PENSIONS

WORKPLACE PENSION REFORM
COMPLETING THE PICTURE

GOVERNMENT RESPONSE TO THE CONSULTATION

January 2010

DWP Department for Work and Pensions

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SECTION 1: INTRODUCTION

1. On 24 September 2009, we published draft pensions regulations for public consultation in a document entitled Workplace Pension Reform – Completing the Picture. This consultation closed on 5 November 2009.

2. The draft regulations covered the following:

   - arrangements for implementing the reforms.

   - elements of the employer duty requirements not covered in the consultation of March 2009, including pay reference periods; voluntary joining for individuals not eligible for automatic enrolment; re-enrolment of eligible individuals; requirements on employers to maintain membership of a qualifying pension scheme; changes to 'the 19 day' rule; and modifications to when postponement can be used for high quality schemes.

   - the quality requirements for defined benefit (DB) and hybrid schemes, including certification for defined contribution (DC) schemes and transitional arrangements during implementation.

   - powers to enforce compliance with the requirements on employers.

3. We consulted formally for a period of six weeks, rather than the usual 12, because we need to provide as much certainty and notice as possible to external suppliers who will be responsible for delivering elements of the employer compliance regime and the personal accounts scheme. Finalising the regulations earlier also avoids the potential costs associated with changing the proposals at a later date, and lastly we felt that all stakeholders and employers, in particular, would similarly benefit from early certainty.

4. Given a shorter consultation period than is normal, and to ensure a thorough and comprehensive response, we shared our thinking with stakeholders through:

   - bi-lateral meetings, seminars and workshops, which we held before and during the consultation period; and

   - meetings with large, medium and small employers; employer representatives, including organisations representing small and medium-sized businesses; employment agencies; intermediaries; trades unions and organisations speaking for individuals; pension providers and insurance companies; pension lawyers; accountants and payroll providers.

5. We received 75 formal written responses to this consultation.

6. We also conducted qualitative research with 66 small and medium-sized employers to explore their responses to a range of aspects of the pension reforms, including the automatic enrolment processes, implementation strategy and compliance regime. This research was conducted as part of the Department for Work and Pension's (DWP) programme of research on pensions, and was commissioned to inform the consultation, the DWP's analysis for the Impact Assessment, and our broader understanding of employers' views on the reforms.

7. Since the consultation closed on 5 November 2009, we have done a thorough analysis of the responses. This document summarises the responses to the consultation and proposes various changes to the draft regulations.

8. It also provides us with the opportunity to respond to some of the issues raised which fall outside the scope of this consultation, but we recognise are of significant importance to enable wider understanding of the reforms or regulations.

9. We are grateful to all those who gave so generously of their time to discuss the issues and share ideas and suggestions. A list of organisations that responded to the consultation is at Annex C.

10. One set of the regulations in this package are subject to the affirmative resolution procedure and will require the approval of both Houses of Parliament before they come into force on the commencement of the employer duty, scheduled from October 2012. These regulations may be subject to drafting and technical amendment.

11. The final regulations will be available on the Office of Public Sector information website at:

    http://www.opsi.gov.uk/si/si-2010-index

    This document is available on the DWP website at:

    http://www.dwp.gov.uk/workplace-pension-reforms

    A paper copy of this document can be obtained from:

    Fiona Mulaisho
    Enabling Retirement Savings Programme
    Department for Work and Pensions
    7th Floor
    Caxton House
    Tothill Street
    London
    SW1H 9NA

    Email: workplace-pension.reform-consultation@dwp.gsi.gov.uk
    Tel: 0207 449 5964

SECTION 2: BACKGROUND, SUMMARY OF SPECIFIC CHANGES AND NEXT STEPS

12. The Pensions Act 2008 (the Act) requires employers to automatically enrol eligible jobholders into qualifying workplace pension saving, with a minimum employer contribution. Individuals who do not want to participate in pension saving have the right to opt out.

13. The Act sets out the ongoing requirements on employers in respect of individuals who remain in workplace pension saving and those who opt out. It sets out minimum scheme quality requirements and provides for a compliance regime to enforce the new requirements. It also sets out how the requirements will be implemented.

14. This document, the third in a series of Government's responses to consultations held by the Department for Work and Pensions (DWP), provides a summary of stakeholders' views on the proposed pensions regulations that are to be made in exercise of powers contained in the Act.

15. **Stakeholders** identified **certification** and **postponement** as the two most controversial areas, and we considered the responses very carefully.

16. Stakeholders were divided over the issue of **certification**, with some wanting the tests to be tighter and some feeling they were too onerous. In addition, there were mixed views over how the process could be made to work and a firm view that the policy, as proposed, would not achieve its original intent. Given this, we have decided to withdraw the certification regulations and to continue to work towards a longer-term solution with our stakeholders.

17. Views on **postponement** were polarised and whilst some stakeholders supported the policy intent, others strongly opposed it. Stakeholders raised concerns that the proposed amendment to the regulations on postponement would not necessarily succeed in its intent – to ensure that individuals would be automatically enrolled even if they only ever worked on short-term contracts. In response, these regulations have been revised and we believe that they now offer the right balance between protecting the rights of jobholders and providing support for employers.

18. **Non-UK schemes** also proved controversial – with stakeholders saying that our approach to these schemes was too tolerant given our lack of control over their regulation. We have addressed these concerns and the revised regulations only allow non-European Economic Area (non-EEA) schemes (that stakeholders raised the most concerns about) to be qualifying schemes, but they cannot be used for automatic enrolment. This will mean that a member will have to make an active choice to join a non-EEA scheme. EEA schemes will still be able to be used for automatic enrolment.

19. Stakeholders provided a range of helpful comments and suggestions across the remaining regulations, on automatic enrolment, information requirements, registration and record keeping, compliance, and quality requirements.

20. We have made changes across a number of areas, to meet stakeholder concerns and to improve the processes set out in regulations wherever possible. We believe these changes are, on balance, a fair offer to individuals, employers and industry as they introduce increased flexibility while removing some of the burdensome prescriptive processes that were identified.

21. We are satisfied that we have re-designed the processes to meet stakeholder concerns without compromising our headline policy intentions or undermining protection for individuals. Our aim remains to establish the minimum level of effective regulation without over-specifying process steps which might place unnecessary burdens on employers or the pensions industry.

Summary of specific changes

Implementation

22. We propose using the **first day of the month for staging dates**, but retain flexibility around the date by which employers must inform the Pension Regulator (TPR) of their preferred date for early automatic enrolment; should this date fall on a weekend or public holiday, employers will be able to use the first working day of that month instead.

23. We propose giving **smaller businesses and those setting up during the implementation period more breathing space** to establish themselves by allowing extra time before they are required to automatically enrol their employees into a pension scheme, bringing them into the reforms after larger existing employers.

24. To accommodate the slightly extended staging period, we now propose that the second transitional period for contributions will start from October 2016 and steady state from October 2017.

Early automatic enrolment

25. We propose amending regulation 3 such that the employer will **no longer be required to set up a scheme before notifying TPR of their wish to automatically enrol early**, or supply a scheme reference number to TPR at that point. The employer will be able to satisfy the conditions for early automatic enrolment by making a declaration to TPR.

Pay reference periods

26. We propose to re-draft the **accidental jobholder provision so that it applies only to workers without annual qualifying earnings.**

27. We propose to **standardise annual pay reference periods** for the purpose of the quality requirement to cater for jobholders automatically enrolled at go-live (i.e. the staging date); jobholders who leave and jobholders who join the employer during the first 12 months after go-live; jobholders whose automatic enrolment is postponed and jobholders joining and leaving during steady state.

Automatic re-enrolment

28. The proposed **re-enrolment date will be a date within one month**, chosen at the **discretion of the employer,** beginning with the three year anniversary of the employer's original staging date and a date within one month every three years after the first re-enrolment date chosen.

Amendments to the postponement of automatic enrolment regulations

29. We propose revising regulation 40 in order to **allow postponement for eligible jobholders** regardless of contract length, but **prevent postponement** for any individual who has already been **postponed by that employer within the previous 12 months**.

Certification of defined contribution schemes

30. We propose **withdrawing the regulations and guidance on certification** and to consult further with the industry group and other stakeholders to see what can be done to help employers within the scope of the primary legislation.

Defined benefits pension schemes and hybrid pension schemes

31. We propose:

- **requiring discretionary revaluation to be accounted for** in a scheme's funding plans for certain career average schemes; and
- enabling employers to choose between **two alternative modified tests for cash balance schemes**.

32. The guidance for employers and actuaries will:

- be clarified on the certification of career average schemes. In particular how the **revaluation of the pensions for those in pensionable service and for those that leave service** is to be included in the quality test.
- make it clearer that to meet the quality requirements a **scheme does not have to exactly match the test scheme or modified test scheme**. For example, it may have its own arrangements for inflation-proofing its pensions, which may differ from the test scheme or the modified version. To qualify, the scheme must provide pensions equivalent to or better than those that would be provided under a test scheme (or benchmark).

Non-UK schemes

33. We propose:

- adjusting the requirement to allow **all non-UK schemes to be qualifying schemes,** but only European Economic Area (EEA) schemes, which are subject to European regulatory requirements, to be used for automatic enrolment.
- **relaxing the 'income in retirement' provision for qualifying schemes** (EEA and non-EEA), though not for schemes eligible for automatic enrolment (EEA only).

Registration

34. We propose:

- **removing** the requirement to provide information on the numbers of **opt outs and voluntary joiners**.
- **significantly simplifying** the requirement for employers to provide **information on why employees have not been automatically enrolled**.
- **removing** the requirement for employers to tell TPR **whether their scheme meets the requirements for delayed automatic enrolment**.
- **requiring registration within two months** of the automatic enrolment date during implementation, giving employers **one month to collate information** now that the opt out requirement has been removed.
- **reducing the information required** at re-registration in the same manner as that required at registration.

Record-keeping

35. We propose that occupational pension **schemes and pension providers will be required to keep**, in respect of those who opt out of scheme membership, **a record of the name of each jobholder who opted out** and **a record of the date on which the employer informed the scheme** that the jobholder had opted out. The requirement to keep the full record of personal information provided by the employer has been removed and no other opt out records need be kept.

Ensuring payment of all contributions due

36. We propose making a small amendment to the due date in regulation 9 in relation to contributions deducted between the automatic enrolment date, the automatic re-enrolment date or the enrolment date and the end of the opt out period. For these, **the due date would be the last day of the second month following the month in which automatic enrolment occurs**. We are proposing that these due date provisions will be included as part of the package of regulations that change the existing 19 day rule.

37. We propose a rate of 4.2% + RPI%, with no floor on RPI. We also propose to amend the definition of RPI in regulation 11(2) (b) to refer to the monthly percentage change in the general index of retail prices for all items.

Fixed penalty notices

38. We propose **reducing** the level of the flat rate fixed **penalty from £500 to £400**.

Time limits on inducements compliance action

39. We propose to leave unchanged the six months complaint time limit but to **extend the period of time over which TPR can look back** when proactively investigating inducements so that that limit aligns with the re-enrolment cycle. This means that TPR will be able to look back in these cases for a possible maximum of **four years**.

Opt out refund process – change to the 19 day rule

40. We propose that the **due date for contributions** deducted from the date of automatic enrolment up to the end of the opt out period will be the **last day of the second month following the month in which automatic enrolment occurs**.

Information (Jobholders affected by transitional provisions)

41. We propose incorporating into regulation 41 the suggestion to include **information about contribution levels**. The drafting will mirror regulation 2(1) (d) (enrolment information).

42. We also propose including the suggestion that information be given about **how the jobholder can opt into** the scheme.

43. We propose amending regulation 41(3) (b) to provide for the **automatic enrolment date instead of the date when the jobholder will become an active member** of the scheme.

Next steps

44. Having removed certification from the second batch of regulations, the remaining regulations will be published on 12 January 2010.

45. It is proposed that these regulations will come into force on the commencement of the employer duties, currently scheduled for October 2012.

46. Recurrent themes in the responses included a strong emphasis on effective communications**,** guidance and information for employers and individuals; and the need for clarifications and clear information on certain topics. DWP will continue to work closely with both TPR and the Personal Accounts Delivery Authority (PADA) to develop a coordinated communication campaign to meet the needs of the different target audiences.

47. DWP will deliver communications and information to individuals and support engagement with employers and their intermediaries by raising awareness of the pension reform and the role employers will play.

48. TPR will deliver communications and education to employers, intermediaries and the industry to support the compliance regime. Guidance will be provided by TPR.

49. On compliance and enforcement, TPR will consult with interested stakeholders on a draft enforcement strategy later in 2010. The strategy will set out its approach to maximising compliance with the new employer duties in line with Better Regulation principles.[1]

50. PADA (soon to be replaced by the Trustee Corporation when established) will provide information about the personal accounts scheme to its prospective employer customers and their advisers. The Trustee Corporation, responsible for running the personal accounts scheme, will communicate with its members as they join the scheme.

[1] Hampton Report: Reducing administrative burdens: effective inspection and enforcement' March 2005. http://www.berr.gov.uk/files/file22988.pdf

SECTION 3: STAKEHOLDERS' RESPONSES TO THE CONSULTATION AND GOVERNMENT'S RESPONSE

(i) DELIVERING THE REFORMS

Implementation Strategy

Background and policy intent

Staging

51. To ensure a smooth implementation of the reforms, it will be necessary to **stage in the application of the duties** to different employers gradually. In doing this, we are seeking the right balance between getting people into saving as quickly as possible and minimising the operational risk associated with implementing reforms affecting more than one million employers and ten million individuals.

52. We propose **bringing employers into the duties by size**, broadly starting with the largest employers and ending with the smallest. Employers will be staged in on a monthly basis, including some months as service breaks within the overall profile, in which no employers are staged in.

53. Within the staged implementation approach, we are proposing to bring a small **test group** of randomly selected small and micro employers into the duties ahead of other similar sized firms. This approach is designed to enable the delivery authorities to understand the responses of small and micro employers, and to adjust their communications and the compliance regime to best meet their needs.

54. Employer size will be ascertained by TPR using pay-as-you-earn (PAYE) data from Her Majesty's Revenue and Customs (HMRC). Employers with more than one PAYE scheme will be required to bring in all of their schemes as soon as their first scheme is subject to the duties.

55. The proposed staging applies to all employers who are operating PAYE schemes prior to a data cut-off date in 2012. New employers who commence operations on or after the data cut-off point will be assigned to further tranches, which will occur towards the end of the staging period. Employers who start trading at or near the end of the staging period will need to start meeting the requirements as soon as they have an eligible jobholder.

Transitional periods

56. The Act prescribes that the quality requirements for pension schemes may be introduced gradually. This is intended to help employers and individuals to adjust over time to the additional costs of pension saving.

57. For **money purchase schemes**, the Act allows employers to phase in the minimum contribution levels over two transitional periods. In the first period, total contributions must be equivalent to at least two per cent of qualifying earnings, out of which the employer must pay at least one per cent. The draft regulations provided that this period will last for the duration of the three-year staging period. In the second period, total contributions must be equivalent to at least five per cent of qualifying earnings, of which the employer must pay two per cent. This period will last for a year.

58. Gradual phasing of contributions is not possible for **defined benefit (DB) and hybrid schemes**, as funding and liability for these schemes has to be maintained at a level agreed between trustees and the employers. Instead, the Act enables employers to delay automatic enrolment into DB and hybrid schemes for prescribed jobholders until the end of the transitional period.

59. The draft regulations set out that the first transitional period will last for three years, starting from the commencement of section 20 of the Act (scheduled for October 2012). Different employers will experience first transitional periods of different lengths depending on their staging date.

60. The Act states that an employer may only delay automatic enrolment into DB and hybrid schemes under transitional arrangements for those individuals who were eligible to join the scheme prior to the employer's staging date. Such jobholders will be able to opt into a qualifying scheme at any point during the transitional period.

61. Where any employer closes their qualifying DB or hybrid scheme during the transitional period (prescribed under section 30 of the Act), the Act prescribes that the employer must immediately automatically enrol jobholders into an alternative qualifying scheme.

62. Where that scheme is a money purchase scheme, the employer must pay employer contributions back to the original staging date (up to three years worth of contributions). The individual may also pay jobholder contributions back to the original staging date if they wish.

What the draft regulations said

63. Regulation 1 sets out the name of the regulations for citation, the date of their commencement and defines relevant terminology for the purposes of these regulations.

64. Regulation 2 prescribes that an **employer will be defined in terms of PAYE scheme size**, or any other description set out in regulation 4, using PAYE data available to TPR at a prescribed date (the data cut-off date). This regulation prescribes that where the duties apply to an employer as set out in regulation 4, and where the employer has more than one PAYE scheme, the duties will apply to every person in all those PAYE schemes at the same time. The regulation provides that an employer with a PAYE scheme established between the data cut-off date and a date in April 2015 will be treated as a new employer in accordance with regulation 4.

65. Regulation 4 includes a table setting out the **staging dates** alongside descriptions of the defined group of employers that are to be brought under the duties on each date. This regulation prescribes that unless an employer satisfies the conditions for early automatic enrolment, the employer duties do not apply to an employer until the corresponding staging date as described in the table.

66. Regulation 5 prescribes that for **money purchase schemes** the length of the first transitional period will be three years beginning with the commencement of the employer duties. The second transitional period will last for one year, following immediately on from the end of the first transitional period.

67. Regulation 6 prescribes that for **DB and hybrid schemes** the length of the transitional period will be three years, beginning with the commencement of the employer duties.

Consultation question

68. We asked for views on the particular date in each month that should be specified as staging dates in regulations. We asked whether stakeholders would prefer this date to be the first of the month (even where this falls on weekends and bank holidays), the first working day of the month, or the first Friday of the month.

Stakeholder responses to consultation

69. Overall, a general concern emerging from the stakeholder responses was the perceived complexity of the staging approach, with widespread views that employers would find it hard to understand what to do and when. Consequently there were unanimous **calls for effective communications** to ensure that employers understand the duties and to minimise the risks of confusion.

70. Many respondents commented on the **length of the staging period.** Opinions were evenly split between those who broadly supported the approach and those who felt that the period is too long, with representatives of employers, workers and the industry on each side.

71. Stakeholders who felt that the staging period was too long commonly argued that this would delay the build up of individuals' pension contributions, and could lead to levelling-down of existing good provision to the minimum. Some also argued that the length of the staging period creates a **competitive disadvantage** to those employers staged in first, and one respondent commented that the complexity involved in the staging approach would create additional burdens for smaller firms in understanding the duties.

