Breakdown by Firm size	Large (£millions)	Medium (£millions)	Small (£millions)	Micro (£millions)
1. Enrolling eligible jobholders, providing them with the required information and providing their details to the pension scheme	19.5	7.1	15.0	8.5
2. Dealing with opt-outs and refunding any contributions deducted by the employer before the opt out was received	4.6	1.8	3.6	4.1
3. The calculation and collection of contributions from employees pay	3.6	5.6	21.2	39.2
4. Payment of contributions to the pension scheme	0.3	0.9	10.2	12.9
5. Dealing with queries about deductions and processing requests to cease pension saving.	0.9	0.4	0.6	0.6

32. Dividing the numbers in Table 5 by the estimated populations of employers in the Workplace Pension Reform Regulations Impact Assessment (2010) gives the average employer costs in 2009/10 price terms. Using these disaggregated costs, the average 'per employee' cost by employer size band of this extra enrolment activity can be calculated. Across all employers this is on average £15. Converting these 'per employee' costs by employer size into 2017/18 prices, using the Office for Budget Responsibility (OBR)'s Autumn Statement 2016 GDP deflator forecasts, gives the average 'per employee' cost of each activity by employer size. This is around £16 across all employers.

33. It is estimated that an additional 70,000 individuals will be automatically enrolled into workplace pension saving as a result of freezing the earnings threshold (paragraph 26) with 62,000 remaining in after opt outs are accounted for (see Annex A for opt out assumption).

34. Multiplying the volumes automatically enrolled by the average 'per employee' cost by firm size for process 1; the volumes of opt outs by the average 'per employee' cost by firm size for process 2; and the volumes of individuals who remain in by the average 'per employee' cost by firm size for process 3-5, it is estimated that during 2017/18 there will be a **one-off administrative cost for employers with additional eligible jobholders worth £0.8 million** (in 2017/18 price terms).

35. Additionally there will be some employers who did not previously have any eligible jobholders and will have additional administrative costs associated with:

- Making an arrangement with a pension scheme;
- Adapting or purchasing in-house or internal payment systems; and
- Training staff to carry out the administrative processes.

36. From the 2010 "Workplace Pension Reform Regulations Impact Assessment" the estimated total cost of these processes is £148m. Dividing this by the estimated population of employers in the Workplace Pension Reform Regulations Impact Assessment (2010) gives the average employer cost of these processes of £136 in

2009/10 price terms. Uprating this estimate to 2017/18 prices using the Office for Budget Responsibility (OBR)'s Autumn Statement 2016 GDP deflator forecasts it is equal to £153.

37. The Pensions Regulator (TPR) estimates that by the end of 2018 between 1.32 and 1.46 million employers will have automatically enrolled their employees. TPR estimate that around 900,000 employers (63 per cent.) will have eligible jobholders to enrol under the current earnings trigger[10]. Using HMRC Pay-As-You-Earn (PAYE), it is estimated that an additional 10,000 employers (1 per cent.[11]) will have eligible jobholders under the proposed change.

38. Multiplying the average cost (paragraph 36) by these extra employer volumes, it is estimated that during 2017/18 there will be a **one-off administrative cost for employers who did not previously have any eligible jobholders of this proposed change worth £1.6 million** (in 2017/18 price terms).

39. There may also be some familiarisation costs imposed on employers who did not previously have any eligible jobholders, however these will be negligible because, all employers (whether they have eligible jobholders or not) would have to familiarise themselves with the relevant literature as they approach their staging date, in order to declare compliance with The Pensions Regulator.

Impact on the Exchequer

40. Freezing the earnings threshold in 2017/18 will have a minimal cost to the Exchequer as there are now slightly more individuals saving and so an associated increase in tax relief on pension contributions. That cost is estimated to be **£0.5 million in 2017/18** (2017/18 price terms).

Impact on pensions industry revenue

41. The pensions industry is estimated to have marginally higher revenues in 2017/18 as a result of freezing the earnings threshold. The increase in the number of savers in any given workplace pension scheme will increase the total volume saved in that scheme and subsequently the total revenues generated from fund charges.

