Title: Workplace Pension Reform Secondary Legislation 2015 - Exceptions to the employer duty for Automatic Enrolment **IA No: DWP0050** **Lead department or agency: Department for Work and Pensions** **Other departments or agencies: N/A**	**Impact Assessment (IA)** **Date: 27th January 2015** **Stage: Final** **Source of intervention: Domestic** **Type of measure: Secondary Legislation** **Contact for enquiries: Lawrence Key** **Lawrence.key1@dwp.gsi.gov.uk**

Summary: Intervention and Options

RPC: Awaiting scrutiny

Cost of Preferred (or more likely) Option				
Total Net Present Value	**Business Net Present Value**	**Net cost to business per year**	**In scope of One-In, One-Out?**	**Measure qualifies as**
N/A	N/A	Zero Net Cost	Yes	OUT

What is the problem under consideration? Why is government intervention necessary?

During the initial stages of automatic enrolment it became apparent that pension saving, or further pension saving, may not be appropriate for some eligible workers. In its response to the March 2013 consultation on technical changes to improve the operation of automatic enrolment, the Government expressed the view that there was a strong case for exempting from the automatic enrolment requirement individuals who are leaving employment, who cancel membership of a pension scheme before automatic enrolment and those with tax protected status for existing pension savings. Government intervention is necessary to prevent employers from undertaking nugatory work and to prevent workers who have little or nothing to gain from being automatically enrolled.

What are the policy objectives and the intended effects?

The policy objective is to prevent unnecessary administrative burden on employers from enrolling and re-enrolling employees for whom automatic enrolment is clearly not suitable. Furthermore it aims to prevent individuals from being adversely impacted by being automatically enrolled into a workplace pension when it is not appropriate. By exempting certain categories of individuals who would not benefit from automatic enrolment from being enrolled in the first place, the administrative burden on employers is reduced as is the risk that individuals will not opt out and so would be adversely impacted.

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)

Two options have been considered: Do nothing (whereby all eligible employees are automatically enrolled) or legislate for the option of allowing employers to exempt certain categories of employees from automatic enrolment (option 1). As the requirements are set out in legislation a non-legislative option is not possible.

Doing nothing is not a reasonable option. Although workers maintain the option to opt out of automatic enrolment there is an unnecessary administrative burden on employers enrolling employees for whom automatic enrolment is clearly not suited. This goes against the original policy objectives of automatic enrolment to minimise the burden on employers.

Option 1, allowing employers to exempt certain categories of individuals, is intended to prevent unnecessary administrative burden on employers from enrolling and re-enrolling employees for whom automatic enrolment is clearly not suitable. Furthermore it aims to prevent individuals from being automatically enrolled into a workplace pension when it is not appropriate. Individuals for whom automatic enrolment would not be beneficial currently have to opt out every 3 years; this is not a desirable option. Option 1 would allow employers to exempt certain categories of individuals for whom automatic enrolment is clearly not suitable or for whom the administrative costs are disproportionate (i.e. because they are due to leave employment) from contributing.

This change is permissive so if the costs are greater than the benefits then employers do not need to change their processes or take advantage of the exceptions; they will only do so if it is beneficial to them.

Will the policy be reviewed? It will be reviewed **If applicable, set review date:** 2017

Does implementation go beyond minimum EU requirements?			N/A		
Are any of these organisations in scope? If Micros not exempted set out reason in Evidence Base.	**Micro** Yes	**< 20** Yes	**Small** Yes	**Medium** Yes	**Large** Yes
What is the CO2 equivalent change in greenhouse gas emissions? (Million tonnes CO2 equivalent)			**Traded:** N/A	**Non-traded:** N/A	

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible Minister: Steve Webb Date: 27/01/15

Summary: Analysis & Evidence

Policy Option 1

Description: Introduce exceptions to the employer duty for Automatic Enrolment

FULL ECONOMIC ASSESSMENT

Price Base Year	PV Base Year	Time Period Years	Net Benefit (Present Value (PV)) (£m)		
2014	2015	10	**Low:** N/A	**High:** N/A	**Best Estimate:** N/A

COSTS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	N/A	n/a	N/A	N/A
High	N/A		N/A	N/A
Best Estimate	N/A		N/A	N/A

Description and scale of key monetised costs by 'main affected groups'

N/A

Other key non-monetised costs by 'main affected groups'

Any potential familiarisation costs are estimated to be marginal due to the proposed change because:

- Employers approaching their staging date would have to familiarise with relevant literature anyway. The Pensions Regulator (tPR) plan to amend this literature to reflect these changes.
- Individuals who have a tax protected status and who are approaching their staging date would have to familiarise with relevant literature anyway. HMRC plan to amend their literature on this to reflect these changes.

