Department for Work & Pensions

Review of the automatic enrolment earnings trigger and qualifying earnings band for 2014/15: supporting analysis

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Contents

Background

Millions of people in the UK are not saving enough for retirement. The measures set out in the Pensions Act 2008 aim to increase private pension saving in the UK. Automatic enrolment into a workplace pension scheme forms part of a wider pensions strategy designed to ensure that the UK has a pension system that enables individuals to save towards achieving the income they aspire to in retirement while minimising the burden on employers and the tax payer.

Automatic enrolment obliges employers to enrol all workers who satisfy age and earnings criteria into a workplace pension arrangement and pay at least a minimum level of contributions.

Annual review

The automatic enrolment earnings trigger determines who gets automatically enrolled. The qualifying earnings band sets minimum contribution levels for money purchase schemes. These thresholds are reviewed each year, and revised if appropriate, taking into account: the prevailing thresholds for National Insurance contributions; PAYE personal tax allowance; basic state pension, inflation and any other factors that the Secretary of State considers relevant.

Although the Secretary of State has some flexibility in the way these thresholds are set, section 14 of the Pensions Act 2008 constrains this flexibility[1]. The reviews must be discrete annual considerations. The Government can set out policy objectives and the principles that should inform the setting of the thresholds. It cannot pre-determine thresholds or the approach for future years.

The first two annual reviews established three principles to be used when reviewing the automatic enrolment thresholds. These principles were endorsed by stakeholders and were used again in the 2014/15 review:

(i) **Will the right people be brought in to pension saving?**

(ii) **What is the appropriate minimum level of saving for people who are automatically enrolled?**

(iii) **Are the costs and benefits to individuals and employers appropriately balanced?**

[1] Annex A of Automatic enrolment earnings thresholds review and revision 2013/14, December 2012, DWP, sets out the review factors as described in the Pensions Act 2008. See: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/184800/ae-thresholds-2013-2014-response.pdf

The Secretary of State considered each of the above principles alongside an assessment of the relevance of the review factors set out in the Pensions Act 2008 in reaching a conclusion on the level at which to set each threshold for 2014/15.

Automatic enrolment earnings trigger

Automatic enrolment into a workplace pension scheme is a policy designed to target low to moderate earners who are either not saving or not saving at least a minimum for their retirement.

The earnings trigger determines who gets automatically enrolled. If the trigger is too high then people whom the policy is designed to target may miss out. If the trigger is set too low people who are very likely to receive a high replacement rate from the State may be included[2].

The Secretary of State considered all the review factors against the analytical evidence and the policy objectives and decided that the PAYE personal tax allowance at its 2014/15 level of £10,000 is the factor that should determine the value of the trigger for 2014/15.

Qualifying earnings band

Lower limit

Workplace pension saving is one of the building blocks for retirement income. Automatic enrolment with an employer contribution is intended to build on the foundation of state pension entitlement. The qualifying earnings band drives the minimum amount that people have to save and minimum employer contributions.

The difference between the earnings level that triggers automatic enrolment and the lower limit of the qualifying earnings band produces a de-minimis mechanism for contributions. Setting the lower limit of the qualifying earnings band at the level of the 2014/15 National Insurance Contributions Primary Threshold of £7,956 and the trigger at £10,000 would produce an overall minimum contribution of around £3.40 a month. Setting the lower limit of the qualifying earnings band at the level of the 2014/15 National Insurance Contributions Lower Earnings Limit of £5,772 and the trigger at £10,000 would produce a de-minimis gap of £4,228 and thus an overall minimum contribution for someone earning just above the trigger of around £7 a month[3].

The Secretary of State considered all the review factors against the analytical evidence and the policy objectives and decided that the National Insurance

[2] See Section 4 of Framework for the Analysis of Future Pension Incomes, September 2013, DWP: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/254321/framework-analysis-future-pensio-incomes.pdf

[3] This figure assumes a minimum contribution during the first phasing profile of 1 per cent contribution by workers matched by employers.