72. Respondents in favour of the proposed staging approach typically felt that this was the most pragmatic solution to a difficult operational challenge, although most added that the length was not ideal. Two stakeholders commented that the lengthy staging approach would **help companies to manage the costs** of making contributions in an uncertain economic recovery.

73. A few stakeholders commented on the **size-based approach to staging**, and again the views were divided. Some supported the approach of staging employers from largest to smallest, on the grounds that this would **minimise the burdens for smaller employers**, who are least likely to have any experience of pension provision.

74. However, some stakeholders were concerned about the approach, on the grounds that it would create competition issues within industry sectors, and also because it will delay provision for those individuals who currently have least access to workplace pension saving. Two stakeholders suggested that staging by industry would be fairer, particularly to employment agencies where costs and pricing are very closely related.

75. A handful of stakeholders expressed views on the proposal for a **test group of small firms** to be brought under the duties ahead of similarly sized employers. They recognised the operational need for this, and felt it to be a sensible idea, but two suggested that membership of the test group should be voluntary.

76. Opinions were divided among those who directly answered the consultation question concerning the **definition of staging dates**. Only a couple of respondents felt that staging dates should fall on the first Friday of the month and the remaining respondents' preferences were evenly divided between the first day of the month and the first working day of the month. Those who argued for the first day of the month explicitly stated that this would be simpler and easier to understand.

77. We had a strong response that specifying single dates for staging would be too inflexible, citing two key concerns. Firstly, stakeholders felt that employers would be unable to complete all the necessary processes for meeting the duties on a single day, and also that it would be better for this timing to coincide with existing administrative cycles. Secondly, stakeholders raised concerns that specifying any single date for staging would not fit with the timings for all pay reference periods, and that employers would therefore have to make part-period calculations of contributions.

78. Stakeholders therefore **called for greater flexibility** to allow employers to pick their own staging date within a month long window, or for regulations to prescribe a formula to align staging with individual employers' payroll cycles.

79. Relatively few stakeholders commented on the **proposed transitional arrangements** and their views were broadly divided between support for the proposals and concerns about the impacts.

80. Those in favour of the transitional arrangements felt this to be a sensible approach, and welcomed the added flexibility. By contrast some respondents felt that the phasing period was too long and would cause unnecessary delays to individuals' savings and tempt employers to level down their existing high quality provision permanently.

81. There were some queries around the detail of the arrangements, specifically around the application of DB and hybrid transitions to different types of jobholders, and also around how phasing of employee contributions might work in the absence of phased employer contributions into money purchase schemes.

Government response

82. Since publishing the consultation document, we have continued to assess the implementation plan in the context of current economic circumstances. Our priority is to get the infrastructure in place as quickly as possible, whilst ensuring the reforms are delivered in an operationally achievable way that also supports the economy as it recovers from the current economic downturn. This is best achieved by supporting employers and individuals to adapt to the reforms in a way that maximises sustainability and ensures the maximum shift in savings culture over the medium to long term.

83. After careful consideration, we have decided to **adjust the implementation plan to help new companies**, which are essential to economic recovery and growth. We will allow new firms setting up during implementation more breathing space to **establish themselves before coming under the employer duties**. New companies will be brought into the duties after the main staging for existing employers is complete.

84. This extra support for business means, in turn, that some employees in existing firms will be automatically enrolled into a workplace pension later slightly later than previously envisaged. As the implementation period has been adjusted, the minimum level of contributions for individuals will increase in the following increments - to three per cent in October 2016 and to five per cent in October 2017. Minimum contributions for employers will increase from one per cent to two per cent to three per cent to the same timetable.

85. We understand stakeholders' concerns about the length of staging and phasing, but feel that this slightly adjusted strategy is the right approach to **support the most vulnerable businesses and those individuals who are least used to saving** and taking into account the current economic circumstances. We have **mitigated the competition impacts of**

staging as far as possible by ensuring that employers of similar sizes are staged in together. We have also aligned the first transitional period for contributions with the staging period, to minimise any disparities in costs between employers who are brought into the duties at different times.

86. We considered **staging by industry** during development of the implementation policy, but concluded that this was neither achievable nor desirable. Operationally it would not be possible to achieve a smooth ramp up of activity, since employers are not evenly distributed by industry. It would also be extremely difficult to define employers by industry for staging of the duties, since there is no central, consistent definition of industry by sector, and some companies span more than one sector. We also feel that staging by industry would have more serious competition impacts, since smaller firms could be brought into the duties ahead of their larger competitors.

87. We have also carefully considered whether **employment agencies** could be staged in as a single group, in line with the concerns raised by stakeholders. We fully recognise the concerns raised by stakeholders, but do not believe this would be feasible. Bringing in the entire employment agency sector in one stage would not be operationally viable - the volume of individuals automatically enrolled, in particular, would be too high. In addition, we have not seen sufficient evidence to support the view that employment agencies form a sufficiently distinct group with unique competitive issues that would justify special treatment. Finally, TPR are unable to identify agencies from HMRC data, rendering them invisible to the compliance regime should we try to stage these companies as an industry group.

88. We therefore do not propose changing our approach of staging firms by size. However, we suggest that there could be an **industry-led solution** to this concern, making use of the flexibility provided by early automatic enrolment in order to bring employment agencies under the duties together, and we will look to provide all possible support to the industry in using this approach.

89. With regard to the **test group of small firms**, we appreciate stakeholder support for this, while recognising concerns around the competitive impacts for those involved. However, were we to make inclusion in the group voluntary, there is a significant risk that we would not achieve the necessary numbers of employers to conduct reliable research and provide robust analysis; this would render the test ineffective. We are aiming to **limit the time lag between the test group and later tranches** as far as possible, to **minimise any competitive impacts**.

90. Stakeholders raised significant concerns around the flexibility of **staging dates**. With regards to concerns around timing of administration, we feel that the one-month joining window **provides employers with freedom to undertake relevant administration at a time that suits them**, to align with existing arrangements.

91. We recognise that this does not resolve concerns around part-period calculation of contributions, but are not able to provide that measure of flexibility for staging under the powers in the Act, nor do we feel this would be desirable. It is necessary at the point of implementation that there is certainty around the date that the employer duties first apply and that these dates are definite dates that TPR can easily identify in accordance with the regulations. This is due to the scale of the operation at implementation and the number of initial compliance activities attached to the original staging date. This is why the Act only allows for specified staging dates, rather than ranges, to be defined in regulations.

92. With regard to the consultation question around the timing of staging dates, there was no single majority view putting one option over another. In response to the specific comments raised around simplicity and clarity, we propose using the first of the month for staging dates.

93. However, we also propose **retaining the flexibility around the date by which employers must inform TPR of their preferred date for early automatic enrolment**, allowing firms to move these to the first working day of the month should the first fall on a weekend or public holiday.

94. We recognise and agree that communication and information will be vital to support the successful implementation of the reforms. It is important for the reform programme to be communicated effectively to employers and their intermediaries, as well as to the individuals who are affected. DWP is working closely with TPR and the Personal Accounts Delivery Authority to **develop a coordinated communication campaign** to meet the needs of the different target audiences. Guidance and templates, where appropriate, will be provided by TPR to ensure employers know what they must do, how, and by when, to comply with the employer duty.

Proposal for change: Implementation

- We will give smaller businesses and those setting up during the implementation period more breathing space to establish themselves by allowing extra time before they are required to automatically enrol their employees into a pension scheme, bringing them into the reforms later than the main staging for larger existing employers.
- We now propose that the second transition period for contributions will start from October 2016 and steady state from October 2017.
- We will use the first day of the month for staging dates, but retain flexibility around the date by which employers must inform TPR of their preferred date for early automatic enrolment. Should this date fall on a weekend or public holiday, employers will be able to use the first working day of that month instead.

Early automatic enrolment during implementation

Background and policy intent

95. The implementation regulations set out the dates on which employers will become subject to the employer duties over the staging window. Currently, new employees may be automatically enrolled into occupational schemes but employers may not automatically enrol existing employees, or use automatic enrolment into Group Personal Pensions (GPP) until they become subject to the duties under the Act.

96. For administrative reasons some employers may wish to bring forward their automatic enrolment date to an earlier date. We will provide employers with the flexibility to do so, bringing more people into pension saving early.

97. Employers will be able to bring forward their automatic enrolment to a specified date after October 2012. This will be conditional on the employer informing TPR of their intention to do so, and being in a position to demonstrate that they are ready.

98. As with staging, employers operating more than one PAYE scheme who choose to bring forward their duty date will be required to do so for all of their PAYE schemes.

What the draft regulations said

99. Regulation 3 sets out how the employer duties are to apply to an employer who wishes to bring their automatic enrolment date forward. The employer may select a new, earlier, date from those set out in the table of staging dates under regulation 4. However, in order to bring their duties forward to this date, the employer must satisfy certain conditions:

- identify and contact a suitable scheme, and agree with the provider that they will use this scheme to discharge their duties from the new date.
- notify TPR in writing that they have met the above condition.
- notify TPR by a certain date, corresponding with the chosen date on which the employer duties will apply to that employer. This date is set out in the table under regulation 4.

100. Where the employer satisfies these conditions, they will be notified by TPR that the duties will apply from their chosen, early date. If the employer does not satisfy the conditions set out in regulations for early automatic enrolment, the employer duties apply to that employer on the date allocated to them according to the table in regulation 4.

Consultation question

101. We asked how TPR should establish that the employer will be ready. Specifically, we asked whether the employer should be required to have a scheme in place before applying, or whether they should be able to sign a declaration that they are confident they will be able to discharge their duties.

Stakeholder response to consultation

102. There was **widespread support for the principle** of allowing employers to bring forward their automatic enrolment, and stakeholders were generally **keen to have as much flexibility as possible** for employers during implementation.

103. There was a range of opinions on how employers should demonstrate to TPR that they are prepared to automatically enrol early. Some stakeholders felt that employers should have to have a scheme in place before approaching TPR, to ensure that they are definitely able to discharge their duties. One respondent commented that some employers might underestimate the scale of the task involved in making pension arrangements, and may thus fail to be ready for early automatic enrolment.

104. However, the majority of respondents felt that a requirement to have a scheme in place was unnecessary and overly burdensome, and **called for a light-touch approach**. Most stakeholders felt that asking the employer to **provide a declaration stating their readiness would suffice**, and a handful of respondents felt that the employer should not have to provide any evidence to TPR at all.

105. One of the key factors underpinning these responses was the widespread view that no employer would opt to bring their automatic enrolment date forward unless they had the necessary arrangements in place to allow them to do this successfully, and that most would in practice already have a scheme set up.

106. Most stakeholders thus took the view that the risk of early adopters failing to prepare and becoming non-compliant was overstated. It was felt that an employer who was considering early automatic enrolment would already be aware of the issues and penalties for non-compliance and would factor this into their decision.

107. Some stakeholders pointed out that an employer would not have to provide any evidence to TPR that they were ready for automatic enrolment if they stuck to their prescribed staging date and they therefore felt that the early automatic enrolment process should mirror this as far as possible. There was a commonly-held view that the early automatic enrolment process should be made as easy and simple as possible, in order to **reduce burdens on employers and encourage them to go early**.

108. There were some points raised about the detail of the process. Several stakeholders commented that employers should have to agree the new specific automatic enrolment date with TPR, and one suggested that TPR should provide example time-lines for setting up pension arrangements to help employers with their preparations.

Government response

109. The overall weight of opinion was that the process should be as simple as possible, and that requiring employers to already have a scheme in place prior to notifying TPR would be unnecessary and overly burdensome. We agree that it is important to find the right balance between minimising the burdens on employers (and providers) whilst providing TPR with sufficient assurance that employers who choose to go early will be able to meet their duties.

110. Moving the employer's automatic enrolment date means changing the date when the employer comes under the duties, along with all the associated compliance requirements and enforcement processes.

111. We are keen to avoid potential situations in which employers who choose to go early then become non-compliant, through unfamiliarity with the processes and time needed to set up a new scheme. For this reason, we do not feel it would be appropriate to allow the employer to bring forward their staging date without some proof that they are prepared to discharge their duties. At the same time, we agree that requiring the employer to have a scheme in place before contacting TPR could create unnecessary burdens on both employers and pension providers.

112. We therefore propose amending regulation 3 to **remove the requirement on the employer to provide a scheme reference number to TPR**.

113. To satisfy the conditions for early automatic enrolment, the employer will effectively have to **make a declaration to TPR** that they:

- understand the implications of bringing their automatic enrolment date forward, in that the compliance regime will apply from that date.

- have an agreement with a provider to supply a scheme that will accept all their eligible jobholders from the new date.

Proposal for change: Early automatic enrolment

- We propose amending regulation 3 such that the employer will not be required to set up a scheme before notifying TPR of their wish to automatically enrol early, or supply a scheme reference number to TPR at that point. The employer will be able to satisfy the requirements for early automatic enrolment by making a declaration to TPR.

(ii) MAXIMISING INDIVIDUALS' OPPORTUNITIES TO SAVE

Pay reference periods

Background and policy intent

114. Pay reference periods (which are different for different purposes of the Act) are the device that will make automatic enrolment, the calculation of minimum pension contributions and the scheme quality tests work in practice. We have set pay reference periods to match normal pay cycles so that an employer can identify whether a person should be automatically enrolled and calculate contributions and an annual pay reference period for the money purchase schemes quality test and to identify workers without qualifying earnings.

115. The lower and upper limits of the qualifying earnings band are expressed in annual terms in the Act. Employers using the definition of qualifying earnings in the Act should pro rata the annual threshold and upper limit to normal weekly /monthly (etc) pay periods to identify whether a person should be automatically enrolled and calculate pension contributions.

116. To be a qualifying scheme, the scheme must require contributions, however calculated, to be equal to or more than eight per cent of the jobholder's qualifying earnings in the relevant pay reference period, of which at least three per cent must be the employer's contribution.

117. We do not require existing schemes to change their rules for calculating contributions or change the scheme definition of pensionable pay but we consider that the scheme (or product) documentation must require that the total amount of the contributions in order to be a qualifying scheme over a year must be at least equal to eight per cent of the band of qualifying earnings. If an individual is only in the employment (or only has jobholder status) for a part-year then the annual quality requirement is proportionately reduced.

118. Workers earning less than qualifying earnings - £5,035[2] and under - are excluded from automatic enrolment. To translate this exclusion into practice our policy is to exempt workers without qualifying earnings who become *accidental jobholders* from automatic enrolment. These are individuals with annual contracted earnings under the qualifying earnings band (i.e. £5,035 or less) who may, exceptionally, earn enough to gain jobholder status in an isolated normal pay period but will not earn over the threshold of the qualifying earnings band for the whole year.

What the draft regulations said

119. Regulation 4 prescribes a pay reference period of one week (or the jobholder's normal pay period if that is longer than a week) to identify a jobholder and thereby trigger automatic enrolment.

120. Regulation 4 also prescribes a period of 12 months (or the period of the employment if that is shorter) to calculate whether the quality requirement for money purchase or personal pension schemes is met and a period of 12 months for accidental jobholders.

[2] This threshold is in 2006/07 earnings terms and will be up-rated in line with the rise in average earnings in readiness for go-live.

Consultation question

121. We asked whether the provision to exclude accidental jobholders inadvertently applies to workers with a zero-hours contract.

Stakeholder response to consultation

122. Stakeholders considered that the essential **mechanics of pay reference periods** to enable the employer to identify jobholders and thereby trigger automatic enrolment and calculate contributions were **workable but very complicated**, and **needed detailed guidance** to explain how they would work in practice.

123. Stakeholders asked for a more detailed explanation of **how the annual pay reference period for the quality tests worked**, how this related to normal pay cycles and when an "annual" period would start.

124. Employer organisations, pension providers, accountants and benefit consultants **welcomed the accidental jobholder provision in principle**, as it aims to clarify the distinction between arrangements for people with jobholder status (and qualifying earnings) from workers without qualifying earnings. However, they felt that as drafted, the distinction was confused and conflated the status of the two groups.

125. Large employers in the retail sector saw the provision as a way of making arrangements for part-time jobholders and individuals with fluctuating earnings. Others felt that it could create a disparity between the treatment of salaried jobholders, jobholders with zero-hours contracts and agency workers. Worker representatives did not support the principle of the exemption but accepted a need for such a rule for practical reasons.

126. Stakeholders had significant **reservations about whether the provision as drafted would work in practice**. They felt that it required employers to predict the future or carry out individual end-year "mini certification". They considered that it seemed to catch individuals with zero-hours contracts and in effect exempt them from automatic enrolment.

Government response

Automatic enrolment and the calculation of contributions

127. We recognise that pay reference periods are a complex subject. Stakeholders' responses clearly identified the areas with which people have most difficulties and topics where very clear guidance will be essential to assist employers and providers to operate the provisions of the Act. We will be working closely with TPR to assist in the **development of guidance for employers**.

128. Employers may not wait until a jobholder has accumulated earnings in excess of £5,035 before they automatically enrol. For practical purposes, automatic enrolment is triggered when a jobholder earns over the weekly, four-weekly or monthly threshold in their normal pay cycle straight after go live.

129. This applies equally to jobholders with fluctuating earnings. Earnings over the threshold in a normal pay period will trigger automatic enrolment and the employer will make arrangements to achieve active membership in the usual way. If earnings subsequently dip below the threshold the person does not necessarily lose their active membership status (this will depend on scheme rules) rather contributions will resume next time earnings exceed the relevant threshold.

130. For agency workers, where the agency will not at first know how much the person is likely to earn, automatic enrolment will be triggered when an assignment with sufficient earnings starts (not necessarily the day the person first signs on with the agency). Then the agency calculates contributions due on earnings in the relevant pay reference period based on actual earnings – either using the qualifying earnings formulation or the definition of pensionable pay used by whichever scheme the agency has chosen to use.

Quality Requirements and annual reconciliation

131. The annual pay reference period for the schemes quality test is jobholder specific. We propose to amend the regulations to make it clearer that **this pay reference period starts on the jobholder's "day one" and runs for one year**. "Day one" for jobholders automatically enrolled at go–live will be the employer's staging date.

132. A jobholder may of course leave that employment at any time and the regulations provide for the "annual" quality test to be the period in the year during which the person was a jobholder with that employer. The provision, as drafted, caters for jobholders with the employer at go-live and jobholders who leave the employer during the first 12 months. It does not cater for jobholders who start with that employer in the first 12 months after go-live; jobholders whose automatic enrolment is postponed or for jobholders joining that employer during steady state.