As this is a permissive change employers are only likely to take advantage of these exceptions if it is more cost effective than using the existing duty.

BENEFITS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	N/A	0	N/A	**N/A**
High	N/A		N/A	**N/A**
Best Estimate	N/A		N/A	**N/A**

Description and scale of key monetised benefits by 'main affected groups'

N/A

Other key non-monetised benefits by 'main affected groups'

Employers who choose to exempt individuals from automatic enrolment will benefit from a reduction in the administrative burden of enrolling workers and, depending on the category of individual, benefit from a potential reduction in employer pension contributions. Similarly individuals who are exempted from automatic enrolment will benefit from not contributing towards a pension that is not suitable for them and make it easier to avoid incurring unwanted tax charges. We have not been able to robustly monetise the impact of these changes on either the individuals or the employers.

Key assumptions/sensitivities/risks — **Discount rate (%)** 3.5%

As the legislation will be permissive, employers are only likely to adopt the new employer exemptions to their duty if the cost of doing so is less than that of complying with the exisiting requirements.
As the exemptions are intended to reduce the administrative burden on employers and potentially reduce employer pension contributions it is likely that they will choose to exercise this right if appropriate.

BUSINESSASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £m:			In scope of OIOO?	Measure qualifies as
Costs: 0	**Benefits:** N/A	**Net:** 0	Yes	OUT

Evidence Base

Background

1. A range of legislation has been introduced to support the Government's strategy to tackle the consequences of increasing longevity and widespread under-saving for retirement. This includes the Pensions Acts of 2008, 2011 and 2014 which set out the high level framework for automatic enrolment. The proposals discussed in this Impact Assessment are intended to introduce technical simplifications to the automatic enrolment framework to ease the burden on employers, particularly having regard to the small and micro businesses that will shortly be required to enrol their eligible workers into a workplace pension scheme.

2. In March 2013 we consulted on the principle of exceptions and the groups who should be exempted, we have recently consulted again on the detail with a view to establishing the impact of the proposed legislation[1]. The response to the recent consultation will be published in early February. Where appropriate, we have referred to responses to the consultation in this impact assessment.

3. Automatic enrolment mandates employers to provide a workplace pension for their eligible workers. Automatic enrolment commenced in July 2012 beginning with the largest employers. All employers that existed in April 2012 are required to meet their duty to enrol their workers into a qualifying workplace pension scheme by April 2017; with small and micro employers starting to stage from June 2015. Around 1.3[2] million employers will ultimately be affected and around 10 million people will be eligible for automatic enrolment[3], with 8 to 9 million people newly saving or saving more[4].

4. In its response to the March 2013 consultation on technical changes to improve the operation of automatic enrolment, the Government expressed the view that there was a strong case for exempting some individuals from the automatic enrolment requirement. These included individuals who are leaving employment, who cancel membership of a pension scheme before automatic enrolment and those with tax protected status for existing pension savings.

Rationale for intervention

5. Legislation currently mandates employers to automatically enrol all eligible workers into a qualifying workplace pension. The government has identified several categories of individuals for whom automatic enrolment is clearly not suitable. Automatically enrolling these individuals only for them to opt out places an unnecessary administrative burden on employers. Furthermore there is a risk that individuals may be inadvertently automatically enrolled into a workplace pension when it is not appropriate.

6. Government intervention is necessary to remove this obligation on employers so that certain categories of individuals would be exempt from automatic enrolment. This would remove the unnecessary administrative burden on employers as well as mitigate the risk to individuals of being adversely affected.

Policy objectives

7. The policy objective of the proposed changes is to prevent unnecessary administrative burden on employers from enrolling and re-enrolling workers for whom automatic enrolment is clearly not suitable. Furthermore it aims to prevent individuals from being automatically enrolled into a workplace pension when it is not appropriate. By exempting certain categories of individuals who would not benefit from automatic enrolment from being enrolled in the first place the

[1] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/381566/technical-changes-to-automatic-enrolment.pdf
[2] http://www.thepensionsregulator.gov.uk/docs/automatic-enrolment-employer-staging-forecast.pdf
[3] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/266348/review-of-ae-earnings-trigger.pdf
[4] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/323953/dwp-annual-report-accounts-2013-2014.PDF

administrative burden on employers is reduced as is the risk that individuals fail to opt out and so are adversely impacted.