Contributions Lower Earnings Limit at its 2014/15 value of £5,772 is the factor that should determine the lower limit of the qualifying earnings band for 2014/15.

Upper limit

The upper limit of the qualifying earnings band caps mandatory employer contributions. It distinguishes the automatic enrolment target group of low to moderate earners from earners in a higher tax band who might reasonably be expected to have access to a scheme that offers more than the minimum and are more likely to make personal arrangements for additional saving.

The Secretary of State concluded that mandatory employer contributions should still be capped and decided that the National Insurance Contributions Upper Earnings Limit at its 2014/15 value of £41,865 is the factor that should determine the upper limit of the qualifying earnings band.

Proposed thresholds for 2014/15

- £10,000 for the automatic enrolment earnings trigger
- £5,772 for the lower limit of the qualifying earnings band
- £41,865 for the upper limit of the qualifying earnings band.

The analysis in this document presents the costs, savings levels and demographic effects associated with the proposed automatic enrolment earnings thresholds and the options considered for 2014/15.

Methodology

Estimates of **employer and individual contributions** show the additional costs to employers and individuals of the proposed changes to workplace pension reforms. They are calculated using:

- Estimates of the number of workers for and from whom additional contributions are due;
- workers' average qualifying earnings estimated using the Annual Survey of Hours and Earnings (ASHE) [4]; and
- Assumed minimum contribution rates for employers and workers (both 1 per cent of band earnings in 2014/15).

Estimates of **individual tax relief** are calculated by multiplying the estimates of individuals' additional pension contributions by the appropriate income tax rate. An adjustment is applied to allow for tax relief paid on contributions by higher rate income tax payers.

Estimates of **employer tax relief** represent the tax no longer paid by employers who respond to the additional pension contribution costs of the workplace pension reforms by reducing profits or wages paid to their workers. These are calculated by multiplying the estimates of employers' additional pension contributions by estimates of the percentage of employers who will reduce profits or wages and then by the appropriate rate of corporation tax or employers' national insurance contributions respectively. Estimates of the percentage of employers responding to the additional costs of the reforms by reducing profits or wages are taken from the 2011 Employer Pension Provision survey[5].

Estimates of the number of workers for and from whom additional contributions are due are based on Department for Work and Pensions (DWP) modelling which makes use of the latest available evidence on the employer and pensions' landscape, individuals' and employers' attitudes to pension provision and the workplace pension reforms, and employers' choice of pension scheme[6].

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

[5] Table 6.10 shows employers' most likely strategy in response to the increase in total pension contribution costs resulting from automatic enrolment.

[6] A range of sources have been used, including the Employer Pension Provision Survey 2011 and the Annual Survey of Hours and Earnings 2012. Further details of the sources and methods used are available in the Impact Assessment that accompanied the Employers' Duties (Implementation) (Amendment) Regulations 2012: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/220500/wpr-rev-implementation-ia-final.pdf

Eligible workers are defined as those:

- Ordinarily working in Great Britain;
- Aged at least 22 and under State Pension age;[7]
- Earning more than £9,440[8] in 2013/14 earnings terms.

Estimates of the **demographic effects** of different earnings triggers are produced using the ASHE 2012 and the Labour Force Survey (LFS) 2012/13[9]. Analysis is presented for two groups: the population eligible for automatic enrolment and the population who are eligible but not currently saving in a workplace pension – the "target population". By definition all individuals in the target population are eligible for automatic enrolment. The eligible population is defined above. The definition of the target population is set out below.

Target population: covers eligible individuals who are either (i) not saving in a pension scheme; or (ii) saving in a pension scheme where the employer contributes less than 3 per cent of the individual's salary, and is not a defined benefit scheme[10].

ASHE 2012 was used to analyse the eligible target population by gender and age. LFS 2012/13 was used to analyse the eligible population by disability status and ethnicity[11].