133. We propose to standardise annual pay reference periods for annual reconciliation purposes to cater for jobholders automatically enrolled at go-live (i.e. the staging date); jobholders who leave and jobholders who join the employer during the first 12 months after go-live; jobholders whose automatic enrolment is postponed and jobholders joining and leaving during steady state. Eventually all jobholders will have a period for annual reconciliation which ends on the anniversary of the employer's original staging date.

Accidental jobholders

134. The accidental jobholder provision was never intended to provide an alternative automatic enrolment route for agency workers or workers with fluctuating earnings, or to enable employers to adapt the regulations to deal with workers with irregular earnings. Nor do we expect employers to predict the future and we recognise that, as drafted, the provision is too wide and accidentally catches individuals with zero-hours contracts.

135. We propose to retain the principle but **re-draft the regulation to limit its application** to the minority group for whom it was intended. When a worker without qualifying earnings has an unexpected earnings spike over and above their regular wage the actual value of the spike is added to contracted annual earnings. If this still produces total earnings of £5,035 or less they will not be automatically enrolled.

136. We propose to clarify that the 12 month pay reference period in relation to accidental jobholders will commence on the employer's staging date (and each anniversary of that date) or the date the worker started with that employer.

137. If the value of the earnings spike in a pay reference period, when added to their contracted annual salary (even if not all of it has been earned yet) takes them over the annual threshold then the 12 month pay reference period will cease to operate. Instead, the person will be subject to a weekly or monthly pay reference period and the spike in earnings will be accommodated in the first weekly/monthly period.

138. Employers will be required to make a factual decision, based on actual additional earnings plus an assumption of continuing contracted earnings, **to identify the point when a worker** without annual qualifying earnings **acquires jobholder status**. When this happens the earnings spike ends the annual pay reference period. The person, now a jobholder, should be automatically enrolled at that point and contributions deducted in the appropriate pay reference periods thereafter. We will not require the employer to backdate contributions.

Proposal for change: Pay reference periods

- We propose to re-draft the accidental jobholder provision so that it applies only to workers without annual qualifying earnings
- We propose to clarify that the 12 month pay reference period in relation to accidental jobholders will commence on the employer's staging date (and each anniversary of that date) or the date the worker started with that employer.
- We propose to standardise annual pay reference periods for annual reconciliation purposes to cater for jobholders automatically enrolled at go-live (i.e. the staging date); jobholders who leave and jobholders who join the employer during the first 12 months after go-live; jobholders whose automatic enrolment is postponed and jobholders joining and leaving during steady state.

Voluntary saving

Background and policy intent

139. The Act prescribes that employers must automatically enrol all their workers aged 22 and over, under pensionable age and earning more than £5,035 a year into a workplace pension scheme. The Act also makes provision for voluntary saving on an opt in basis for people who are not eligible for automatic enrolment.

140. To make it easy for people to opt in once they have made a decision to save in a pension, they can give notice of opt in in writing to their employer by letter or e-mail. Employers and providers are free to provide a form if they choose but we do not want to legislate to impose a standard form.

141. Employers will not necessarily know that an individual is about to give notice of opt in and we want to avoid a situation which requires an employer to backdate pension contributions to the date of the notice, because this could include a period for which wages have already been paid.[3] Our policy for these voluntary opt in savers is to mirror a common current pensions practice and enable membership to start from a forward date. The liability for pension contributions will start from and including the first day of the next pay reference period after the employer receives notice or the one after that if payroll has closed down. This principle of a prospective start date for active membership applies to both jobholders and workers without qualifying earnings, and avoids a "contributions cliff edge".

142. Once a jobholder has given notice of opt in the standard automatic enrolment arrangements will apply. The employer must make arrangements to achieve active membership, provide

[3] In the automatic enrolment process it is membership that is backdated not contributions (which are taken from "Day One") so the situation of arrears and backdated contributions does not arise.

jobholder information to the scheme and enrolment information to the jobholder. A jobholder who opts in voluntarily has a right to opt out within the opt out period, with a full refund.

143. For workers without qualifying earnings the employer can make arrangements with the individual and a scheme in accordance with scheme rules. We do not wish the employer to have to identify and set up a scheme that will take these individuals in anticipation of receiving an application. All we require the employer to do is to make arrangements to achieve active membership if they get such a request with a scheme that will take them as members.

144. The employer, having made arrangements with a scheme to take a worker without qualifying earnings, may not disengage thereafter. The employer has a continuing role to pay the worker's contributions to the scheme. We are content to leave the frequency of such contributions as a matter to be decided between the scheme and the individual and the employer, subject to scheme rules.

What the draft regulations said

145. Regulation 19 prescribes how jobholders must give notice of opt in and applies the standard automatic enrolment joining processes and one month joining window to opt in. The regulation exempts an employer from having to take any enrolment action where the jobholder changes their mind before the enrolment date and withdraws their opt in notice and sets the start of active membership (the enrolment date) as a forward date tied to the jobholder's normal pay cycle.

146. Regulations 20 and 21 extend the opt out and refund provisions to people who become active members as a result of opting in voluntarily.

147. Regulations 23 and 24 prescribe how a worker without qualifying earnings applies to join pension saving and sets out what an employer must do to achieve active membership of a tax registered scheme for the individual.

Stakeholder response to consultation

148. Stakeholders were **generally supportive of the principle** that gives **universal access to pension saving** to jobholders who are not eligible for automatic enrolment, but sceptical about whether it is necessary to provide an opt out right for someone who has chosen to opt in.

149. From a practical perspective stakeholders **endorsed the light administration approach** which allows an **opt in notice to be simply in writing** without the need for a specified form from either the scheme or the employer. They urged that administrative requirements for voluntary savers should be kept to a minimum using established automatic enrolment processes rather than separate processes.

150. There was some confusion about whether the quality requirements and annual reconciliation applies in the case of opt in.

151. Other minor comments included: some concern about allowing jobholders under age 22 into a **scheme which operates an age limit**; the **information requirements** on employers in relation to voluntary saving rights; and the obligations (if any) on employers and schemes to retain the opt in form or to **keep records of opt in**.

152. Stakeholders were critical of the requirement that employers arrange membership of a scheme for workers without qualifying earnings because employers are not obliged to make a

pension contribution for workers without qualifying earnings. Stakeholders found it hard to see why the employer should be required to provide access to a specific scheme and provide a service to remit contributions to the scheme rather than just point the individual in the direction of a personal pension policy.

Government response

153. As stakeholders broadly endorsed the principle of one process for all we propose to retain the provision which **applies the basic automatic enrolment processes to jobholders who opt in**.

154. A jobholder who opts in is in a consensual - rather than a compulsory - environment and having given notice of opt in has, in effect, given permission for the employer to make arrangements with a scheme. This enables the employer to satisfy the requirements of the Data Protection Act and can pass jobholder data to the scheme in advance of the enrolment date.

155. After a jobholder has given notice of opt in the employer will take pension contributions from earnings. **It is a requirement of the Act to give jobholders who change their mind an opt out right** with a right to get their money back **even though they opted in voluntarily**. We accept it is unlikely that someone would go to the trouble of opting in only to opt out again straight away but not impossible and the Act gives them a right to a refund.

156. Our intention is to provide access to workplace pensions saving vehicle on request for workers without qualifying earnings with active membership and ongoing worker pension contributions *facilitated by the employer*. There is no obligation for an employer to pay a pension contribution for these individuals although some employers may choose to do so.

157. We believe **the policy for workers without qualifying earnings is best delivered if employers** identify a scheme prepared to take the individual, **make whatever arrangements the scheme rules require** to take them as members and deduct contributions through payroll. We do not accept that the employer has no role other than to introduce the worker to a pension provider and we do not propose to change our policy in this area.

158. Once a jobholder has given notice of opt in and is an active member of an automatic enrolment scheme they are, for all purposes, in exactly the same position as someone who was automatically enrolled into a scheme. The minimum (equivalent) contribution levels, the quality tests and annual reconciliation (where appropriate) all apply.

159. Where a scheme operates a **qualifying age threshold** the scheme will not be an automatic enrolment scheme in relation to any individual under the qualifying age. Stakeholders sought confirmation of this point in relation to younger jobholders who may give notice of opt in but it applies equally to automatic enrolment where a scheme **may not be an automatic enrolment qualifying scheme** for persons under, say, age 25 if there is an age 25 age bar.

160. Employers would **have to identify an automatic enrolment scheme** that would take the individual or seek to change the scheme requirements. In such situations the scheme would however be an automatic enrolment qualifying scheme (providing it satisfied the quality criteria) for jobholders over the age bar.

161. Other concerns raised by stakeholders about information requirements on employers in relation to voluntary saving rights and obligations on employers and schemes to retain the opt in form or to keep records of opt in, are addressed in the Provision of Information section of this report, (Page 65).

Automatic re-enrolment

Background and policy intent

162. The Act places a duty on employers to re-enrol periodically jobholders who have left pension saving either during or after the opt out period. While pension saving may not have been the right choice at the point at which the jobholder opted out or left, a jobholder's financial situation or priorities may change.

163. Under our proposals, employers will have a duty to re-enrol jobholders who are not active members of a workplace pension every three years.

164. An anniversary to trigger auto re-enrolment has to be easily identifiable by employers and give providers and TPR manageable volumes of activity at any one time. To achieve this, re-enrolment will be linked to the anniversary of the employer's staging date so that employers will only have to carry out re-enrolment for those members of their workforce who are eligible jobholders but who are not active members of a qualifying scheme once every three years.

165. We propose some flexibility for jobholders who have only recently opted out or cancelled their membership before the re-enrolment date. We think it is reasonable to assume that jobholders who have recently opted out (or ceased saving after opt out) are more likely to opt out again and also are unlikely to have had a significant change of circumstances. Therefore we intend that anyone who has taken such a decision within 12 months of the re-enrolment date is exempt from re-enrolment until the next three year anniversary.

166. We are proposing two exceptional circumstances where the routine three year re-enrolment will not be appropriate, and it will not be sufficient to depend on a jobholder proactively opting in. In these special cases the employer will be required to immediately re-enrol jobholders. The special circumstances will be rare but are where:

- a third party takes action which stops membership or lowers the contribution level in a high quality defined contribution scheme used under postponement (where the employer contributes six per cent); and

- a third party takes actions which stops an individual being a member of a qualifying scheme or the scheme ceases to be a qualifying scheme.

167. Where an employee stops being a jobholder (earnings fall below £5,035 or they are no longer considered to be working in Great Britain (GB)) but then starts again, the re-enrolment date will be the day the jobholder status returns. We do not intend that this situation should necessitate the full enrolment process in all cases, so where the jobholder remains a member of the scheme (but not an active one) the re-enrolment process will simply require that the employer makes arrangements with the scheme to achieve active membership again.

What the draft regulations said

168. Regulation 13 prescribes a three-yearly cycle for automatic re-enrolment linked to the employer's staging date.

169. This regulation also provides for immediate re-enrolment where a person other than the employer or the jobholder takes action that results in the jobholder ceasing to be an active member of a quality scheme, or the scheme ceases to qualify, or the scheme ceases to be a

quality scheme that can be used for the purposes of postponement as outlined in section 4 of the Act.

170. Where a jobholder ceases to earn above the qualifying earnings threshold or ceases ordinarily to work in GB and therefore no longer meets the definition of jobholder outlined in section 1(1) of the Act, the re-enrolment date is the date that jobholder status returns - i.e. the day on which the person's earnings rise above the qualifying earnings threshold or the jobholder returns to ordinarily work in GB.

171. Regulation 14 provides that the arrangements the employer must make to achieve active membership for a jobholder with effect from the automatic re-enrolment date are the same as for automatic enrolment, and the regulation also replicates the one month joining window for re-enrolment.

172. Regulation 14 also outlines that where a jobholder falls below the lower earnings limit or stops ordinarily working in GB the employer must enter into arrangements with the scheme from the date that jobholder status returns to make the member an active member. The regulation also provides an over-riding definition of active membership for re-enrolment purposes.

173. Regulation 15 prescribes an exclusion period of 12 months prior to the re-enrolment date for those jobholders who ceased to be an active member of a qualifying scheme through their own choice or who gave notice to opt out during the opt out period.

174. Regulations 16 and 17 apply opt out provisions and refund rights to re-enrolment.

Consultation questions

175. We asked whether there are any circumstances where action could be taken by a third party that either results in the jobholder no longer being an active member or the scheme ceasing to qualify without the employer knowing about it in advance.

176. We also requested any views that stakeholders had on the timescale for re-enrolment in the exceptional circumstances.

Stakeholder response to consultation

177. Stakeholders **broadly support that re-enrolment should take place every three years** on a fixed date from the employer's staging date, as this provides a sensible compromise between the burden on employers and the need to encourage scheme membership.

178. A significant number of stakeholders **called for flexibility to align payroll cycles** at the staging date (and therefore the re-enrolment date) with one stakeholder stating that employers should have flexibility to change their re-enrolment date to allow, for example, groups of companies to align their re-enrolment dates.

179. Some stakeholders **sought clarification** as to whether **re-enrolment applied to those that had left pension saving after the opt out period** as well, as those that opted out within it and also sought clarity as to what re-enrolment date would apply where a jobholder moved from one company to another.

180. In relation to the re-enrolment date for the exceptional circumstances, a number of stakeholders were of the opinion that it was unlikely that there would be many circumstances where a third party would take action that results in the scheme ceasing to qualify or the

181. Stakeholders also saw the merit of **ensuring that the jobholder enjoys continuous membership** and does not suffer a break in contributions in these circumstances. Some stakeholders felt that the one month joining window allowed the employer sufficient time to take the necessary action to rectify any third party action.

182. A significant number of stakeholders said that **although rare** there was the possibility that a **third party error could occur that the employer would not be aware of** until after the event, also where the pension provider introduces an immediate change or where HMRC de-registers a scheme, the employer is unlikely to know in advance. In these cases stakeholders felt that a grace period of between one month and three months from the date the employer becomes aware of the change would be preferable.

Government response

183. Given the broad support for re-enrolment, we will keep it as it is so that it occurs **every three years**.

184. Where an employee leaves one company and joins another they will be automatically enrolled from the date the new employment starts (provided they are an eligible jobholder). If they then choose to opt out of pension saving or leave they will be re-enrolled in line with the new employer's re-enrolment date**. Re-enrolment applies to those jobholders who opted out during the opt out period or left pension saving subsequently**.

185. There has been a significant stakeholder voice asking that staging dates are more flexible to allow alignment with payroll cycles. It is necessary at the point of implementation that there is certainty around the date that the employer duty first applies and that this date is a definite date that TPR can easily identify. This certainty is needed due to the scale of the operation at implementation. This is why the Act only allows a single staging date.

186. As we move beyond the implementation period there is scope for more flexibility at the point of re-enrolment. It is not appropriate for employers to be able to choose any date in the year to re-enrol. This is firstly because the Act does not allow employers to carry out re-enrolment more frequently than every three years and secondly, we have to consider volume constraints to deal with the re-enrolment process and queries from employers.

187. We are able to **provide some flexibility around the re-enrolment date** that will allow employers to align with payroll cycles and we propose that we will allow employers to choose a date within a one month window, beginning with the three year anniversary of the employer's original staging date. This **one month window** will apply to each re-enrolment event.

188. The two exceptional circumstances included in the Act are there as protection to jobholders to ensure that in these specific scenarios, the jobholder could be re-enrolled back into a qualifying scheme as soon as possible. In the rare instances where these circumstances occur, there is potential detriment to the jobholder if they miss out on contributions. Therefore it is felt **appropriate that membership should be seamless** and the jobholder should enjoy continuous membership. We therefore propose to **keep immediate re-enrolment for these exceptional circumstances**. In line with TPR's risk-based approach to enforcement, procedural obstacles such as where the employer is genuinely unaware of the third party action until some time after the event, will be taken into account in making risk based decisions to pursue enforcement activity.

189. We have considered the regulations in respect of achieving active membership for re-enrolment purposes and have refined our approach. By focussing on the definition of an automatic enrolment scheme, we can **remove the need to define active membership within the re-enrolment regulations**. This is because an automatic enrolment scheme must be a qualifying scheme as required by section 20 and section 26 of the Act in relation to the jobholder. Therefore where a jobholder is not an active member of an automatic enrolment scheme, they must be re-enrolled.

Proposal for change: Automatic re-enrolment

- There will be greater flexibility around the re-enrolment date.
- The re-enrolment date will be a date, chosen at the discretion of the employer, within one month of the three year anniversary of the employer's original staging date and a date within one month every three years after the first re-enrolment date chosen.
- We will remove the definition of active membership for re-enrolment purposes in regulation 14.

Employer duty to maintain active membership

Background and policy intent

190. The employer has a duty to enrol a person into a scheme and also maintain a jobholder's active membership of a qualifying workplace pension scheme while they are employed unless the jobholder themselves takes action to disengage from membership.

191. An employer may not cause a scheme to cease to qualify or eject a jobholder from a qualifying scheme, or induce them to terminate active membership or opt out without the jobholder becoming an active member of another qualifying scheme.

192. There is no requirement that the end of active membership of the old scheme and the start of active membership of the replacement scheme are seamless, nor that pension contributions continue without interruption. The policy intention is to allow employers a short prescribed period to finalise the move from one scheme to another.

193. An employer is not in breach of the prohibition on inducement if they induce a jobholder to give up membership of a qualifying scheme provided the jobholder becomes an active member of another qualifying scheme within this period.

194. The period is not intended to be the first time that an employer approaches a provider to arrange a replacement scheme. We want to provide the employer with some leeway to finalise, rather than start, joining arrangements in the replacement scheme. It is a safety net so that an employer is not in breach of the employer duty because of an administrative delay, possibly beyond their control.

What the draft regulations said

195. Regulation 26 prescribes a period of one month after the date that the jobholder ceases active membership of a qualifying scheme or the scheme ceases to be a qualifying scheme for the jobholder to become a member of a replacement scheme.

Stakeholder response to consultation

196. Regulation 26 prompted **very few responses** but there were two distinct themes. Employee representatives felt that regulation was not necessary because existing legislation that requires a 60-day consultation period on scheme changes already provides sufficient cover. They felt that an extra month would provide an employer with the opportunity to avoid their obligations by continually re-organising their scheme and reward employers who did not plan properly. In any case membership should be backdated to the date when the old scheme ceased to exist.