42. Evidence from DWP's "Pension Charges Survey 2015: Charges in defined contribution pension schemes"[12] suggests that the average (member weighted) annual charge of automatic enrolment qualifying schemes is 0.49 per cent. The Pensions Charges survey fieldwork was carried out before the introduction of the Charge Cap so consequently these might be slight over-estimates. Multiplying this annual management charge by the estimated increase in total pension saving gives **a rise in pension industry revenue of around £0.02 million in 2017/18** (in 2017/18 price terms).

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[10] http://www.thepensionsregulator.gov.uk/docs/automatic-enrolment-commentary-analysis-2016.pdf

[11] Using HMRC PAYE data, the number of employers with employees earning between the proposed trigger and 2016/17 trigger only is divided by the total number of employers in that month to give this proportion. The months from June 2015 to April 2017 are used as a proxy for the whole period since staging began in October 2012. The data uses income information only up to 2015/16 and so may be an overestimate as earnings growth up to 2017/18 is not accounted for.

[12] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/483179/Pension_charges_survey_2015_charges_in_defined_contribution_pension_schemes.pdf

Summary of costs and benefits

43. A summary of the administration as well as transfer costs and benefits associated with the proposed policy change between April 2017 and March 2018 are presented in Table 6. The majority of costs and benefits are income transfers with gains to individuals and the pensions industry offset by losses for employers and the Exchequer. However, once all these income transfers are netted out, there is still a small administrative cost for employers affected by the proposed change.

Table 6: Summary of the administration and transfer costs and benefits for the proposed policy change in 2017/18 (£ million, 2017/18 terms)

	2017/18
Employers	
Increased contribution costs	-2.2
Additional administration costs	-2.3
Net benefits	-4.6
Pensions Industry	
Increased revenue	0.0
Net benefits	0.0
Individuals	
Increased contribution costs	-1.6
Increase in total contributions into pensions*	4.3
Net benefits	2.7
Exchequer	
Increased individual tax relief	-0.5
Net benefits	-0.5
Overall	-2.3

Source: DWP Modelling.
Costs are presented as negative numbers, benefits as positive numbers.
* The increase in total contributions is net of provider charges – so reflects the increase in pension industry revenue from the amount charged on higher total pension contributions.

Risks and assumptions

44. The present value calculation is most sensitive to the number of employers, eligible workers, opt-out rates, earnings of workers who remain automatically enrolled (for whom employers are required to make minimum pension contributions). The latest forecasts on the number of employers and eligible workers, and research evidence on opt-out rates were used. More details on the methodology can be found in Annex A.

Rationale and evidence that justify the level of analysis (proportionality approach)

45. This assessment has made use of available data – ONS Annual Survey of Hours and Earnings (ASHE) 2015 data, 2015 Employer Pension Provision (EPP) survey, 2015 Charges Survey and - alongside DWP's internal volumes modelling, The Pensions Regulator's 2016 revised employer staging profile and informal engagement with stakeholders to verify the assumptions.

Direct costs and benefits to Business

46. The proposal imposes a burden on businesses and is within the scope for the Business Impact Target (BIT). It is estimated that the increase in contributions and one-off administrative costs will cost employers an estimated £4.6 million in 2017/18 price terms. For the purposes of the BIT, net costs to business are to be presented in 2014 prices and discounted to 2015, in order for all policies to be compared using consistent pricing and discounting. Using a one year appraisal period from April 2017 and 3.5 per cent. discount rate in line with the Treasury's Green Book, it is estimated that as a result of the increase in these direct costs to employers there is **an Equivalent Annual Net Direct Cost to Business (EANDCB) worth £4.1 million** (2014/15 prices).

Wider impacts

47. Freezing the earnings threshold in 2017/18 will have a further minimal, indirect cost to the Exchequer of around £0.2 million (in 2017/18 price terms). This is from the tax no longer paid by those employers who respond to the additional pension contribution costs of the policy change by reducing profits or wages paid to their workers. This will result in a loss of tax revenue to the Exchequer. See Annex A for more detail on this methodology.

48. There may be some additional, albeit negligibly small and non-monetised impacts associated with this proposed policy change.