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

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[7] Here State Pension age is defined as it was in 2007, where men reached State Pension age on their 65th birthday, and women reached State Pension age on turning 60. When automatic-enrolment begins in October 2012, the State Pension age of women will be slightly higher, due to the equalisation of State Pension age.

[8] This threshold is converted into 2012/13 earnings terms at £9,144 so that it is on the same terms as the ASHE data.

[9] The data sets: April – June 2012, July – September 2012, October – December 2012 and January – March 2013 were combined to represent 2012/13.

[10] Defined benefit pension schemes are occupational pension schemes specifying the benefits that are paid on retirement.

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

Results

Impact of proposed thresholds for 2014/15

Table 1 shows the impact on employers, individuals and Government associated with retaining the 2013/14 automatic enrolment earnings thresholds in 2014/15 and the proposed thresholds for 2014/15.

Under the proposed thresholds, the overall level of pension saving is estimated to be £1,380 million in 2014/15, around £9 million lower than it would be if the thresholds remained at 2013/14 levels. Around £4 million of this decrease would be from lower employer contributions; around £4 million would be from lower individual contributions; and around £1 million would be from reduced tax relief on individual contributions.

Table 1: Estimates of the impact of changing the earnings trigger and upper and lower limits of the qualifying earnings band on employers, individuals and Government (£ million, in 2014/15)

	Earnings Trigger	Qualifying Earnings Band - Lower Limit	Qualifying Earnings Band - Upper Limit	Employer Contributions	Individual Contributions	Individual Tax Relief	Level of Pension saving	Employer Tax Relief
Baseline	£9,440 (2013/14 PAYE personal tax allowance; current earnings trigger)	£5,668 (2013/14 National Insurance Lower Earnings Limit; current qualifying earnings band lower limit)	£41,450 (2013/14 Upper Earnings Limit; current qualifying earnings band upper limit)	£690m	£550m	£160m	£1,390m	£60m
Proposal	£10,000 (2014/15 PAYE personal tax allowance)	£5,772 (2014/15 National Insurance Lower Earnings Limit)	£41,865 (2014/15 National Insurance Upper Earnings Limit)	£690m	£540m	£160m	£1,380m	£60m
Difference	-	-	-	-£4m	-£4m	-£1m	-£9m	£0m

Notes:

1. Source: DWP Modelling.
2. Estimates are expressed in 2014/15 earnings terms.
3. Figures are rounded to the nearest £10 million and £1 million, as appropriate to reflect uncertainties associated with the modelling approach used, and therefore may not sum exactly.
4. Pension saving is the sum of employer contributions, individual contributions, and individual tax relief.

Impact of changing the earnings trigger in 2014/15

Table 2 shows the impact on employers, individuals and Government associated with retaining the 2013/14 earnings trigger in 2014/15 and various options considered for the value of the 2014/15 earnings trigger.

With an earnings trigger of £9,440, around 10 million individuals are estimated to be in the eligible target population for automatic enrolment, of which around 37 per cent are women. Around 170,000 fewer individuals are eligible for automatic enrolment when the earnings trigger is set at £10,000, of which around 120,000 (69 per cent) are women. Overall, when the earnings trigger is set at £10,000, around 36 per cent of the eligible target population are estimated to be women.

Raising the value of the automatic enrolment trigger from £8,105 to £9,440 in the 2013/14 annual review excluded around 420,000 individuals, of whom around 300,000 (72 per cent) were women.

Statistics published by the Office for National Statistics show that women are more likely to work part-time[12] and earn less than men[13], so they will be disproportionately represented in the group excluded from automatic enrolment by an upward revision of the earnings trigger and conversely in any group brought into pension saving by a decrease in the trigger.

Setting the earnings trigger at the value of the 2014/15 National Insurance Contributions Primary Threshold of £7,956 would add around 510,000 individuals to the eligible target population and increase pension saving by around £9 million in 2014/15.