197. Actuaries and accountants were agnostic on the need to regulate but felt that a time limit of one month is a sensible approach.

Government response

198. We acknowledge there is existing legislation for occupational and personal pensions that requires employers who employ over 50 people to consult on certain scheme changes with active and future members (and their representatives) within a 60 day window. Large organisations advised by lawyers and accountants in such matters are very likely to take timely action and not need an additional administration period. However, smaller companies or those with a peripatetic workforce may need this gap to finish the process of the switchover and to prevent accidental breach as a result of a minor administration delay or events beyond their control. Therefore we intend to keep the one month gap.

Amendments to the postponement of automatic enrolment regulations

Background and policy intent

199. The Act allows employers to postpone automatic enrolment for a period of time where they offer a high quality scheme. This provision is intended to encourage employers offering higher-quality schemes to continue to do so.

200. This measure was contained in regulation 17 of the draft Pensions (Automatic Enrolment) Regulations which we consulted on in Spring 2009. This regulation, as drafted, enabled employers to use postponement for all jobholders, including those on short-term contracts. The response to the consultation raised concerns around the potential impacts of postponement, specifically that some workers may never be automatically enrolled if they only ever worked on short-term contracts and for employers operating postponement schemes.

201. This issue is a finely balanced one, between ensuring individuals' access to saving and minimising the burden on business. We decided to re-consult on an amended draft regulation in order to invite views on whether this achieved a suitable balance; this amendment aimed to protect the rights of short-term workers by restricting the use of postponement.

What the draft regulations said

202. Regulation 40 specifies that postponement may only be used where jobholders are due to become active members of the relevant scheme; that is, jobholders whose contract extends beyond the postponement period.

203. This regulation specifies that the postponement period is three months, and that for a further three months the employer must not do anything which might mean that the member ceases to be an active member of the scheme or that the scheme ceases to qualify for postponement.

204. This regulation sets out that postponement may be used with regard to qualifying defined-benefit schemes and for money purchase schemes where the employer contribution is equivalent to at least six per cent of qualifying earnings and total contributions are at least 11%. This regulation also sets out the corresponding quality requirements for hybrid schemes to be used for postponement.

Consultation question

205. We asked whether our proposal to limit the use of postponement solely to jobholders who would achieve active membership of a qualifying scheme beyond the postponement period provided sufficient protection for short-term workers. We also wanted to know whether there were circumstances where short-term workers could still miss out on pension saving due to postponement, and if so, how these could be addressed.

Stakeholder response to consultation

206. This issue attracted a substantial response, and stakeholders' **views were strongly polarised**.

207. Employee representative bodies **strongly supported the intention** to protect the rights of short-term workers and ensure they don't miss out on pension saving. That said, many stakeholders felt that employers would be able to find other ways to evade the duties, and that the amendment would thus fail to meet the policy intent.

208. Stakeholders across the spectrum of representative groups (including employers) highlighted **concerns that the proposed amendment to the regulation would not necessarily succeed in its intent**. Whilst it would in theory ensure individuals could access pension provision, in reality employers could still avoid the duties by manipulating their employment practices. For example, stakeholders suggested that **employers could use serial postponement to avoid the duties** through issuing repeated short-term contracts to individuals; alternatively they could dismiss workers within the postponement period to avoid contributions.

209. Large employer and industry representatives **very strongly opposed the amendment** disallowing postponement for short-term workers, on a number of grounds. Several stakeholders felt that the amendment was **going against the policy intent of the original provisions** under the Act, since at that time postponement was seen as an explicit provision for employers with high quality schemes to avoid the volumes of administration for high-churn workers.

210. **Administrative burdens for employers** were commonly mentioned, with this seen as being disproportionate to the benefit provided to workers. Some stakeholders felt that the requirement to enrol short-term workers would lead many employers to level down their existing good provision and discourage others from offering contributions above the minimum, thus defeating the original purpose behind postponement, of rewarding employers with high quality schemes. Concerns were also raised about the burden for pension providers in administering large number of small pension pots.

211. Respondents made a couple of **alternative suggestions for amendments** to the postponement policy, which they felt might be more effective. The most common suggestions were to tighten up the regulation further by disallowing postponement for workers on contracts of less than six months, or to protect workers in an entirely different way by preventing repeated postponement of the same individual. A couple of stakeholders suggested allowing

Government response

212. This is a very finely balanced issue, and we are committed to finding the right path between protecting individuals' opportunities to save and creating disproportionate burdens for employers.

213. We are very concerned by the issues raised by stakeholders around the potential use of postponement as a loophole for employers to evade the duties for their whole workforce, and it is clear from respondents' comments that the proposed amendment to regulation 40 cannot prevent this.

214. At the same time, we recognise that our original intention in providing for postponement in the The Actwas always to support existing high-quality provision, and that a key part of this support for employers was around minimising burdens for firms with a high turnover of staff.

215. We therefore propose to remove the amendment to draft regulation 40 (i.e. **return to allowing postponement for workers on contracts of less than three months**) and look for other, more effective ways to prevent employers from exploiting any potential loophole.

216. The most serious risk appears to be the potential to use serial contracts to repeatedly postpone individuals, and of the options suggested by respondents we feel that the best approach is therefore to prevent repeated postponement.

217. We propose amending the regulation to **prevent an employer from postponing any individual who has previously been postponed by that employer within a 12 month period**. This would mean that any individual returning to the same employer to work for a short period of time within the same year (e.g. at Christmas and summer time) would not be postponed each time.

218. We believe that it now offers the right balance between protecting the rights of jobholders and providing support for employers.

Proposals for change: Amendments to the postponement of automatic enrolment regulations

- We propose revising regulation 40 in order to allow postponement for eligible jobholders regardless of contract length, but prevent postponement for any individual who has already been postponed by that employer within the previous 12 months.

(iii) MAXIMISING EXISTING GOOD PROVISION

Certification of defined contribution schemes

Background and policy intent

219. To qualify as an automatic enrolment scheme and be used for other enrolment activities arising from the Act, a defined contribution scheme must require contributions equivalent to eight per cent of qualifying earnings. Qualifying earnings are a band of earnings between £5,035 and £33,540 in 2006/7 terms and includes most components of pay. Many employers calculate their pension contributions on basic pay, which excludes many pay components such as over time, commission and bonuses, etc.

220. Certification was intended to reduce the administrative burden, and to allow employers to continue using their existing schemes and payroll arrangements without having to reconcile occasional and marginal shortfalls in the contributions, resulting from unexpected pay increases during the certification period. Annex A contains the commentary on the draft regulations on which we consulted.

Consultation question

221. We asked for views on the detailed operation of the certification process.

222. In addition, we were interested in views on how we could ensure that sample checking was robust enough and could give a reasonable indication of the extent to which a scheme met the relevant quality requirements.

Stakeholder response to consultation

223. The majority of respondents (employers, pension scheme advisers, pension providers, benefit consultants and employer representatives) who commented on the high level policy said that the **certification process was too prescriptive and needed to be simplified** for it to be of use to employers.

224. For example, one stakeholder suggested that the process set out in the draft regulations would be cumbersome and, therefore, unappealing for employers. In particular, they felt that the requirement to individually test at-risk groups of workers each year in order to prevent repeat failure is deeply unproductive and unhelpful.

225. However, there was **some limited support** for certification with a couple of stakeholders calling it a common-sense approach that will enable employers to continue with their existing schemes.

226. A few put forward suggestions on how we could improve the processes, focusing on sample checks, a substitute for individualised checks, and the structure and level of the shortfall. Both of these are an integral part of the certification process and were designed to minimise the burdens on employers.

227. Some stakeholders **called for greater clarity in the guidance**, particularly on how risk-based sample checking would work in practice and the extent to which employers could use sample checks and still comply with the legislation. Others said that the guidance was overly

prescriptive and employers should decide the detail of any checks, based on the profile of their workforce and their pay and reward arrangements.

228. Commenting on the level and structure of the shortfall, some said that it had been set too low and made too onerous to provide any real easement. Others questioned the concept of an acceptable shortfall altogether, viewing it as undermining the minimum level of workplace pension saving being targeted through the reforms.

229. In addition, a few stakeholders **rejected the certification process entirely**, putting forward alternative proposals such as:

- a scheme level test, rather than the present individualised one which requires each jobholder to receive the minimum contributions set out in the legislation;
- calculating a new minimum level of contributions on the existing pensionable pay definition used by employers; or
- allowing employers to continue with their existing payroll systems for employees who are active scheme members prior to the staged enrolment duty, but calculate the pension contributions for new entrants after that date using qualifying earnings.

Government response

230. We have carefully considered the comments that we received on our proposals for the certification of defined contribution schemes. We do not under-estimate the challenge of developing a business model that does not disadvantage individual savers, but genuinely reduces the administrative burden for employers who calculate their pension contributions on a definition of pensionable earnings different from qualifying earnings.

231. Our analysis of the responses overall suggests that **technical amendments to the existing draft regulations and guidance will not go far enough**, with stakeholders generally viewing the certification process as currently conceived as not meeting the policy intent. In addition, **stakeholders often had diametrically opposed views** about the way the policy needed to be amended, whilst a few stakeholders went so far as to say the process should be rejected entirely and a different solution found.

232. Given this response, we have decided that **it would not be feasible to take forward the current certification process at this time, and neither would a minor adjustment in the policy meet the concerns of the majority of our stakeholders**. We, therefore, need to undertake a fundamental review of the whole process, and we hope to work closely with our stakeholders on this.

Proposal for change: Certification of defined contribution schemes

- We propose to withdraw the regulations and guidance on certification and to consult further with the industry group and other stakeholders to see what can be done to help employers within the scope of the primary legislation.

Defined benefits pension schemes and hybrid pension schemes

Background and policy intent

233. Scheme quality requirements set minimum standards for defined benefits and hybrid pension schemes used to fulfil the new enrolment duties arising under the Act. The scheme quality requirements will ensure that workers in these schemes will generally be saving towards their retirement at least at the minimum level and many will be significantly above this level.

234. A combination of regulations, alongside rules and guidance which we will publish later, will set out the detailed requirements, the schemes to which they apply and how they are to be applied. The requirements for defined benefits and some hybrid schemes are based on a test of overall scheme quality in which the pensions or benefits that a scheme provides are compared against a benchmark.

235. This is referred to as the test scheme standard and applies to non-contracted-out schemes. For other hybrid schemes the quality test requires the payment of minimum contributions and/or a test of over all scheme quality, which may be in some cases modified. Contracted out schemes will qualify on the basis of the existence of a contracting–out certificate, which is taken as evidence that the scheme meets the reference scheme test (the scheme quality test for contracted-out schemes).

What the draft regulations said

The commentary on the draft rules in Annex B, describes common hybrid schemes and the quality requirements that apply where these requirements have been modified, the regulations set out those modifications

236. **Regulation 27 relates to certain schemes providing career average benefits excluded from being qualifying schemes**. To qualify to be used to fulfil an employer's enrolment duties, career average schemes must re-value the earnings on which the pensions of active members are calculated. Schemes that do not provide for any revaluation of accrued benefits are excluded from being qualifying schemes. However, those that provide for discretionary revaluation can qualify provided that the discretion is:

- exercised by the scheme trustees or managers;
- exercised by the scheme trustees or managers only with the employer's consent; or
- is accounted for in the scheme's statement of funding principles or a similar statement of the funding plan where schemes are not required to have a statement of funding principles.

237. **Regulation 28 prescribes further requirements that the test scheme must meet.** The test scheme which serves as a benchmark has certain features set out in section 23 of the Act. These regulations set out additional features, thus the test scheme is one that:

- increases the pensions where a person leaves service before normal pension age, in accordance with the final salary method in section 84(1) of the Pension Schemes Act 1993, and
- increases the pensions in payment, in accordance with section 51 of the Act1995.

238. **Regulation 29 provides for the appropriate age in the test scheme to rise incrementally.** The appropriate age (pension age) in the test scheme has been set at 65. However, this

regulation enables it to increase, over three decades starting from 2024, to age 68 to reflect changes in State Pension Age.

239. **Regulation 30 prescribes the requirements that have to be met in order for a scheme to satisfy the test scheme standard.** The actuary or the employer in specified cases can determine whether their scheme meets the test scheme standard which is the quality requirement for non-contracted-out defined benefits schemes.[4]

240. However, neither the actuary nor the employer can certify the scheme, if the pensions for more than ten per cent of jobholders are not equal or better than those that would be provided under the test scheme.

241. **Regulation 31 defines a number of terms used in the regulations in relation to hybrid schemes** and states that any reference to the "paragraph (a) requirements" or the "paragraph (b) requirements" in the regulations mean the quality requirements for money purchase schemes and those for defined benefits schemes, respectively.

242. Regulation 31 further explains that a relevant rule is one made under the powers in section 24 of the Act. Section 24 sets out the quality requirements for hybrid schemes. Rules made using powers under that section describe certain types of hybrid schemes and state which quality requirements apply and whether they are modified.

243. **Regulation 32 modifies the test scheme standard for money purchase lump sum accruals.** For the purpose of determining whether the scheme satisfies the modified requirements, the comparator (test, scheme) requires:

- annual accruals of at least 16 per cent of qualifying earnings in the last three tax years preceding the end of pensionable service; or

- annual accruals of at least eight per cent of qualifying earnings in the last three tax years preceding the end of pensionable service and annual increases of a minimum of 3.5 per cent over and above price inflation capped at 2.5 per cent until the member attains normal pension age.

244. Regulation 33 **modifies the test scheme standard for final salary lump sum accruals.** For the purpose of determining whether the scheme satisfies the modified requirements, the comparator (test, scheme) provides for "the amount available for the provision of a pension to a member to accrue at an annual rate of at least 16 per cent of average qualifying earnings in the last three tax years preceding the end of pensionable service."

245. Regulation 34 **modifies the different quality requirements, allowing them to be satisfied in aggregate** and applies where any relevant rule specifies a type of hybrid scheme and states that the quality requirements for money purchase schemes and defined benefits schemes can apply with the modifications made by this regulation. The modification enables the money purchase and defined benefits quality requirements to be combined and to be satisfied in aggregate.

246. Where the scheme quality requirements are modified because of this regulation, neither the actuary nor the employer can certify, if the resulting aggregate for more than ten per cent of the members is less than 100 per cent.

[4] Schemes whose members are in employment that is not contracted-out of the State Second Pension Scheme.

Stakeholder response to consultation

247. Career average schemes are a small but important part of the pension landscape. There was broad consensus across respondents to the consultation that **employers should be able to use career average schemes** to fulfil their enrolment duties. However, there were mixed views on how we should accommodate schemes that do not guarantee revaluation in the nexus of qualifying schemes. Some stakeholders suggested that schemes with accruals above the quality threshold should be able to trade these off against revaluation.

248. Many felt that **schemes providing for discretionary revaluation should be capable of qualifying** under the employer duty, if the revaluation is accounted for in the scheme's funding plan. A few stakeholders felt that any discretion to provide for revaluation should be exercisable by the trustees and one notably felt that to qualify, revaluation must be guaranteed. However, a common emerging theme is that employers must have a say in the funding and application of discretionary revaluation.

249. Our **proposal to increase the appropriate age in the test scheme**, incrementally from 65 to 68, to make it easier for employers to review and change the pension ages in their schemes, **was generally welcomed**. Most supported our proposal for a gradual increase very broadly in line with increases to State Pension Age.

250. The majority of stakeholders, with a couple of exceptions, agreed that increases in the appropriate age in the benchmark test scheme should be linked to changes in State Pension Age. A small number favoured the appropriate age in the test scheme being increased with immediate effect to 68. Other respondents argued that it should exactly track increases to State Pension Age.

251. Of those that commented, almost all of our stakeholders said, whilst the full range of known hybrid schemes had been identified and covered, the risk-sharing landscape was ever changing. Thus, regulations should not stifle innovation in this area by being overly prescriptive.

252. On the other, hand, some respondents called for the development of additional benchmarks for career average and hybrid schemes, arguing that the one size fits all final salary model benchmark makes it difficult for employers to self-certify which will lead to actuarial certification and the associated cost.

253. On the specific issue of the proposed alternative test for cash balance schemes, the preferred option was based on an annual lump sum accrual of 16 per cent of qualifying earnings with annual increases of limited price indexation capped at 2.5 per cent.

254. Quite a few respondents felt that in this challenging economic environment a quality test based on annual accruals of eight per cent with annual increases of 3.5 per cent over and above limited price indexation (capped at 2.5 per cent) was a little optimistic. Enabling employers to choose between the two tests should give them the flexibility to pick the one most suitable for their scheme.

255. A significant number of stakeholders would have preferred a longer consultation period to consider in more detail the operation and implications of the proposed quality requirements for employers with hybrid pension schemes. Some also noted that the guidance to assist employers in certifying their defined benefits and hybrid schemes must be further simplified to be of use.

Government response

256. We recognise the significant contribution that employers are making to workplace pension saving and through the reforms want to encourage this to continue.

257. We propose to **enable career average schemes to qualify**, even if they do not guarantee to revalue the earnings on which the pension is calculated, as long as they provide discretionary revaluation of at least limited price indexation capped at 2.5 per cent. However, the **revaluation must be funded for and included in the Statement of Funding Principles**, or funding plan for schemes that do not have to put in place a Statement of Funding Principles.

258. The Statement of Funding Principles **must be agreed between the employer and the trustees** and **based on the advice of the actuary,**. We, therefore, believe that this strikes an appropriate balance between ensuring that employers are involved in any decisions about the funding of discretionary revaluation and providing greater certainty to scheme members so that they are encouraged to make a long term commitment to workplace pension saving.

259. We will **increase the appropriate age in the benchmark test scheme so that it broadly keeps pace with State Pension Age**. We think that the simplest way, which may help employers who self-certify their schemes, is the approach that we set out in the draft regulations. Increases to the appropriate age broadly read across to changes in State Pension Age.

260. **Cash balance schemes will have the choice of a modified form of the test scheme standard** based on:

- annual accruals of a lump sum based on 16 per cent of qualifying earnings and increases of limited price indexation capped at 2.5 per cent. This is based on applying annuity conversion factors to the 1/120th annual pension accruals in the test scheme to express it as a lump sum accrual; or

- annual accruals of a lump sum based on eight per cent of qualifying earnings and increases of 3.5 per cent in real terms (over and above limited price indexation capped at 2.5 per cent).This is broadly based on the recommendation made by the Pensions Commission of the level of pension saving that a median earner with a solid state pension would need to meet their aspired income replacement in retirement.