49. The proposed change will cause an additional 70,000 individuals to be eligible for automatic enrolment. By contributing to a pension, they will experience a small fall in net earnings from working. This may increase the level of in-work benefits they are entitled to, such as Universal Credit, Tax Credits and Housing Benefit. Conversely, the proposed change will cause an increase in their private pension saving, which may reduce the level of income related benefits received in retirement. However, these changes will only be marginal and represent a transfer between the Exchequer and individuals so have not been included in this impact assessment.

50. Additionally, saving in a workplace pension produces a welfare gain to society through people enjoying increased well-being over their lifetime as a result of transferring income from a period when their income is relatively high (when working) to a period in which their income would otherwise be lower (in retirement) - sometimes referred to as consumption smoothing. This transfer of income represents an increase in value to individuals because the income they have deferred will be worth more to them in retirement than it would have been when they were in work. Freezing the earnings threshold in 2017/18 will have a negligible benefit in terms of an increase in the value of consumption smoothing.

Other Impacts

<u>Equality</u>

51. In accordance with its duty under section 75 of the Northern Ireland Act 1998, the Department has conducted a screening exercise on these legislative proposals and, as

they merely discharge the Department’s statutory duty to substitute the amounts of the upper and lower limits of the automatic enrolment qualifying earnings band and do not alter policy, has concluded that they do not have significant implications for equality of opportunity. In light of this, the Department considers that an Equality Impact Assessment is not necessary.

<u>Environmental</u>

52. There are no implications.

<u>Rural proofing</u>

53. There are no implications.

<u>Health</u>

54. There are no implications.

<u>Human rights</u>

55. The Department considers that the regulations are compliant with the Human Rights Act 1998.

<u>Competition</u>

56. There are no implications.

I have read the Regulatory Impact Assessment and I am satisfied that the benefits justify the costs.

Signed for the Department for Communities

Anne McCleary
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9 March 2017

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Annex A – Methodology

This annex covers the methodology used to estimate the volumes of individuals who will be automatically enrolled into a workplace pension by the end of 2017/18 and total pension saving[13], under the proposed automatic enrolment earnings thresholds.

The estimates are modelled in three key steps:

1. Estimating the number of workers for and from whom additional contributions are due in 2017/18

To look at the overall impact of automatic enrolment (AE), estimates of the pre-AE volumes of employers and employees by employer size are derived from the latest HMRC Pay-As-You-Earn (PAYE) data. This is combined with volume projections from The Pensions Regulator's 2016 revised employer staging profile up to when the reforms will be implemented.

These volumes are used to estimate the **AE eligible target population** (under each policy option) along with the latest available data sources:

- Proportions of all employees who have no pension or a non-qualifying pension pre-automatic enrolment are applied to the projected employee volumes; derived from the 2011 Employers' Pension Provision (EPP) survey, weighted to the Inter-Departmental Business Register (IDBR), to identify the AE **target population**[14].

- **Eligibility rates** for AE at the relevant trigger level are then applied to the target population volumes; determined from the ONS' Annual Survey of Hours and Earnings (ASHE) data[15] broken down by pension provision status, employer size and industry. This identifies those aged between 22 and State Pension age, who earn over the earnings trigger.

It is the difference in the AE eligible target population, under the current and proposed earnings trigger, that gives the estimated number of individuals affected by the policy change.

Assumptions are made about how many people will opt out of a scheme upon being automatically enrolled by their employer. This analysis assumes an opt-out rate of 10 per cent., based on evidence from the 2015 Employers' Pension Provision Survey[16] and observed opt-out rates to date. This gives the total volume of individuals newly saving (no pension pre-AE) or saving more (in a non-qualifying workplace pension pre-AE) as a consequence of AE.

Estimates of the **demographic effects** of different earnings triggers are produced using:

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[13] Further details of the sources and methods used are also available in the Impact Assessment that accompanied the Employers' Duties (Implementation) (Amendment) Regulations 2012: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/220500/wpr-rev-implementation-ia-final.pdf

[14] The target population covers individuals who are either (i) not saving in a pension scheme; or (ii) saving in a pension scheme where the employer contributes less than 3 per cent of the individual's salary, and is not a defined benefit scheme (occupational pension schemes specifying the benefits that are paid on retirement).