Description of options

Do nothing

8. Maintaining the status quo and doing nothing would mean that employers would continue to enrol all eligible workers and if it is not appropriate they would have to opt out. This process would be repeated on a 3 year cycle due to the requirement to re-enrol eligible workers if they have opted out. Whilst this option does allow individuals an exit mechanism from automatic enrolment it is not a desirable option as it places an unnecessary administrative burden on employers. Furthermore there is a risk, that due to inertia, workers would accidentally remain in pension saving when it is not in their interest.

9. Both the unnecessary administrative burden and the risk of a potential negative impact on individuals go against the original policy objectives of automatic enrolment. For these reasons it is not a viable option going forward.

Option 1: Exceptions to the employer duty for Automatic Enrolment (preferred option)

10. The preferred option is to allow employers to exempt certain categories of individuals from automatic enrolment. These categories of individuals are those:
    - Who are leaving employment;
    - Who cancel membership of a pension scheme before automatic enrolment; and
    - With tax protected status for existing pension savings, including those who have been paid a winding up lump sum in a particular circumstance.

11. For individuals who hand in their notice, give notice to retire, or who are under notice of dismissal and their period of notice spans their automatic enrolment or re-enrolment date it may not be beneficial to be automatically enrolled for such a short period. Doing so would not only create a trivially small pension pot for the individual but also mean unnecessary administrative costs for the employer. Stakeholders responded to our recent consultation highlighting this issue and commenting that the current situation creates additional administrative work for employers with little benefit for workers.

12. Some employers may choose to enrol workers into a pension scheme when they start work through their contract. Currently, where these workers cancel their membership they may still have to be automatically enrolled when they become eligible jobholders (i.e. they reach the age 22 and have appropriate earnings, or when the employer reaches its staging date) even if they have only recently left the pension scheme. For these individuals it does not make sense to be automatically enrolled, they have recently made an active decision about pension saving and so it would not be in their or the employer's interest to enrol them only for them to either opt-out straightaway or inadvertently and unwantedly contribute towards a pension through inertia.

13. The intention is to remove duplication for these individuals but leave people's right to access pension savings intact. This means introducing an exception to the employer duty so that where a person cancels membership after joining, the employer has no further obligation until a point in the future. Stakeholders have responded positively to this suggestion and have highlighted the current situation as an unnecessary administrative burden on employers and potentially confusing to their workers.

14. Some employees who have already accrued pension savings above the lifetime allowance are protected from tax charges, under enhanced or fixed protection provisions, provided no further tax-relieved pension contributions are made. Similarly individuals who have received a winding up lump sum are protected from tax charges provided no further tax-relieved pension

contributions are made. Automatic enrolment puts these arrangements at risk because of the nature of the employer duty where the worker is automatically enrolled into a pension scheme. At the moment the only option available to individuals with this protection is to self-identify and opt out. If for any reason they do not do so within the statutory time limit they could face significant tax charges. The underlying employer duty is still there and creates nugatory work that has started to have a negative impact on the credibility of the policy. This is an experience which may have to be repeated every three years when eligible workers will be re-enrolled.

15. Both individuals who have tax protected status and individuals who cancel membership of a pension scheme before automatic enrolment retain the right to opt in, and so if they wish to benefit from automatic enrolment they may still do so.

Employers potentially affected

16. All employers who have to automatically enrol or re-enrol workers will be potentially affected by this change. The Pension's Regulator (tPR) estimate that by 2017/18 when Automatic Enrolment has been fully implemented that approximately 1.3 million employers will have automatically enrolled their employees[5]. In addition three years after staging, employers are required to re-enrol any workers who have opted out or left pension saving. At this stage employees must again opt out of Automatic Enrolment if they do not wish to save.

17. Whilst we are able to estimate the number of employers that could potentially implement the proposed changes, it is a permissive change so there is nothing mandating an employer to make any changes. Automatic enrolment is a relatively new policy and there is limited evidence on how employers will respond to these technical changes; therefore we are unable to make any robust conclusions or assumptions on what proportion will take advantage of the exceptions to the employer duty. Stakeholders continue to be supportive of the exceptions to the employer duty. Respondents to our recent consultation indicated that employers are likely to implement the changes as they are likely to be of benefit to both employers and workers.