261. Providing alternative benchmarks will **enable employers to apply a test** of scheme quality that **most closely suits their scheme**.

262. Recent movements in the stock market may make an assumed real return of 3.5 per cent seem unrealistic, today. However, pensions are a long term investment and over the longer term investment returns may improve so that 3.5 per cent over and above inflation might not be seen as overly optimistic. In the short term, employers may well prefer the alternative test based on 16 per cent annual accruals with annual increases capped at 2.5 per cent.

263. We recognise that the risk-sharing landscape is a rapidly changing one. That is why the **technical detail of the quality requirements will be set out in a combination of rules and guidance,** which can be amended more quickly than regulations.

264. Whilst we are publishing the draft rules (commentary in Annex B) alongside the final regulations for completeness we intend to **continue to work closely on these tertiary products with our stakeholders** to ensure we are developing a workable regulatory

framework for qualifying schemes. We will, where appropriate, ask a small group of interested stakeholders to help us improve the clarity of the guidance and rules.

Proposal for change: Defined benefits pension schemes and hybrid pension schemes

Legislation will require:

- discretionary revaluation to be accounted for in a scheme's funding plans.
- enable employers to choose between two alternative modified tests for cash balance schemes.

The guidance for employers and actuaries will:

- be clarified on the certification of career average schemes. In particular how the revaluation of the pensions for those in pensionable service and for those that leave service is to be included in the quality test.
- make it clearer that to meet the quality requirements a scheme does not have to match the test scheme or modified test scheme. For example, it may have its own arrangements for inflation proofing its pensions, which may differ from the test scheme's or the modified version.

The guidance will also address the interaction between the quality requirements and use of longevity factors.

Non-UK schemes

Background and policy intent

265. Some employers may wish to use schemes established outside of the UK as their qualifying scheme (non-UK schemes). Non-UK schemes refer to both those registered within the European Economic Area (EEA) and those registered outside of the EEA. Within the EEA pension schemes are subject to European regulatory requirements whereas non-UK schemes based outside of the EEA are subject to the requirements of the country they are administered in.

266. We aim to minimise burdens on employers by allowing them to continue to use their existing provision where possible, and therefore we want as broad a range of schemes as possible to qualify. This will also allow individuals already in a non-UK scheme to continue with their existing provision.

267. We consulted on the basis that schemes meeting UK scheme requirements, plus additional criteria to bring them into line with what is expected of UK schemes, should be qualifying and can be used for automatic enrolment. In the draft regulations non-UK schemes were also required to provide the minimum eight per cent of contributions whether or not they are eligible for UK tax relief.

268. In the consultation document, we discussed the issuing of guidance on the use of non-UK schemes for automatic enrolment and when it will, or will not, be appropriate for an employer to use these schemes. There was also an option to amend the regulations in the future to

exclude non-EEA schemes from automatic enrolment if evidence suggested that an unacceptable risk was emerging.

What the draft regulations said

269. Regulation 36 sets out that non-UK money purchase schemes, defined benefits schemes and hybrid schemes must meet the quality requirements of the corresponding UK scheme, bar having their main administration in the UK.

270. Regulation 37 sets out that, unless the Migrant Workers Directive is applicable, non-UK personal pension schemes must meet quality requirements similar to UK schemes; these are broadly:

- all the benefits provided to the jobholder are money purchase benefits; and
- the jobholder must receive a minimum of eight per cent contributions, including a minimum of three per cent contributions by the employer, or be a scheme where the Migrant Workers' Directive applies.

271. Regulation 38 sets out the additional requirements, which are:

- in the country where the scheme has its main administration there must be a regulatory body which regulates that scheme;
- at least 70 per cent of the jobholder benefits will provide an income for life and should not be paid before retirement age; and
- UK tax relief is given in respect of contributions paid by an individual or the employer's contribution includes an additional amount representing the value of any tax relief, which would have been applicable if the scheme was registered.

Consultation questions

272. We welcomed views on the extent to which non-UK pension schemes would be able to participate as qualifying schemes for the purposes of the Act.

273. We asked whether the provisions of regulation 38 (prescribed requirements for non-UK qualifying schemes) provide adequate protection for individuals being automatically enrolled into non-UK schemes and what other safeguards might help. We also asked whether draft guidance on the use of non-UK schemes would be helpful and if so what its scope should be.

274. We welcomed views on only allowing schemes to qualify if they are eligible for a form of UK tax relief, meaning that in most cases non-UK schemes could only be qualifying rather than automatic enrolment schemes.

275. Finally we asked how we could ensure jobholders receive the full amount of total contributions if they do not qualify for UK tax relief.

Stakeholder response to consultation

276. Stakeholders had split views on two aspects of the policy. Firstly, there were **a range of views on the extent to which non-UK schemes would be able to participate as qualifying schemes**. Some stakeholders saw the provision of non-UK schemes as being necessary whereas others felt that non-UK schemes would be undesirable and, based on

current practice, were not likely to be part of the target market. Other stakeholders welcomed the inclusion of non-UK schemes as long as it could be ensured that they provided equivalent benefits to UK schemes.

277. Secondly, stakeholders also had **split views on whether the current draft regulatory provisions provided adequate protection for individuals being automatically enrolled into non-UK schemes**. Some stakeholders felt that the current provisions seemed appropriate whereas others felt that our safeguards were unsuitable as different countries apply different standards. Others said that current provisions were appropriate as long as the protections given to members were equivalent to those in UK schemes.

278. Stakeholders also commented that the current **requirement that these schemes must provide an income in retirement excluded pension schemes from a significant number of countries**. Specific examples of Gibraltar and American 401K schemes were cited as schemes that would not qualify.

279. Only allowing schemes to qualify if they are eligible for a form of UK tax relief was generally seen as unnecessary and there was broad agreement with the policy consulted upon that if there was a shortfall because a scheme does not qualify for UK tax relief, it should be made up by the employer.

Government response

280. Stakeholders' views on our original position demonstrate broad concern over the appropriate regulation of non-UK schemes. Automatic enrolment schemes do not require the individual to make an active choice to be enrolled into a scheme whereas qualifying schemes do. We have therefore **adjusted the policy to allow all non-UK schemes to be qualifying schemes but only EEA schemes**, which are subject to the same European regulatory requirements as UK schemes, **to be used for automatic enrolment**.

281. This addresses most of the concerns regarding the regulation and governance of these schemes. An individual in a non-EEA scheme, under the employer duty would have had: to already be a member of that scheme when the employer duty fell; and to have actively chosen to join the scheme (which in most cases would mean the individual had entered the scheme before they came to the UK). In addition, their employer would have to be content to pay their contributions into that scheme.

282. Although this change in policy has more limitations for certain individuals it does continue to maximise existing good provision, as it may prevent individuals with existing provision from having to be automatically enrolled into a UK scheme. It also limits compliance issues, which should help to ensure that savers are enrolled into secure workplace pension arrangements, supported by a robust regulatory regime.

283. As this proposal **removes the risks associated with the automatic enrolment of individuals into non-EEA schemes,** guidance on the use of non-UK schemes for automatic enrolment should no longer be necessary.

284. Stakeholders also agreed that the current provision for an 'income in retirement' would prevent some schemes from qualifying at all. Given this, we will **relax the 'income in retirement' provision** so that schemes which do not require annuitisation and may enable benefits to be taken before the age of 55, can qualify. This relaxation would apply only **to qualifying schemes (EEA and non-EEA),** not for schemes eligible for automatic enrolment (EEA only).

285. This means **more good quality non-UK schemes will be allowed to qualify** without leaving individuals inadequately protected, and schemes in countries such as America, Canada, Australia and New Zealand will be able to qualify, which previously would have not been able to do so.

286. The original 'income in retirement' provision will remain for automatic enrolment schemes, meaning only individuals who have actively chosen to join a qualifying non-UK scheme will be affected. It is our view that this strikes a good balance between stakeholder views on maximising existing provision, allowing good non-UK schemes to qualify and providing adequate protection for savers.

Proposals for change: Non-UK schemes

Our proposals are:

- To adjust policy to allow all non-UK schemes to be *qualifying* schemes but only European Economic Area (EEA) schemes, which are subject to European regulatory requirements, to be used for automatic enrolment.

- To relax the 'income in retirement' provision for qualifying schemes (EEA and non-EEA), not for schemes eligible for automatic enrolment (EEA only).

(iv) EMPLOYER COMPLIANCE

Registration

Background and policy intent

287. Registration is critical to ensuring employer compliance. Registration information is needed because there are no existing sources that allow employer data to be linked to pension data in a timely and reliable manner. Registration will be used to detect early non-compliance and establish, from the outset, a culture of compliance and a level playing field amongst employers.

288. TPR will inform employers about their duty to register at the same time they are told about auto-enrolment. TPR will then be able to make ongoing checks of registration data against HMRC data on PAYE schemes and with employers' chosen pension schemes where possible.

289. Re-registration every three years will ensure that TPR has up-to-date information and can continue to operate an effective compliance regime.

What the draft regulations said

290. Regulation 3 sets out that employers have up to nine weeks to register after their staging date and that following implementation, new employers will have three months to register after PAYE income is first payable to any worker.

291. Regulation 3 requires employers to register in respect of each relevant PAYE scheme and provide information including the employers' identifying/contact details, pension scheme details, numbers of workers automatically enrolled into the scheme, number of opt ins and opt-outs and the number of workers not saving and reasons for not doing so.

292. Regulation 4 requires all employers to re-register every three years and provide employer contact and scheme details, updated information on the numbers of employees re-enrolled and of those that are already saving.

Consultation questions

293. We asked respondents whether:

- the proposed regulations achieve the right balance between minimising additional burden for the employer and enabling TPR to check compliance effectively;
- any of the information included was irrelevant;
- the nine week and three month registration windows for new businesses provided sufficient time for the employer to complete registration; and
- it was reasonable to ask employers to re-register every three years.

Stakeholder response to consultation

294. Most stakeholders seem to support the principle of registration, but had some questions about the details.

Information requirements

295. There was widespread concern regarding the **administrative burden** of the registration process. Several stakeholders were concerned that registration could be complicated for those employers with multiple PAYE schemes and that those employers with an in-house occupation scheme would be duplicating the information provided as part of TPR's existing occupational scheme returns.

296. Although there was a general consensus that the **employer and scheme information requirements were necessary** to ensure compliance, concern was expressed about the **burden and complexity of worker information requirements**.

297. There were suggestions that the information would quickly become out-of-date and that, with tight deadlines, employers may not have sufficient time to complete the process or may guess the required information. This was linked to concerns that employers who find registration difficult will be penalised.

298. Several stakeholders felt that the information requested was to collect statistics rather than to facilitate a risk-based approach to compliance. One stakeholder expressed concern that registration information would not allow TPR to identify non-compliance by employment agencies.

299. To ease the potential for excessive burden, stakeholders said that registration should be possible both online and on paper, and that there should be greater tie-in with HMRC processes. Several respondents pointed out that the registration process will need to have sufficient flexibility for employers operating more than one pension scheme. Stakeholders also wanted to be forewarned of registration requirements as soon as possible and stressed that guidance should be made available and user testing be undertaken.

Registration deadline at implementation

300. The proposed **registration deadline** of nine weeks was considered by many respondents to be **impractically short**. A key reason was the **time required to collate opt out information**, with some stakeholders noting the challenges of larger workforces and multiple sites. A three month deadline was proposed by many stakeholders to allow successful interaction with opt out information and match the monthly cycle of the joining and opting out windows.

301. There was widespread consensus that the three-month **registration deadline for new employers is workable**. However, it was emphasised that new employers should not be penalised for not registering if they have applied for but not yet received their PAYE scheme number.

Re-registration process

302. Re-registration was a less contentious issue, with the majority of stakeholders agreeing that **re-registering every three years is reasonable** as long as there are adequate reminders and the process is streamlined as much as possible. It was suggested that re-registration should be risk-based and not be required of employers with a strong record of compliance.

Government response

303. In light of the consultation responses several amendments have been made to the registration and re-registration process to mitigate stakeholder concerns.

Information requirements

304. We agree that for some employers the registration process that was proposed may have proven burdensome, and have revisited the information requirements, focussing on reducing them to the absolute minimum information that TPR will need to check compliance. In light of stakeholder concerns we have **removed the requirement to provide information on the numbers of opt-outs and voluntary joiners** (opt-in and workers requesting to join).

305. We now propose that employers need only tell TPR how many workers have had their automatic enrolment delayed (under section 4 or section 30 of the Act) and the remaining number in the PAYE scheme not enrolled. Separated numbers for employees outside the age and earning bands will no longer be required.

306. To ensure that registration is sufficiently flexible for employers operating more than one pension scheme, we have clarified that employers will need to specify the number of new and existing members saving in each scheme.

307. From the scheme information section we have **removed the requirement on employers to tell TPR whether their scheme meets the requirements for delayed automatic enrolment**. We have also simplified the scheme details so that the same basic information is required from all employers. These are the scheme name, employer pension scheme reference and scheme address (if not already held by TPR).

308. We consider that with these modifications the administrative effort of registration will be significantly reduced.

309. TPR will respond to failure to register as part of its risk-based, graduated and proportionate approach to enforcement. TPR will consult with interested stakeholders and publish its enforcement strategy later this year.

310. We are reluctant to introduce a new field requiring employers to identify whether they are an employment agency, but TPR intends to work closely with interested stakeholders and explore other ways that it can obtain information that will help it to detect risk in this sector. While it is not possible to integrate registration into HMRC processes more closely at this stage, we will continue to keep under review the possibility of doing so in future.

311. The points about communication and registration format raised by stakeholders are already part of TPR's plans for its compliance approach.

Registration deadline at implementation

312. Many stakeholders commented that the registration deadline of nine weeks was unrealistic due to the length of time required to collate opt out information. The **removal of the requirement to provide opt out numbers has facilitated a more workable deadline** for initial registration. During implementation and at re-registration employers will now have two months to register from their staging date or re-enrolment date (and a full month following the close of the joining window). This two month deadline will enable TPR to follow up on non-compliant employers quickly before unpaid contributions begin to build up.

313. In line with TPR's risk-based approach to enforcement, procedural obstacles, such as not yet having a PAYE number, will be taken into account in making risk-based decisions to pursue enforcement activity.

Re- registration process

314. The **information required at re-registration will be reduced** in the same manner as that required at registration. In addition, TPR's intention is that re-registration forms will be pre-filled wherever possible so that employers will only need to update their employer scheme details if they have changed. TPR also intends to explore where changes to occupational scheme returns may be made to reduce duplication.

315. We consider that three yearly re-registration will be key to ensuring a continued culture of compliance and a level playing field amongst employers.

Proposals for change: Registration

We propose the following changes to simplify registration and ensure that employers are able to meet their registration deadlines:

- remove the requirement to provide information on the numbers of opt outs and voluntary joiners.
- significantly simplify the requirement for employers to provide information on why employees have not been automatically enrolled.
- remove the requirement for employers to tell TPR whether their scheme meets the requirements for delayed automatic enrolment.
- require registration within two months of the automatic enrolment date during implementation and the re-enrolment date, giving employers at least one month to collate information after the close of the joining window.
- reduce the information required at re-registration in the same manner as that required at registration.

Record-keeping

Background and policy intent

316. Employers, trustees of occupational pension schemes and personal pension providers will be required to keep certain specified records to enable TPR to check employer compliance at a detailed level. These requirements are set out in regulations to ensure that employers can demonstrate their compliance with the employer duty.

317. It is anticipated that many of the records specified in these regulations will already be retained for other purposes. Our intention has been to keep new record-keeping requirements to a necessary minimum.

318. The regulations do not stipulate the format in which records must be kept: employers, trustees and providers are free to use paper or electronic formats.

What the draft regulations said

319. Regulation 6 will require employers to retain records which relate to the scheme or schemes they use to satisfy the employer duty, the enrolment process (whether automatic, as in the case of eligible jobholders, or on a voluntary 'opt in' basis), the processing of opt out forms and calculation and payment of contributions.

320. Regulation 7 will require trustees and managers of occupational pension schemes, and pension providers, to keep membership records, including records of jobholders who opt out, in order to assist TPR in monitoring overall enrolment and opt out activity, identifying trends and investigating possible employer duty and inducements breaches.

321. Regulation 8 sets out the retention periods for records. Most records will be kept for a maximum of six years, but the requirement on employers to carry out automatic re-enrolment allows us to specify a shorter retention period of four years for opt out records. Existing rules governing disposal of records when companies wind up will not be affected.

Consultation question

322. We asked respondents whether they were broadly content with the record-keeping requirements, and whether they considered that certain records need not be kept or be included. Respondents were also asked whether they foresaw any particular difficulties in meeting the requirements for certain types of employers or schemes, and whether they felt it reasonable to expect schemes to keep records of opt outs.

Stakeholder response to consultation

323. Respondents broadly agreed that **a requirement to keep certain specified records would be necessary** to support an effective compliance regime: there was little support for the view that it should be left to employers to decide which records they should enter.

324. It was generally felt that the requirements could well turn out to be **burdensome** in practice, particularly for small employers, though larger employers and employers who were already running pension schemes would adapt more easily.

325. Employer representative organisations raised various queries relating to the technical operation of the record-keeping requirements, including the **possible duplication of records**. They were concerned about the implied need for both employers who operate in-house occupational pension schemes and the schemes themselves to keep duplicate records, and the possibility that employers and occupational pension schemes who carry out administrative work on each other's behalf, or who use third-party administrators, might fail to meet the requirements. They also asked for clarification on how the requirements would fall on former trustees of occupational pension schemes.

326. Respondents felt that, while it made sense for the **retention periods** for contribution records **to be in line with existing HMRC requirements**, the retention periods for opt out records were inconsistent with TPR's proposed 'look back' period for investigating possible cases of coercion or inducement, which was proposed to be twelve months. They suggested that the retention period and the 'look back' period should be harmonised.

327. Respondents felt strongly that occupational pension **schemes and pension providers should not be required to keep records relating to the opt out process**. They consistently expressed the view that since the operation of the opt out process was part of the 'employer duty', and employers were already required to keep copies of opt out forms, TPR should look

Government response

328. Employers will already keep many of the records for other purposes. We are requiring records to be retained, rather than documents (although in the cases of certain certificates relating to contracting out, we specify that the record must be a copy of those certificates and it will be easier for an employer to keep a copy of opt out and opt in notices). We are also allowing employers, occupational pension schemes and pension providers to **choose the storage format which best suits their business needs**. We believe that these measures will do much to **reduce the financial and administrative burdens** of record-keeping.