[15] For more details on ASHE methodology, see the ONS documents here: http://www.ons.gov.uk/ons/taxonomy/index.html?nscl=Annual+Earnings

[16] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/504346/rr919-employers-pension-provision-2015.pdf

- ASHE data for the year 2012/13 to analyse the eligible target population by gender and age;

- the Labour Force Survey (LFS) 2012/13[17] to analyse the eligible target population by disability status and ethnicity[18].

2. Estimating workers' average pensionable earnings

The average pensionable earnings (an individual's gross salary minus the lower earnings limit of £5,876 up to a capped upper earnings limit of £45,000) of individuals working for different sized employers is determined from the latest ONS Annual Survey of Hours and Earnings (ASHE) data for the year 2012/13 to establish the pensions landscape prior to the implementation of Automatic Enrolment.

3. Total pension contribution of different groups and total pension saving

To calculate the associated pension savings estimates of the proposed policy change, including contributions costs to employers and individuals, a simple equation is used:

Volumes of individuals newly saving or saving more **x** average pensionable earnings **x** minimum legal contribution rate

It is assumed 30 to 40 per cent. of employers immediately contribute 3 per cent. and workers 5 per cent., based on the 2015 Employer Pension Provision (EPP) survey evidence. Otherwise both employers and workers contribute 1 per cent. of band earnings in 2017/18 as outlined in regulations.

Estimates of **individual tax relief** are calculated by multiplying the estimates of individuals' additional pension contributions by the appropriate income tax rate.

To note

Estimates of the contribution costs and tax relief associated with different thresholds are uncertain due to the use of modelling techniques that draw on a range of different data sources. Estimates of the impact of this uncertainty on the accuracy of the estimates are not available so some caution should be exercised in interpreting the figures presented.

DWP will continue to monitor trends within the pension landscape and the economic context into which these reforms will be introduced, and so continue to improve the understanding of how the reforms will affect employers, individuals and the pensions industry.

Estimates of **employer tax relief** represent the tax no longer paid by employers who respond to the additional pension contribution costs of the workplace pension reforms by reducing profits or wages paid to their workers. These are calculated by multiplying the estimates of employers' additional pension contributions by estimates of the percentage of employers who will reduce

[17] http://www.ons.gov.uk/ons/guide-method/method-quality/specific/labour-market/labour-market-statistics/index.html
The data sets: April – June 2012, July – September 2012, October – December 2012 and January – March 2013 were combined to represent 2012/13.

[18] LFS does not collect data on employer contributions to pensions so it is not possible to produce analysis for the eligible target population.

profits or wages and then by the appropriate rate of corporation tax or employers' national insurance contributions respectively. Estimates of the percentage of employers responding to the additional costs of the reforms by reducing profits or wages are taken from the 2015 EPP survey[19].

[19] Page 60 explains employers' most likely strategy in response to the increase in total pension contribution costs resulting from automatic enrolment.

Annex B – Equality implications of changes to the earnings trigger

It is estimated that there are around 11 million workers in the eligible target population for automatic enrolment, of which just under two in five (37 per cent.) are women.

Freezing the automatic enrolment trigger at £10,000 results in a real terms decrease in the trigger and thus includes more individuals. This increase in the target population has been estimated at 70,000 (of which 75 per cent. are women).

As women are more likely to work part-time, or earn less than men, there will be a higher proportion of them represented in the group included in automatic enrolment by a downward revision of the trigger.

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 automatically enrolled 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 these opt in rights.

The latest evidence suggests that the proportion of black and minority ethnic groups (BME) in the eligible group would remain at 9 per cent. if the trigger was frozen at £10,000.

The latest evidence also suggests that freezing the earnings trigger at £10,000 would result in the proportion of disabled people in the revised eligible group remaining at 10 per cent.

The median age of those eligible for automatic enrolment freezing the earnings trigger at £10,000 is 41 years whilst the median age of those in the eligible target group is 38 which indicates that there is a slightly higher proportion of younger workers in the eligible target group in comparison to the eligible group. This is unsurprising given that typically participation in workplace pensions has risen with age.

The changes under consideration for the 2017/18 review are not expected to particularly affect individuals according to their sexual orientation, religion or belief.