18. To obtain more evidence on the number of employers who would take advantage of the exceptions to the employer duty would require a large scale survey of employers. Given that these changes are permissive and deregulatory and that completing the survey would impose a burden on employers the cost would be disproportionate. Furthermore it may provide potentially un-robust information as employers may change their decision as the composition of their workforce changes.

Individuals potentially affected

19. We are proposing that three categories of workers be exempt from the employer duty. Individuals coming under these categories do not have to be automatically enrolled by their employer. These are:

- Where an individual has a protected tax status (including those who have been paid a winding up lump sum in a particular circumstance) and additional pension saving can lead to an unwanted tax charge.
- Where an individual will shortly be leaving their employment.
- Where an individual has recently ceased pension saving having been contractually enrolled.

[5] http://www.thepensionsregulator.gov.uk/docs/automatic-enrolment-employer-staging-forecast.pdf

20. HMRC estimated that in April 2014 there were approximately 120,000 individuals with pension savings of over the life time allowance of £1.25 million and who would therefore be eligible for tax protected status[6]. We do not know how many of these are in work or who would meet the eligibility criteria for automatic enrolment but as they are high net worth individuals it is likely that the majority will meet the primary criteria of income over £10,000 per year if they are in employment.

21. To estimate the number of individuals who would shortly be leaving employment, who recently ceased pension saving under contractual enrolment or who have received winding up lump sums would require detailed information from employers. This data is not currently available and to obtain it would require an employer wide survey. This would be disproportionate considering that the proposed change is deregulatory; furthermore it would impose an unnecessary burden on employers.

Monetised and non-monetised Costs and benefits

22. This section explores the costs and benefits that may be faced if employers exercised their choice to apply exceptions to the employer duty. As previously mentioned, the legislation will be permissive and employers can choose whether or not to apply the exceptions to the employer duty. If they choose not to, this will maintain the status quo and they will not incur any new costs. As the exemptions will reduce the administrative burden on employers and potentially reduce employer pension contributions it is likely that they will choose to exercise this right if appropriate i.e. if the benefits of doing so are greater than the costs.

Familiarisation costs

23. Whilst there were familiarisation costs imposed on employers by the introduction of automatic enrolment, any additional familiarisation costs due to the proposed technical changes are deemed to be marginal because:

- Employers approaching their staging date would have to familiarise with relevant literature anyway.TPR plan to amend this literature to reflect these changes; and

- Individuals who have a tax protected status and who are approaching staging date would have to familiarise with relevant literature anyway. HMRC plan to amend their literature to reflect these changes.

Employers

24. There are approximately 1.3 million employers who would be potentially affected by this change. As the change is permissive employers are likely to only choose to adopt the changes if the benefits are greater than the costs. Respondents to the recent consultation were positive about the changes and believed that they would reduce the administrative costs imposed on employers.

25. Information on the cost of individual administration activities is not readily available with costs likely to vary by employer size; with this in mind we are unable to robustly monetise the benefit to employers of a reduction in these costs due to the proposed changes.

[6] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/264435/11._Pensions_lifetime_allowance_-_individual_protection.pdf

26. As previously mentioned (Para 17) we have also been unable to robustly estimate the proportion of employers who will adopt the changes. As the exemptions will reduce the administrative burden on employers and potentially reduce total employer pension contributions (by exempting certain groups of individuals) it is likely that they will choose to exercise this right if appropriate. Response to our recent consultation indicates that where applicable employers are likely to change their processes in line with the proposed changes. We therefore estimate that there will be a **net benefit to employers but we are unable to monetise this benefit**.

Individuals who are exempt from automatic enrolment

Jobholders with a tax protected status

27. As previously mentioned (paragraph 20) HMRC estimate that approximately 120,000 individuals are eligible for tax protected status due to their level of pension saving. We do not know how many of these are in work or who would meet the eligibility criteria for automatic enrolment but as they are high net worth individuals it is likely that the majority will meet the primary criteria of income over £10,000 per year if they are in employment. We have been unable to estimate the number of individuals who have been paid a winding up lump sum and who would be affected by this change however consultation responses indicate that employers expect this to be a small number of individuals.

28. Being exempt from automatic enrolment is likely to be a benefit for this group as if they did not opt out they could lose their tax protected status. Engagement with external stakeholders suggests that this could cost the individual a significant amount of money due to the tax liability created. This exception reduces the risk that an individual would forget to opt-out either at enrolment or re-enrolment and therefore lose their tax protected status.