329. On possible duplication of records, **employers, trustees and providers need not personally hold the prescribed records**; they may for instance delegate administrative functions to third party administrators and other providers of services. These regulations are not intended to interfere with such existing practices. However, the legal responsibility for ensuring that the records are kept and produced to TPR on request will rest with the employer, trustee or provider.

330. For this reason, employers who operate in-house occupational pension schemes and the schemes themselves **will not have to keep the same records twice**. It will be acceptable for an employer to keep records on behalf of the scheme or vice versa, provided that either party has access to the records in question and can provide them to TPR if required.

331. We do not intend to require individuals to keep records after they cease to act as an employer, trustee or pension provider, provided that a person who ceases to act in any of those capacities transfers any records they are holding to their successor. If TPR discovers in the course of an investigation that a former trustee or employer failed to create or keep a prescribed record, it will be open to TPR to hold that person responsible for the breach.

332. Trustees and providers will recognise that the requirement to retain records for six years for the purposes of these regulations does not override any requirement that there may be on them to keep those same records for periods longer than six years in connection with the discharge of their fiduciary duties or their contractual obligations towards savers. [5]

333. In response to stakeholders' suggestions, we have **aligned the retention period for opt out records with TPR's 'look back' power** to investigate allegations of inducement, both periods will be four years.

334. While we recognise the strength of opposition to the requirement on occupational pension schemes and pension providers to keep records of opt outs, we nevertheless believe that TPR's ability to identify underlying trends in enrolment and opt out volumes will be significantly hampered if this requirement is removed completely.

335. However, we propose to remove the requirement to keep the full record of personal information provided by the employer at the time of automatic enrolment. Schemes and providers will now be **required to keep only the name of each jobholder who opted out** of scheme membership **and a record of the date** on which they opted out.

[5] Guidance covering the broader record-keeping requirement on trustees is available from TPR at http://www.thepensionsregulator.gov.uk/pdf/RecordKeepingPDF.pdf

336. No other opt out records need be kept. TPR plans to discuss this requirement further with schemes and providers during the coming months.

Proposals for change: Record-keeping

- Occupational pension schemes and pension providers will be required to keep, in respect of those who opt out of scheme membership, a record of the name of each jobholder who opted out and a record of the date on which the employer informed the scheme that the jobholder had opted out. The requirement to keep the full record of personal information provided by the employer has been removed and no other opt out records need be kept.

Ensuring payment of all contributions due – Due date

Background and policy intent

337. The Act allows TPR to issue an unpaid contributions notice (UCN) to an employer in response to a report from a pension scheme that they have failed to pay the required contributions on time.

338. To be able to issue a UCN TPR must be "of the opinion" that the contributions have not been paid on time. This depends on knowing exactly what that deadline was. However, at present not all scheme reports to TPR include this date – many just state the month.

339. We proposed prescribing a due date which, in effect, allows TPR to assume a particular date in the month without having to seek further information from schemes. This would minimise burdens on schemes and help TPR to manage the anticipated high volumes of such cases post 2012. If stakeholders supported changes to the 19 day rule for the period during which a worker is being automatically enrolled, we said we would consider amending this due date accordingly.

340. This due date would be merely for the purposes of issuing the UCN. It would not affect regulations around pay reference periods, annual reconciliation and certification, nor affect other properties of the scheme agreement, such as the level of contributions. Schemes would not be obliged to make any changes to schedules as a result.

What the draft regulations said

341. Regulation 9 sets a due date for all unpaid contributions (including employer and worker) of the 19th day of the month following the month the worker contributions were deducted or when employer contributions were due.

342. This regulation also provides that for occupational defined benefit schemes and certain hybrid schemes the due date will be whatever the due date is under their schedule of contributions. For those hybrid schemes, this will apply to the defined benefit element of the scheme whilst the defined contribution part will be subject to the proposed 19th day due date.

Consultation Question

343. We asked whether there were any other categories of schemes, which typically might have longer employer due dates in their schedules.

Stakeholder response to consultation

344. Of those who commented **no specific objections were received** to the proposed due date, and no other categories of schemes which typically have longer employer due dates in their schedules were identified. A small number indicated some misunderstanding around what we have prescribed here, thinking we have also prescribed the proposed 19th day due date for defined benefit schemes. That is not the case.

Government response

345. As stated in the consultation document, the exception to the proposed 19th day due date for occupational defined benefit schemes means that the due date for these schemes will be whatever the due date is on their schedule of contributions. We will not be altering existing legislation that governs schedules of contributions (and payment schedules). Schemes will not be obliged to make any changes as a result.

346. We gave a commitment in the consultation document to consider amending the due date in regulation 9 to align with any change to the existing 19 day rule, which was also under consultation.

347. Given the proposed changes to the 19 day rule (section V on Minimising Refunds), we will align the due date regulation accordingly.

Proposal for change: Due date

- We propose making a small amendment to the due date in regulation 9 in relation to contributions deducted between the automatic enrolment date, the automatic re-enrolment date or the enrolment date and the end of the opt out period. For these, the due date would be the last day of the second month following the month in which automatic enrolment occurs. We are proposing that these due date provisions will be included as part of the package of regulations that change the existing 19 day rule.

Ensuring payment of all contributions due - Unpaid relevant contributions

Background and policy intent

348. The Act provides a way to address the potential disadvantage to workers from their employer's wilful failure to comply, where this leads to the build up of a large backlog of worker contributions.

349. TPR will have the ability to consider requiring employers (in an unpaid contributions notice or a compliance notice) to pay their own and the worker's contributions themselves where:

- contributions are overdue; or

- the employer duties or the inducements provision have been breached and backdated contributions are required to put the worker back in the position they should have been in.

The Act requires that for this requirement to be available to TPR the "prescribed period" has to have expired.

350. When prescribing the length of the period we want to achieve the right balance of protection for the worker with a proportionate impact on an employer. We want to ensure that for workers the period is reasonable from the point of view of choosing to make good missing contributions or taking a very small loss in the value of the fund.

351. We also want to be fair to employers, giving them sufficient time to sort out any problems with processes before being liable to potentially being asked by TPR to pay both sets of contributions on their own account.

What the draft regulations said

352. Regulation 10 provides for the length of the prescribed period to be three months, after which TPR can consider requiring an employer to pay both employer and worker unpaid or backdated contributions on the employer's own account.

Consultation question

353. We asked whether limiting in this way TPR's ability to use this specific discretionary power struck the right balance between protecting the savings of individuals and not having a disproportionate impact on employers.

Stakeholder response to consultation

354. There was active support among the vast majority of respondents for the three month period. Stakeholders generally felt that **a period of three months struck the right balance from both the worker and employer perspective**, but a small number felt a greater understanding was needed about how TPR would use this discretionary power.

355. A couple of respondents expressed concerns about a three month prescribed period. They felt it was too short and had reservations about TPR having the power to send out notices requiring employers to pay both sets of contributions early in the compliance process, risking catching the bewildered rather than wilfully non-compliant. Particular concerns were expressed about this during staging but not so much after the implementation stage.

356. A few respondents commented that having a three month prescribed period must not be seen as a grace period for paying contributions and extinguish the requirement to pay these on time.

Government response

357. The vast majority of responses endorse our proposition that a period of three months does strike the right balance between operational viability (thereby maximising compliance activity), protection for individuals and the bewildered employer, and a proportionate effect on employers.

358. In response to those few stakeholders who are concerned that three months is too short, we did consider a longer prescribed period of up to six months but concluded that there were too many disadvantages for this to be a feasible option. A period rising towards six months has serious implications for gaps in workers' pension savings that may not be able to be made good by them, including the possibility of some of them opting out completely, and lessens the impact of the compliance regime.

359. TPR will take a risk-based, graduated and proportionate approach to enforcement. TPR will consult with interested stakeholders and publish its enforcement strategy later this year.

360. This provision is not intended to allow for a period of grace for an employer to pay over contributions or extinguish the requirement to pay them when due. In fact, we see it as a way of encouraging employer compliance with paying contributions on time, with a suitable measure of protection for a worker where this does not happen.

Ensuring payment of all contributions due - Requirement to pay interest

Background and policy intent

361. The Act gives TPR the discretion to ask an employer to pay interest when requiring them to pay outstanding contributions, which is intended to help compensate the individual for any investment growth loss suffered.

What the draft regulations said

362. Regulation 11 provides for interest to be calculated by the employer on a simple per annum basis at 4.9% plus RPI. Where a notice is issued prior to the publication of RPI in any given month, the RPI published in the previous month will apply.

363. The regulation also provides for the start and end of the period over which interest is to be paid which, for an unpaid contributions notice, begins with the due date prescribed in regulation 9, and ends when the outstanding amount has been paid. For a compliance notice, interest will be charged on the amount of outstanding contributions from a trigger date specified in the notice, which could be the original date of the breach, ending when the employer complies.

Consultation question

364. We asked whether this measure of interest provided a fair and appropriate level of restitution or if there was a better approach.

Stakeholder response to consultation

365. Of those who commented, just under **a third supported our proposal**, but a **similar proportion thought it was too high** or apparently penal, or too complex. The others **suggested alternative models** including a number of options we had considered prior to the consultation:

- calculating the exact loss for the fund concerned;
- using a simple flat rate of five per cent, eight per cent or ten per cent;
- tracking the Bank of England or other base rate;
- placing a floor on the Retail Prices Index (RPI) to account for negative RPI; and
- reducing the 4.9% fixed element to reflect the likelihood that pension funds (especially from 2012) are unlikely to invest 100% in equities.

366. One respondent pointed out that we need to clarify in the regulations the exact measure of RPI we intend to be used in calculating the amount of interest on unpaid contributions.

367. A few stakeholders asked for clarity as to how any interest paid is to be treated in terms of a contribution and for tax purposes including the annual contribution limit.

Government response

368. The wide-ranging and varied responses suggest that there is **no obvious alternative agreed method to arrive at an interest rate** that accurately and easily replicates lost investment growth. We reviewed the case for the leading alternative models suggested, but concluded that their drawbacks were too serious:

- to calculate the exact loss suffered is operationally impractical for TPR to achieve.
- a single flat rate, whilst simple, is arbitrary and does not future-proof the regulations against changing economic conditions.
- the Bank of England rate is more a macroeconomic tool than an index, and interest reflects how far the Bank is from its inflation target, not likely pension scheme performance.

369. We also considered placing a floor on the value of the retail price index so as to ensure the actual rate will not go below the 4.9%. However, when RPI is negative, the real value of returns is higher. A floor on RPI would in effect give individuals a windfall, which is not the policy intent. If the total rate fell below 0%, TPR could simply not apply interest.

370. We agree that the process for calculating interest should be as simple as possible, whilst maintaining the policy intent of the measure. We believe the perceived complexity here arises from the worry that employers will be asked to calculate the amount of interest using a two part formula. However, we can confirm that **TPR will be able to pre-calculate the rate when issuing a notice** so an employer will see a single figure that will include the RPI element.

371. Stakeholders commented that a model of investment return, which assumed 100% investment in equities, was unrealistic. This has helped us refine our thinking. We have done further work that shows the average UK pension scheme has about an 80:20 equity-gilts split investment.[6] The Barclays Equity Gilts Study shows gilts have an average 100-year return of 1.3%. Assuming an 80:20 equity-gilts split, the average return is 4.2%.[7] In recognising this**, we propose reducing the fixed component to 4.2%.** This is consistent with the policy intention to approximate investment loss.

372. Any interest paid by an employer at the request of TPR will be treated as a contribution by the employer to the worker's pension fund. Should the worker be a member of the personal accounts scheme, interest paid in accordance with a Compliance or Unpaid Contribution Notice will not count towards the annual contribution limit if it relates to a contribution due in a previous tax year. An amendment will also be made to the relevant tax legislation to ensure a worker is not liable to an income tax charge on the interest received.

373. Amending regulation 11(2) (b) will make it clear that RPI means the monthly *percentage change* in the general index of retail prices for all items.

[6] Bank of New York Mellon Asset Servicing study of UK Pension Schemes
[7] http://www.barcap.com/egs/

Proposal for change: Requirement to pay interest

- We are proposing a rate of 4.2% + RPI%, with no floor on RPI. We also plan to amend the definition of RPI in regulation 11(2) (b) to refer to the monthly percentage change in the general index of retail prices for all items.

Ensuring payment of all contributions due - Estimating contributions

Background and policy intent

374. TPR will not always know the amount of outstanding contributions from the scheme report and if the employer fails to engage with TPR to calculate the correct amount payable TPR needs a method of estimating how much is payable. The Act therefore allows TPR to estimate the amount of contributions that an employer has failed to pay and the sources of information it may use in estimating the amount of unpaid contributions.

375. This measure will be used where an employer continuously fails to engage with TPR about the amount of contributions owing. Once in enforcement the notices will normally include the requirement to estimate the contribution. The rationale is that an employer should not gain from their refusal to engage.

What the draft regulations said

376. Regulation 12 provides the mechanism by which TPR can estimate the amount of unpaid contributions that an employer has failed to pay. It prescribes the formula to be used by TPR in estimating the amount of unpaid contributions, which translates as:

maximum qualifying earnings divided by 12
x 8 per cent
x number of jobholders affected (or PAYE scheme size where the number of jobholders affected is unavailable)
x number of months late

377. The regulation also allows TPR to estimate contributions owed using certain sources of information additional to information provided by the employer, which are:

- a late payment report;
- anything reported or sent to the Regulator by any person, including trustees and managers of occupational schemes, providers of a personal pension scheme, and pension scheme members; and
- any information disclosed to the Regulator under section 88 of the The Act 2004.

Stakeholder responses to consultation

378. Very **few stakeholders commented** on this regulation. Of those that did, one wanted a lower percentage in the estimated formula until 2017 to account for phasing. Another wanted clarification of what would happen to the excess amount of contributions if the estimated amount is paid.

Government response

379. Ultimately, TPR wants the employer to engage to ensure the correct amount of outstanding contributions is paid when due. If so, employers need never pay the estimated value. We therefore think it is unnecessary to complicate the estimation formula to account for phasing during the early years of the reforms.

380. Should the estimated amount be paid, it will be a matter for the scheme and the employer to consider how to apportion the monies paid.

Penalties and reviews of compliance activity - Fixed penalty notices

Background and policy intent

381. The fixed penalty is intended to get the attention of employers who have failed to engage with the reforms despite the provision of information and support.

382. We proposed a flat-rate fixed penalty of £500 in the belief that this level would be high enough to act as a serious "wake-up call" to employers who have not responded to earlier warnings, but low enough not to excessively affect small businesses. We also knew that a flat-rate penalty would be much easier to administer and communicate to employers than a scaled rate.

What the draft regulations said

383. Regulation 13 prescribes that the penalty where TPR issues a fixed penalty notice is £500.

Consultation questions

384. We asked whether the proposed flat-rate fixed penalty of £500 seemed proportionate.

385. We also asked whether it would be desirable and reasonable to offer a discount on the fixed penalty level for those who pay the penalty promptly and whether such a discount would be likely to increase rates of compliance with the employer duties or only affect compliance with the requirement to pay a penalty.

Stakeholder response to consultation

386. About half of the stakeholders who commented on this issue were **content with both the flat-rate structure and level of this penalty**. They believed it to be appropriate bearing in mind the availability of higher escalating penalties for more serious and persistent non-compliance and the fact that the fixed penalty will be issued, in the vast majority of cases, after several previous warnings.

387. However, about a quarter of respondents expressed **concerns that the flat rate or the level of the penalty could have a disproportionate effect on small businesses**. Some wondered whether the penalty would be seen as a 'price worth paying' by larger employers and recommended scaling it according to the size of the firm.

388. Many were **keen to know more about TPR's enforcement strategy** and the circumstances in which these penalties might be issued. For example, some were concerned that penalties might be issued in response to minor administrative errors. Others wondered how blame would be apportioned between employers and third parties such as trustees or scheme

managers. Some advocated a light-touch approach generally during the early years of the reforms.

389. Very few stakeholders supported the idea of a **discount for prompt payment** of this penalty. Many felt such a discount **would add unnecessary complexity** to the penalty system and that it would not necessarily increase incentives to comply promptly but simply encourage early payment of the penalty itself. There were some concerns that this might actually create perverse incentives for the more unscrupulous employers to delay non-compliance still further while facing a reduced penalty.

390. Two stakeholders expressed a **concern that individuals might be able to take a case to an employment tribunal** rather than report their employer's non-compliance to the Regulator. Furthermore, they would be likely to prefer to take this route because of the possibility of compensation compared with the possibility of their employer receiving a financial penalty which would simply be paid into the Consolidated Fund.

Government response

391. We believe the fixed penalty needs to be simple for its recipients to understand and simple for TPR to apply. We considered the option of scaling this penalty according to the size of the firm by reference to PAYE data, and recognise that scaling might make the penalty a somewhat more effective deterrent for firms. However, we feel that scaling the penalty would make it overly complex and difficult to administer without adding a great deal to its deterrent value.

392. We therefore propose to **keep the flat-rate structure of the fixed penalty**. Scaling the escalating penalties on the other hand is a necessity if those are to deter the most serious and persistently non-compliant employers. We do not anticipate escalating penalties will need to be issued nearly as frequently as the fixed penalty and feel the extra complexity in terms of administration and communications is justified in that context.

393. However, we acknowledge the concerns raised about the level of the penalty and its potential to impact heavily on small firms. In response, we propose to **reduce the level of the fixed penalty to £400**. We estimate that this is just above the level required to cover the costs of administering and recovering the penalty. We believe this level will still have a significant deterrent effect.

394. TPR will take a, risk-based, graduated and proportionate approach to enforcement. **TPR will consult with interested stakeholders and publish its enforcement strategy later this year**. The possible use of publicity about successful enforcement action, which we anticipate might be an effective deterrent for some firms, will be included in that strategy.

395. With regard to the concern that TPR might not be the preferred route to redress for workers whose employers have failed to comply with their duties we can confirm that there is no choice on this matter. Our legislation makes clear that contravention of any of the new employer duties does not give rise to a right of action for breach of statutory duty.

396. Furthermore, whilst the duties are supplemented by two individual *rights* enforceable before an employment tribunal there is **no mechanism by which the *duties***, which are enforceable by TPR, **can also be enforceable in the same respect by an employment tribunal**. For example, there is no individual right to be auto-enrolled into a qualifying pension scheme saving which could give rise to an ability to take a case to an employment tribunal.

397. The route that is open to individuals where they believe there has been a breach of the new employer duties is for them to make a complaint to TPR who will be able to consider

investigation of the alleged breach and if appropriate take compliance action against the employer. The only new individual rights, enforceable before an employment tribunal, created in the Act are rights not to suffer detriment or unfair dismissal on grounds related to the new employer duties.

398. Any penalties recovered (after the issue of penalties by TPR) must, following standard regulatory practice, be paid into the Consolidated Fund rather than to the workers who may have suffered from the non-compliance. The aim of these penalties is to deter employers from such non-compliance and in some circumstances ultimately to force them to comply with Notices which may require them to make back payments of unpaid contributions for their workers. This is entirely different from the compensatory powers available to an employment tribunal when a claim is presented to it.

399. Given the lack of support for the idea, we **do not intend to provide for a prompt payment discount**.

Proposal for change: Fixed penalty notices

- We propose to reduce the level of the flat rate fixed penalty from £500 to £400.

Penalties and reviews of compliance activity - Escalating penalty notices

Background and policy intent

400. Escalating penalties are intended to address entrenched employer behaviour by providing a meaningful deterrent to the most serious or persistent non-compliance. We proposed a system of escalating penalties with proposed penalty levels calculated by estimating the total amounts of unpaid contributions that a non-compliant employer could owe over a two-year period.

401. Our approach was to scale escalating penalties, to vary by employer size and aim to address the financial advantages of non-compliance. In most cases this will be estimated using PAYE data. Where the penalty is in respect of a failure to comply with an Unpaid Contributions Notice, the exact number of people affected will be used when known by TPR because it is provided by a pension scheme. We do not propose to scale escalating penalties in the context of third party non-compliance. There would appear to be no meaningful way to do this according to the number of people affected and not every third party will have a PAYE scheme.

What the draft regulations said

402. Regulation 14 prescribes the structure and levels of the escalating penalty.

403. It prescribes a £200 per day penalty when an escalating penalty notice is issued to someone other than the employer of the affected person, i.e. a “third party”.

404. And it prescribes daily rates of escalating penalties as shown in the table below to apply in respect of employer non-compliance.

Size of PAYE scheme	**Penalty**
1 - 4 workers:	**£50** per day
5 - 49 workers:	**£500** per day
50 - 249 workers:	**£2,500** per day
250 - 499 workers:	**£5,000** per day
500+ workers:	**£10,000** per day

Stakeholder responses to consultation

405. The **majority of stakeholders did not comment** on the proposed structure and level of escalating penalties. Some stakeholders expressed support for them while others were concerned that the level of escalating penalties are potentially very high and queried whether this was appropriate and reasonable.

406. **Reassurance was sought** that these penalties would **only be used for the most serious and persistent non-compliance**. Some stakeholders were also concerned that scaling the penalties by reference to a firm's PAYE scheme size could have a disproportionate effect on firms who have a large payroll, particularly on those whose non-compliance might only have affected a small percentage of their workforce.

Government response

407. Escalating daily penalties are intended to act as an effective deterrent for the most entrenched non-compliance and as a lever to force the payment of outstanding contributions. To do that, the penalty levels have been carefully calculated by reference to the amounts of money a non-compliant employer might stand to gain in terms of unpaid contributions.

408. By their very nature, **escalating penalties will not be issued from 'day one' of non-compliance,** but only after only a series of contacts from TPR in the form of warnings. Therefore, the level of the escalating penalty needs to take this initial period of non-compliance into account as well as the continuing non-compliance.

409. The intention is for the amount of the penalties to at least equal the financial advantage of non-compliance within two years. Our calculations build in an estimate of the number of people affected as far as possible given the information that TPR will have. In relation to Unpaid Contributions Notices, this will often be the exact number of people affected as reported by the scheme. For Compliance Notices, firm size as approximated by PAYE scheme size will be the only reliable source available.

410. We fully appreciate that the vast majority of employers will not deliberately fail to comply with their duties to such an extent and **we only anticipate escalating penalties to be necessary in rare cases. TPR will consult with interested stakeholders and publish its enforcement strategy in 2010.**

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Penalties and reviews of compliance activity - Prohibited recruitment conduct penalties

Background and policy intent

411. This prohibition on certain forms of recruitment conduct is designed to deter employers from trying to screen out of the recruitment process any job applicants who might want to save in a qualifying workplace pension. TPR have a separate power to issue a fixed penalty notice where it believes an employer has contravened this measure.

412. We proposed fixed penalties that vary by employer size and are higher than the other fixed penalties for non-compliance. This reflects the fact that employers who deliberately contravene this measure are in effect trying to avoid all of their duties under the reforms, and that escalating penalties cannot be applied for prohibited recruitment conduct.

What the draft regulations said

413. Regulation 15 prescribed the structure and levels of the penalty applicable for prohibited recruitment conduct, i.e. where an employer has attempted to screen out job applicants who might want to save in a workplace pension scheme.

414. The penalty is to be determined according to the size of the employer's PAYE scheme as shown in the table below.

Size of PAYE scheme	**Penalty**
1 - 4 workers:	**£1,000**
5 - 49 workers:	**£1,500**
50 - 249 workers:	**£2,500**
250+ workers:	**£5,000**

Stakeholder response to consultation

415. **Very few stakeholders commented** on the proposed penalties for prohibited recruitment conduct. Those who did were primarily **interested in getting further clarity** on the sorts of behaviour which might be considered to constitute prohibited recruitment conduct and the ways in which TPR might enforce the measure. Without that clarity they either felt unable to comment on the levels proposed or felt the amounts involved were too high.

Government response

416. This prohibition is designed to deter employers from trying to avoid their new duties from the start by screening out of the recruitment process those job applicants who might want to save in a qualifying workplace pension.

417. The fixed penalties levels reflect the gravity of such employer non-compliance and the fact that escalating penalties cannot be applied for prohibited recruitment conduct. We proposed penalties that are scaled according to firm size because we think it right that larger businesses which are more likely to have access to professional advice on correct recruitment behaviour should face higher fines if they contravene this measure.

418. During 2010, **TPR intend to issue initial guidance for employers and their adviser intermediaries** on the employer duties and what might constitute prohibited recruitment

conduct but, in brief, the sorts of behaviours we anticipate might contravene this measure include:

- advertising a vacancy on the basis of it only being available to those prepared to opt out; or
- asking prospective employees questions at interview, or in the pre-selection stage, about whether or not they intend to opt out; or
- making statements at interview which might suggest to the employee that an offer of employment is conditional on them opting out.

Penalties and reviews of compliance activity - Review and issue of notices

Background and policy intent

419. Recipients of statutory notices under the regime (e.g. Compliance Notices, Penalty Notices, Unpaid Contributions Notices) will be able to ask for a review of a notice by TPR, and also present new evidence. TPR will also be able to initiate a review of a notice if appropriate, and to change its decision as a result.

420. The period within which a person issued with a notice has to make an application for a review, is in line with current regulatory business practice at TPR.

421. The period within which TPR can itself initiate a review of a notice is longer at 18 months because a person may request a review of a notice that is linked to notices or penalties that have been issued previously.

What the draft regulations said

422. Regulation 16 prescribes the time limit for a recipient of a notice to apply for a review of that notice (28 days) and the time limit for TPR to decide to otherwise review a notice (18 months). The start date of both time periods is the date a notice is issued by TPR.

423. Regulation 17 allows TPR to presume that a notice had been correctly issued where TPR has done certain things, such as posting that notice to a person's last known or notified address.

Stakeholder response to consultation

424. Only one stakeholder commented on this area expressing contentment with the proposed review periods.

Government response

425. The proposed review periods appear to be appropriate.

Penalties and reviews of compliance activity - Time limits on inducements compliance action

Background and policy intent

426. The Act prohibits employers from attempting to induce individuals to leave a pension scheme, for example by offering cash bonuses or higher levels of salary in return for opting out or by warning about possible negative repercussions for anyone who does not opt out. To provide certainty for employers, their workers and TPR we intend to prescribe two time limits for enforcement action in relation to inducements.

The time within which a complaint can be made to TPR

427. We proposed that individuals should have up to six months after an inducement attempt to make a complaint to TPR. We believed this struck the right balance between protecting employers from malicious complaints on one hand, and on the other giving individuals or their representatives enough time to prepare and make a complaint.

The time limit applying to proactive investigations by TPR

428. This determines how far back TPR can look from the point where the employer is informed an investigation is being carried out. TPR only have the power to issue a compliance notice regarding inducements that occurred within this time limit.

429. We proposed 12 months from the date of the inducement as the minimum period TPR would need in order to consider taking compliance action in the context of its own proactive investigations.

What the draft regulations said

430. Regulation 18 prescribed that TPR will not be able to issue a compliance notice in respect of a contravention of the inducements measure:

- unless a complaint has been made within six months of the contravention or
- where no complaint has been made, but where TPR has instigated a proactive investigation following their own risk analysis, unless the contravention happened within twelve months before TPR informed the employer of their investigation.

Consultation question

431. We asked whether the proposed twelve months period over which TPR can look back when making their own investigations into inducements was a reasonable limit or whether TPR should be able to take compliance action over a longer period where it uncovers evidence of a breach of the inducements prohibition.

Stakeholder responses to consultation

432. Only a few stakeholders commented on the proposed six month time limit within which compliance action can be taken following a complaint about inducements. One argued for a shorter period of three months saying that it would be in the interests of all parties for such matters to be settled as soon as possible.

433. Two others argued for a longer period of 12 months saying that they felt this was more appropriate, especially since individuals might not, in the early days of the reforms, know what was permissible employer behaviour, or understand the real value of pension scheme membership.

434. On the **second time limit** which applies in cases where TPR has commenced their own investigation a majority of stakeholders thought that the **proposed twelve months was insufficient**. Some argued for no limit, asking why inducements were being singled out in this way when other breaches had no such investigation limit.

435. Others felt that longer time limits of up to six years would be more appropriate. Six years was cited on the grounds that it would align with the record keeping requirement on employers. Three years would be in line with the Pensions Ombudsman's ability to look back in their investigations. And up to four years would align this limit with the re-enrolment cycle as the requirement to re-enrol will arise every three years except when opt out occurs within the last 12 months of that period.

436. Several stakeholders **commented on a need for clarity** on what exactly would constitute a contravention of the **prohibition on inducements** some saying that this was, in fact, a more important matter than the time limits which would apply to investigations in this area. Specific scenarios which stakeholders feared might (but should not) constitute inducements included:

- offering flexible benefits schemes;
- advising workers with 'enhanced protection' on the tax implications of remaining in pension scheme membership; and
- providing information to higher paid workers on the relative merits of staying in or opting out of pension scheme membership following the change to higher rate tax relief in last year's Finance Bill.

Government response

437. We still feel that six months for the time limit on complaints about inducements strikes the right balance. It gives individuals and their representatives enough time to identify breaches and prepare complaints while encouraging those complaints to be made as soon as possible after the actions complained about.

438. The financial incentive for a worker to make malicious complaints in this area is not nearly as great as it would be for one considering taking a case to employment tribunal on unfair dismissal, i.e. the possibility that a complaint might result in TPR requiring an employer to backdate six months worth of pension contributions as opposed to the possibility to claim compensation at tribunal, or achieve an out-of-court settlement.

439. Employers do, however, perceive a risk that aggrieved individuals might see this as an opportunity to make mischief here, and so **in order to provide certainty for all parties** in this area we believe **time limiting complaints to six months is appropriate**.

440. We agree with the majority of stakeholders who commented on the separate time limit which applies to **TPR's ability to look back** in investigation cases. We believe **this limit needs to be extended** and feel it would be most appropriate for it to be **aligned with the re-enrolment cycle of up to four years** (the requirement is to re-enrol every three years except where opt out occurs within twelve months of the re-enrolment date).

441. An investigation time limit tied to this timescale would mean that TPR would, if it came across evidence of inducement, be able to investigate all current cases, i.e. all those induced opt outs which remain effective at the time of investigation. Such a time limit would also align with the proposed record-keeping requirement on opt outs.

Guidance from TPR

442. **TPR's proposed guidance during 2010 for employers and intermediaries** should help to provide clarity on what sorts of employer actions might be considered to breach the prohibition on inducements. On the possible impact of inducements on flexible benefit schemes: such schemes which feature qualifying pension scheme membership as one of the core benefits ought not to be at any risk of contravening this measure.

443. Where such schemes offer alternative benefits when a worker opts out of qualifying pension scheme membership there may be a contravention, but it will depend on the detailed circumstances of the case and whether the offer of such a scheme could be considered to be an action the 'sole or main purpose' of which was to induce opt out.

444. An employer giving factual information about the tax implications of pension scheme membership for workers with 'enhanced protection' should not, in practice, be at risk of being considered in breach of the inducements measure.

445. Neither ought an employer giving their workers information about the implications of the higher rate tax relief changes in this year's Finance Bill fall foul of this provision. However employers should avoid giving their workforce *advice* on whether or not it would be worthwhile saving in a pension as such advice should only be provided by an authorised professional. Guidance is already available on this subject from the FSA and TPR.

Proposal for change - Time limits on inducements compliance action

- We propose to leave unchanged the six months complaint time limit but to extend the period of time over which TPR can look back when proactively investigating inducements so that that limit aligns with the re-enrolment cycle. This means that TPR will be able to look back in these cases for a possible maximum of up to four years.

(v) MINIMISING REFUNDS

Opt out refund process – change to the 19 day rule

Background and policy intent

446. Under the new employer duty, a jobholder must become an active member of a qualifying scheme with effect from day one (the automatic enrolment date). The regulations provide that contributions must be deducted on the first occasion an individual is paid after that date.

447. Where a jobholder chooses to opt out, the effect is that they were never members of the scheme and therefore any contributions paid by the jobholder must be refunded.

448. There will be times when contributions are deducted by the employer and will have to paid over to the scheme during the joining and opt out window. These contributions would have to be refunded to the jobholder if they subsequently opt out.

449. Our policy for the administration of the reforms is to minimise burden and process wherever possible. In response to the consultation on the draft Pension (Automatic Enrolment) Regulations 2009, it became obvious that employers and schemes foresee that having to pay over contributions and then subsequently refund those contributions for an individual who opts out creates significant burden and cost in the light of the constraints of the current 19 day rule.

450. The policy intention by proposing a (limited) extension to the 19 day rule is to provide employers and schemes with greater flexibility during the joining window and opt out period to reduce cost and administration burden, and remove risk of contributions due for refund losing value where immediate vesting occurs.

What the draft regulations said

451. The Occupational and Personal Pensions Schemes (19 Day Rule) (Amendment) Regulations prescribe a new period in which an employer must pass over any contributions deducted to trustees or managers where a jobholder becomes an active member of an occupational pension scheme under the automatic enrolment, opt in or re-enrolment regulations.

452. This new period applies only to contributions deducted from the jobholder's automatic enrolment date, automatic re-enrolment date or the voluntary enrolment date up to the end of the opt out period.

453. The prescribed period in these circumstances is a period starting from the automatic enrolment date and ending 19 days from the end of the second month following the month in which automatic enrolment applies.

454. The regulations leave the 19 day rule unchanged for contributions deducted after the end of the opt out period. In this case contributions must be passed to the trustees or managers within 19 days from the end of the month in which the contributions are deducted from earnings.

Consultation question

455. We asked:

- whether lengthening the due date for contributions deducted during the joining window and opt out period by one month significantly increased risk to members' benefits and whether any increased risk was justifiable in relation to the cost/burden saving achieved through minimising refunds.

- how costly or difficult would it be to make the necessary system changes to implement and facilitate an initial alternative due date in respect of those members who have been automatically enrolled.

Stakeholder responses to consultation

456. The majority of **stakeholders welcomed the change to the 19 day rule**, particularly the small employer representatives with some expressing the view that it is **vital in reducing the administration burden** for employers of jobholders who opt out. Stakeholders did not feel that this change significantly increased the risk to members' benefits and felt that the cost of system changes would be minimal compared to the administrative savings on refunds.

457. Larger employers and their representatives also welcomed the change but felt there may be administrative complexities in having dual due dates. A number of stakeholders felt the extension did not go far enough and sought an extension to ensure that the opt out period is covered in all cases.

458. Other comments received by a minority of stakeholders were:

- the change was unjustified and there was a significant risk to members' benefits;

- significant system changes would be needed and a change in the payment schedule legislation would be welcomed to avoid having to reflect new due dates; and

- employers may wish to continue to pay contributions by the original due date but offset future payments to reflect those that have opted out.

459. Stakeholders asked whether schemes can write a rule to specify whether sums will be accepted prior to the expiry of the opt out period and also whether paying contributions over by the new due date would be considered maladministration by the Pensions Ombudsman.

460. It was recognised by stakeholders that paying contributions over by the new due date is voluntary and therefore where employers do not want the complexity or cost of system changes they can pay over contributions by the original due date.

Government response

461. The majority of stakeholders see the change to the 19 day rule as positive and we feel this goes a considerable way to answering stakeholders concerns about the administrative burdens of refunds raised during the earlier consultation.

462. We recognise that there will be some system changes required to reflect dual due dates and some increased administrative burden around accounting for the extra contributions. However, where employers feel that changes are too complex and it is simpler to pay all contributions over by the same date, they can continue to do so. We do not intend to make

463. We recognise that **extending the due date** to allow the opt out period to pass in all cases will allow more employers **to minimise unnecessary cash flows from employers to schemes**, which will **reduce administration costs for employers** and potential investment loss for schemes. Therefore we recommend changing the due date from the 19th day to the last day of the second month following the month in which automatic enrolment occurs.

464. In response to schemes wanting to create a rule that specifies whether sums will be accepted prior to the expiry date: schemes and employers will normally agree a particular due date when drawing up payment schedules; any changes to scheme rules would be done in consultation or by agreement with the employer.

465. Under current arrangements some employers have an agreement with their scheme that contributions may be retained by the scheme to offset scheme administrative expenses.

466. Following an opt out, the regulations will require a refund of contributions to the employer. However, we do not envisage that this would preclude a business agreement between the employer and the scheme which, in legal terms, re-directed refunds back to the scheme to be used for other purposes – in practice the money may never leave the scheme.