29. In response to the recent consultation stakeholders were overwhelmingly positive about the proposed change for these individuals and believed it would provide a significant benefit to those individuals affected.

30. The alternative of just maintaining opt out as an exit mechanism does work as it terminates scheme membership. However, both the employer and the individual will have been put through unnecessary inconvenience and expense due to the opportunity cost of doing so. We therefore estimate there is an **unquantifiable benefit to both individuals and employer** of implementing this change.

Jobholders leaving employment

31. Existing labour market data does not contain information on the number of people who have either given notice or been given notice of the end of their current employment. We therefore cannot currently estimate the number of people who would be exempt from automatic enrolment due to falling under this category. To obtain a robust estimate would require a large scale employer survey, which (given the change is deregulatory and permissive) would be disproportionate.

32. Jobholders who have given notice of their intention to leave employment or to retire are likely to have little to gain from being automatically enrolled in a pension scheme for such a short period of time. There is a small risk that some jobholders who previously would have benefited from being automatically enrolled for this period will not be. However given that the money accrued

over the notice period is likely to be small[7] and that the jobholder maintains the right to opt in this impact is viewed to be negligible. Responses to the recent consultation aligned with this view, commenting that it created additional and unnecessary administrative work for the employer with little benefit to employees.

Jobholders who have recently ceased pension saving being automatically enrolled

33. Jobholders who have recently ceased pension saving have made an active decision to not contribute to their pension. The alternative of just maintaining opt out as an exit mechanism does provide the technical ability to cease pension saving again as it terminates scheme membership, however, both the employer and the individual will have been put through an unnecessary inconvenience and expense due to the opportunity cost of doing so. It is superfluous and imposes an unnecessary cost to both the employer and worker to ask this individual to opt out again. The individual retains the right to opt in and so this is unlikely to negatively impact upon them. We therefore estimate there is an **unquantifiable benefit to both individuals and employers** of implementing this change**.**

Feedback from consultation

34. As previously discussed (paragraph 2) the Government recently consulted on the proposed technical changes to automatic enrolment. The consultation period was from 1st December 2014 to 9th January 2015 and a wide range of stakeholders responded (employers, pension's professionals, payroll providers and organisations representing employers and employees). The consultation was on the detail of the policy and draft regulations and the general view from respondents was overwhelmingly in favour of the changes.

35. Stakeholders continue to be very supportive of the introduction of these exceptions to the employer duty. In particular respondents commented that the changes would be of benefit to both employers and individuals and remove the risk of reputational damage to automatic enrolment. Furthermore they commented favourably upon the permissive approach which would allow employers flexibility on introducing the exceptions. Stakeholders indicated that these changes will offer an administrative saving and remove unnecessary bureaucracy however no evidence was provided to allow us to estimate this saving.

Small and Micro Business Assessment

36. The change applies to all employers regardless of size. As the measure is permissive, small and micro businesses will not be adversely affected. This change is likely to result in a net benefit for small and micro businesses as they have yet to stage and will be able to use the exception options. However, as previously stated we have been unable to robustly quantify this benefit.

Rationale and evidence that justify the level of analysis

37. For this assessment we have made use of available data – tax protection data from HMRC, and the tPR staging profile - alongside consultation and informal engagement with stakeholders to verify our assumptions. As the measure is permissive with no direct costs, it is not proportionate to gather further evidence by surveying employers.

[7] At the current contribution rate of 2% an individual would save between £7-60 per month under Automatic Enrolment.

38. Where appropriate we have used responses to the recent consultation to strengthen our evidence. Whilst stakeholders were generally positive about the proposed changes they provided little evidence to help quantify any benefits.

Direct costs and benefits to Business (OITO)

39. This change does not impose any additional burdens on business as it is purely permissive and employers will only apply exceptions to the employer duty if they feel it will be in their interests to do so.

40. From all the evidence we have gathered through the consultation, we believe that there will be a benefit to business due to the proposed changes. Employers will benefit from a reduction in the administrative burden of automatically enrolling some workers as well as potentially benefitting from a reduction in pension contributions.

41. The proposals are deregulatory and within the scope for One-In, Two-Out. We are unable to quantify or monetise the benefit for this measure, therefore it is to be considered **an OUT with a zero net cost to business.**