467. With regards to the Pensions Ombudsman's view of employers who used the new due date, the question for the Ombudsman would be whether deferring payment of contributions was justifiable, whether or not payment was made within statutory time limits. Whether the Ombudsman would make any finding of maladministration would depend on the specific complaint, facts and circumstances before him.

Proposal for change - Opt out refund process – change to the 19 day rule

- To minimise refunds the due date for contributions deducted from the date of automatic enrolment up to the end of the opt out period will be the last day of the second month following the month in which automatic enrolment occurs.

(vi) PROVISION OF INFORMATION

Background and policy intent

468. Section 10 of the Act requires the Secretary of State to make regulatory provisions for all jobholders to be given information about the effect of sections 2 to 8 (the employers' duties in respect of jobholders) and for all workers to whom section 9 (the duty in relation to workers without qualifying earnings) applies to be given information about the effect of that section.

469. Draft provisions in this consultation require employers to give written information, by a certain timeline, to specific categories of individuals which were not previously consulted on. These include:

- jobholders who are outside the automatic enrolment age bands;
- workers without qualified earnings;
- jobholders whose employers provide defined benefit and hybrid schemes who choose to use the transitional provisions to postpone automatic enrolment;
- all jobholders and existing members of qualifying scheme to inform them of their right to remain an active member without employer interference; and
- jobholders whose employer makes use of the phasing of contributions about the effect on them.

What the draft regulations said

470. Regulation 2(1) (g) prescribes that as part of the enrolment information the employer must give information that tells the jobholder that they have the right to continuous active membership without interference from the employer unless they have active membership of another qualifying scheme.

471. Regulation 2(2) prescribes that employers who provide money purchase and personal pension schemes and who choose to phase in contributions gradually over the implementation period must reflect this in their enrolment information to those jobholders who are affected.

472. Regulation 18 requires employers to give jobholders who are outside the automatic enrolment age bands written information to alert them to their right to opt into pension saving, the levels of employer and jobholder contributions, and details of where to go for further information about pensions and saving for retirement. Those individuals who choose to exercise their right must give the employer a written and signed opt in notice. An electronic notice can be accepted but must be accompanied with a statement confirming that the jobholder personally submitted it.

473. Regulation 22 prescribes that the employer must give workers without qualifying earnings written information to alert them of the right to ask their employer to make arrangements for them to join pension saving. The worker can either give a written and signed joining notice to the employer or can give notice electronically, provided it is accompanied with a statement confirming that the worker submitted the notice.

474. In addition, the worker must be informed that they have the right to choose how much to contribute (in accordance to scheme rules) and be given details of where to go for further information about pensions and saving for retirement.

475. Regulation 25(c) requires that when confirmation is given to individuals that they are members of a qualifying scheme, the employer must also include a statement that the jobholder has a right to continuous membership of that scheme without interference from their employer unless the jobholder becomes an active member of another qualifying scheme.

476. Regulation 41 requires an employer who operates a defined benefit or hybrid pension scheme who chooses to make use of the transitional provisions must provide certain prescribed information to the jobholder. This includes information about the scheme into which the jobholder will become an active member, the date when the jobholder will become a member of that scheme, details of where more information can be accessed on pensions and saving for retirement and the right to opt in to pension saving during the transitional period.

Consultation questions

477. We asked whether:

- the information given to jobholders whose employer made use of the transitional period to gradually adjust to the reforms should be given within one month rather than the two months prescribed in the regulations; and

- any other key pieces of information that should be given to these individuals.

Stakeholder responses to consultation

478. There was **overwhelming support** from stakeholders for the **information to be given** to individuals **no later than two months after the date from which the transitional period starts** (i.e. what would have been the auto-enrolment date). A few stakeholders suggested that the deadline should be reduced to one month in order to have parity across all the information provisions.

479. Although the majority of stakeholders **did not believe that there were any other key pieces of information** that should be given to these jobholders, there were suggestions to include information about contribution/benefit levels, who to contact, automatic re-enrolment, risks and funding, and how an individual might opt in. Stakeholders also acknowledged that jobholders would get additional information from the scheme.

480. Other comments were mostly focused on **improving the drafting of the new information provisions**, in particular to Regulations 2 (enrolment information) and 25 (information to existing scheme members).

481. It was suggested that **regulations 18 and 22 place a disproportionate burden on employers** by requiring them to alert individuals, who are not eligible for automatic enrolment of their right to join pension saving. Instead, it was suggested that the onus should be placed on the jobholder to approach the employer about opting in. It was also suggested that all individuals, irrespective of their status, should be given the same information and that the requirement for employers to give information to workers about their rights runs contrary to the norms of employment processes.

482. Another stakeholder sought clarification between requirements under the current FSMA regime and section 9 of the Act

Government response

483. We have carefully considered all **drafting suggestions** made for the information-related provisions and **taken on board any those that help improve clarity**.

484. For Regulation 41, we will **keep the two month deadline for the provision of information** as consulted on. The regulations give employers the flexibility to give this information earlier than the deadline, whether that is prior to the transitional start date or on the transitional start date.

485. We will **incorporate the suggestion to include information about contribution levels**. We realise that it is not usually possible for defined benefit schemes to provide information about contribution levels. We will therefore mirror the drafting in the enrolment information, regulation 2(1) (d), so that it is given if known. We will leave it to scheme information to inform the individual about accrual rates, the benefit structure of the scheme, funding and risks involved.

486. We will also **add in the requirement for information to be given about how the jobholder can opt into the scheme**. This should not significantly affect employers and schemes existing arrangements.

487. However, we do not see the need to include information about auto re-enrolment at this stage. Individuals when they are enrolled into a qualifying pension scheme will be given enrolment information which will include information about automatic re-enrolment.

488. For regulation 18 and 22, the **suggestion to place the onus on the jobholder**, who is not eligible for automatic enrolment, to approach the employer about opting in **cannot be considered**. The policy is that individuals are made aware of this new right rather than having to find out about it themselves. In addition, section 10 of the Act requires that a 'prescribed person' must give information to the jobholder about the effect of section 7 (Jobholder's right to opt in).

489. Although it is not routine employment practice for employers to give information to their workforce about their rights, many employers already adopt the good practice of making information available from day one of employment, such as information about maternity rights, statutory sick pay, pension schemes etc. We believe that the employer is best placed to be the 'prescribed person'. The employer has the necessary information to determine whether automatic enrolment is applicable to a worker or not.

490. The regulations clearly set out the minimum key pieces of written information which different categories of workers must receive from their employer. Whether employer gives additional information to what is prescribed is a matter for the employer. There will be **guidance provided by TPR to help employers meet this and other information requirements**.

491. In relation to the question raised about financial promotions under the Financial Services and Markets Act 2000 regime, we do not consider that communications by an employer to comply with the requirements of the regulations will constitute promotions which are prohibited by FSMA. The financial promotion restriction does not apply where a communication is required or authorised by or under an enactment.[8]

[8] Article 29 of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (S.I. 2005/1529)

Proposals for change: Provision of information

- We will incorporate into this provision the suggestion to include information about contribution levels. The drafting will mirror regulation 2(1) (d) (enrolment information).
- We will also include the suggestion that information be given about how the jobholder can opt into the scheme.
- We will amend regulation 41(3) (b) to provide for the automatic enrolment date instead of the date when the jobholder will become an active member of the scheme.

SECTION 4: RESPONSES TO THE IMPACT ASSESSMENT

Background on the Impact Assessment

492. The draft Workplace Pension Reform (Completing the Picture) Regulations 2010 set out some of the detailed processes that employers will have to complete in order to comply with the Act. The Impact Assessment, published alongside the draft regulations, presented impacts which related only to these aspects of pension reform (not the total reform package) and is based on the best available data.

Stakeholder response to consultation

493. Key stakeholders provided responses to the Impact Assessment. In particular, there were two areas of concern. Firstly that the **costs to employers of administering the new process were too low** and secondly that the **administrative costs did not take account of the individual processes required to comply**.

Government response

494. Estimates of the **administrative costs to employers are based on the specific requirements set out in the regulations** for:

- the remaining automatic enrolment aspects of the reform.[9]
- implementation;
- registration;
- compliance; and
- changes to the nineteen day rule.

495. The Standard Cost Model[10] approach has been used to estimate the administrative costs resulting from the draft Workplace Pension Reform (Completing the Picture) Regulations 2010, with consideration being given to the activities involved for each employer, who in the firm will carry out each activity, how frequently, how much they get paid and how long it will take.

496. The **assumptions used in the costing represented the best available data and evidence** about the likely number of employers and individuals who would be affected by each of the requirements in the regulations, the time taken for each task and data on wages.[11]

497. DWP have estimated that the additional administrative costs to employers resulting from the specific processes in the draft regulations are £234 million in year one and £22 million in ongoing years thereafter.[12] These costs result from this specific set of regulations, not the overall reforms as a whole and are the costs above and beyond firms' 'business as usual' costs. The actual cost to each employer of complying with these regulations will depend on

[9] It excludes those already costed in the Impact Assessment of Pensions (Automatic Enrolment) Regulations 2009. http://www.dwp.gov.uk/docs/pension-auto-enrol-imp-assess.pdf
[10] http://www.berr.gov.uk/files/file44503.pdf
[11] The high level methodology behind administrative cost estimates is detailed in Annex G of the Pensions Bill - Impact Assessment (published April 2008). This methodology has been updated to reflect the detailed processes that employers are obliged to complete as a result of the draft regulations.
[12] DWP modelling.

their specific circumstances, how many employees they have and whether they are already contributing to their employees' pensions. The average administrative costs per firm shown in the Impact Assessment show an equal split of these additional costs between all firms within different size bands.

498. The Government recognises the challenges faced by small firms in particular and are confident that **on-going costs resulting from the regulations have been fully captured** using the latest available information. Small employers will have an important role to play in the delivery of reforms. We have designed these reforms to ensure that costs are kept to a minimum and we continue to consult closely with relevant employer groups and businesses on what other steps we can take to ensure these reforms are delivered smoothly.

499. Research with small employers[13] highlighted that small employers had adopted a pragmatic approach to previous legislative reform such as the National Minimum Wage. They found previous implementation easy to manage because many administrative tasks were outsourced. They accepted the cost of legislative change as an inevitable part of running a business.

500. There was no evidence of budgeting for previous government legislation, even when the associated costs were considered expensive. In the past, additional costs had been absorbed by a reduction in profits.

501. Recently published qualitative research with small employers[14] suggested that adjusting to the reforms would be less burdensome than expected, particularly where employers have existing schemes in place. Many stated that additional payroll processes would be simple to administer as software packages will be automatically updated.

502. **Estimates of the administrative costs will continue to be updated and reviewed in light of new evidence received**. A full Impact Assessment, updating the overall costs and benefits of these reforms will be published when the regulations are laid in Parliament in January 2010.

[13] Thomas, A. and Philpin, C. (2009) *Understanding small employers' likely responses to the workplace pension reforms: report of a qualitative study*, DWP research report no. 617.
[14] Wood, A., Robertson, M. and Wintersgill, D. (2010) *Consultation on workplace pension reforms: Qualitative research with small and medium sized companies.* DWP Research Report

SECTION 5: Annex A - Certification Commentary

What the draft regulations on which we consulted said

503. Regulation 47 defines the terms used in the regulations.

504. Regulation 48 prescribes the content and format of the certificate required under Section 28 of the Act, by cross referring to the template in schedule 2 to the Regulations. An employer must sign the certificate and retain it for six years. Employers can decide the date from which the certificate starts, and it can remain in force for up to a year or a shorter period.

505. Regulation 49 states that employers may only give a certificate if they are of the opinion that the scheme will meet the relevant quality requirement for the jobholders that they employ and who are active members of the scheme.

506. Regulation 50 provides that a scheme will be not treated as having met the quality requirement at the end of the certification period, if:

a) the total contributions payable by the employer and the jobholder is below 7.6% of the required amount;

b) the scheme satisfied the quality requirement for less than 90% of jobholders who were active scheme members; or

c) jobholders experienced a shortfall in their contributions more than once in a consecutive 24 month period.

507. Regulations 51 applies where the shortfall exceeds the levels set out in regulation 50 in which case the employer must make up the shortfall to the required amount of contributions under the relevant quality requirement. A scheme will then be treated as having met the relevant quality requirement if the employer makes the applicable payment.

Section 5: Annex B - The Hybrid Scheme Quality Requirement Rules 2010 Commentary

The draft rules have been published alongside the regulations for completeness. We will continue to work on their content with stakeholders.

Commentary

1. Rule 1 - *Citation, commencement and interpretation* **-** sets out some of the terms used in the rules

2. Rule 2 – *Application: general* applies to any hybrid which is a type specified within the descriptions set out in rules 3 –10 of the Hybrid Schemes Quality Requirements Rules 2010

Applying the rules: each rule sets out how section 24(1) of the Act (quality requirements for UK hybrid schemes) is to apply when determining whether a particular scheme of the type specified in the rule satisfies the quality requirement in relation to a particular jobholder. Also whether the application of a quality requirement is modified.

3. *Rule 3 – Contracted-out hybrid schemes* **-** applies to: a scheme that is a contracted-out scheme

Applying the rule: Section 21(1) of the Act applies to a scheme relating to jobholders in contracted-out employment with the effect that a scheme qualifies on the basis of those jobholders' contracted-out employment. For jobholders not in contracted-out employment, the applicable quality requirements are to be determined, in accordance with rules 4-10.

4. *Rule 4 – the general rule for hybrid schemes* - applies to: hybrid schemes under which the benefits that will be provided include both defined benefits and money purchase benefits, excluding contracted-out schemes which are subject to rule 3 and any scheme specified in rules 5-10. The rule aims to simplify the rules for most hybrids schemes for which the quality requirements do not need to be modified.

A*pplying the rule:* a scheme qualifies if either the money purchase or the defined benefits quality requirements are satisfied, it is irrelevant which.

5. *Rule 5 – Sequential hybrid schemes* – applies to schemes which provide for both defined benefits and money purchase benefits but where a member cannot accrue both types of benefits at the same time, although the member may transfer between the two, in accordance with scheme rules.

Applying the rule: the general rule in rule 4 applies except that both the money purchase and defined benefits quality requirements must be satisfied.

6. *Rule 6 – Self-annuitising hybrid schemes* - applies to: schemes under which:

a) The rate or amount of pension or other benefits to be paid, in respect of the scheme members at or after their retirement at normal pension age, will be calculated wholly by reference to payments made by the member or another person in respect of the member (or transfer or other credits), but

b) A number of pensions or other benefits provided to members at or after their retirement may be paid from the scheme's resources.

7. Applying the rule: the money purchase quality requirements referred to in section 24(1) of the Act apply unmodified.

8. *Rule 7 Cash balance hybrid schemes* – applies to schemes under which the rate or amount of pension or other benefits to be paid on behalf of a member at or after their retirement at normal pension age will be calculated as a lump sum and calculated otherwise than wholly by reference to payments made by the member or another person (or transfers or other credits). The lump sum will be available for the provision of a pension or an annuity.

Applying the rule: the defined benefits quality requirements are applied in accordance with section 24(1), subject to the prescribed modification in regulation 41 of the Occupational and Personal Pensions (Automatic Enrolment) Regulations 2010.

9. *Rule 8 - Final salary lump sum hybrid schemes* – applies to schemes under which the rate or amount of pension or other benefits to be paid to or in respect of scheme members at or after their retirement at normal pension age will be calculated by reference to their salary in the period immediately prior to ceasing to be an active member (or transfers or credits). The lump sum will be available for the provision of a pension or an annuity.

Applying the rule: the defined benefits quality requirements are applied, in accordance with section 24(1), subject to the prescribed modification in regulation 42 of the Occupational and Personal Pensions (Automatic Enrolment) Regulations 2010.

10. *Rule 9 - Combination hybrid scheme*- applies to schemes under which members accrue both defined benefits and money purchase benefits for the same period of service.

Applying the rule: The provisions relating to defined benefits and money purchase benefits are to be treated as if they were being provided under separate schemes and the quality requirements that apply are to be determined as follows:

a) The first step is to apply the general rule in rule 4, and if this is satisfied, there is no need to take the second step.

b) If neither the money purchase quality nor defined benefits requirements are satisfied, nevertheless those requirements may be treated as satisfied, in accordance with the modification prescribed in regulation 43 of the Occupational and Personal Pensions (Automatic Enrolment) Regulations 2010.

11. *Rule 10 – Schemes where more than one rule applies* - applies where schemes which provide for benefits in such a way that, if the provisions of the scheme providing for different benefits were treated as separate schemes, the scheme would fall within any of rules 4 - 9.

Applying the rules: in respect of each separate scheme apply the relevant quality requirements in accordance with rules 4-9.

SECTION 5: Annex C - List of respondents

ABI
Aegon
Aon Consulting
Allen and Overy LLP
Association of Chartered Certified Accountants
Association of Consulting Actuaries
Association of Disabled Professionals
Association of Pension Lawyers
Aquilaheywood
AVIVA
Barclays Bank
Barnett Waddington LLP
BCC
Blue fin
British Broadcasting Corporation (BBC)
Buck Consultants
Building and Construction Employers Benefit Schemes
Capita Hartshead
CBI
C. & J. Clark International Limited
Chartered Institute of Personal development
Devon County Council
EEF
Equality and Human Rights Commission
Eversheds
Fidelity
Foremost Services Limited
Friends Provident
FSB
Globe Connections
GMB
Hewitt
HSBC
Hymans Robertson LLP
ICAEW
Institute of Chartered Accountants of Scotland
Investment Management Association (IMA)
Institute of Directors (IOD)
Jaguar Land Rover
Jardine Lloyd Thompson Benefit Solutions Ltd
J. Sainsburys
Legal & General
Lloyds Banking Group
Local Government Employers (LGE)
Logica
Marks and Spencer
Mercer
NAPF
PricewaterhouseCoopers
Prudential
Punter Southall
REC
Rexel UK Limited
Road Haulage Association
Royal Society for the Protection of Birds
Sacker & Partners LLP
Scottish Life and Royal London's
Scottish Widows
Standard Life
Tesco
TISA (Tax Incentivised Savings Association)
The Actuarial Profession
The Co-operative Group Ltd
The Institute of Payroll Professionals (IPP)
The Pearl Group
The Pensions Advisory Service
The Pensions Management Institute
The Pensions Trust
The Society of Pension Consultants
Towers Perrin
Travers Smith
TUC
Unison
Watson Wyatt
Whitbread Group Plc

ISBN: 978-1-84947-179-4