Individuals earning below the earnings trigger are likely to be able to achieve their target replacement rates through the single-tier pension if they remain low earners[14]. For these individuals it may not be beneficial to direct income from working life into workplace pension saving. Furthermore, anyone who is not automatically enrolled into a workplace pension because of an increase in the earnings trigger will retain the right to opt-in and will receive an employer contribution as long as they earn above the lower limit of the qualifying earnings band. Employers are required to provide information about these opt-in rights.

[12] See Labour Market Statistics published by ONS: http://www.ons.gov.uk/ons/rel/lms/labour-market-statistics/november-2013/index.html

[13] See ONS analysis of the pay differences between men and women: http://www.ons.gov.uk/ons/rel/ashe/patterns-of-pay/1997-to-2012-ashe-results/patterns-of-pay-2012.html#tab-Pay-differences-between-men-and-women

[14] See Section 4 of Framework for the Analysis of Future Pension Incomes, September 2013, DWP: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/254321/framework-analysis-future-pensio-incomes.pdf

Table 2: Estimates of the impact of changing the earnings trigger on employers, individuals and Government (£ million, in 2014/15)

Earnings Trigger (in 2014/15 terms)	Rationale	Demographic Effects	Employer Contributions	Individual Contributions	Individual Tax Relief	Level of Pension Saving	Employer Tax Relief
£9,440 (baseline)	2013/14 PAYE personal tax allowance; current earnings trigger	Target group: 10 million Women - 37% BME - 9% Disabled - 13%	£690m	£550m	£160m	£1,390m	£60m
£10,000	2014/15 PAYE personal tax allowance	Excluded group: 0.17m Of which women: 69%	-£2m	-£1m	£0m	-£4m	£0m
£9,695	2013/14 threshold increased by estimated price inflation (CPI)	Excluded group: 0.07m Of which women: 71%	-£1m	-£1m	£0m	-£1m	£0m
£9,547	2013/14 threshold increased by estimated earnings inflation (AWE)	Excluded group: 0.03m Of which women: 71%	£0m	£0m	£0m	£0m	£0m
£7,956	2014/15 National Insurance Contributions Primary Threshold	Newly included group: 0.51m	£4m	£3m	£1m	£9m	£0m
£5,772	2014/15 National Insurance Contributions Lower Earnings Limit	Newly included group: 1.50m	£7m	£5m	£1m	£10m	£1m
£5,882	2014/15 Basic State Pension	Newly included group: 1.46m	£6m	£4m	£1m	£10m	£1m

Notes:

1. Source: DWP Modelling.
2. Estimates are expressed in 2014/15 earnings terms.
3. Scenarios after the baseline present the change in costs and accompanying demographic effects as compared to the baseline.
4. Figures are rounded to the nearest £10 million and £1 million, as appropriate to reflect uncertainties associated with the modelling approach used, and therefore may not sum exactly. Similarly, demographic effects are rounded to the nearest 1 million, 0.01 million and 1 per cent, as appropriate.
5. The lower and upper limits of the qualifying earnings band are held constant at their 2013/14 levels of £5,668 and £41,450 respectively.
6. Pension saving is the sum of employer contributions, individual contributions, and individual tax relief.
7. Demographic effects for gender have been estimated from the ASHE and from the LFS for ethnicity and disability. ASHE estimates are for the eligible target population and LFS estimates relate to the eligible population.

DWP analysis of the LFS suggests that the proportion of black and minority ethnic groups (BME) in the eligible population are 9 per cent with an earnings trigger of either £9,440 or £10,000; workers with a disability comprise 13 per cent of the eligible population under either trigger.

DWP analysis of the ASHE suggests that the median age of individuals in the eligible target population under a £9,440 trigger is 38 years compared to 41 years for the private sector as a whole. This indicates that there is a slightly higher proportion of younger workers in the eligible target population. This pattern does not change when the earnings trigger is set at £10,000.

Table 3 shows that the age breakdown of the eligible target population changes very little with changes in the value of the earnings trigger. Around one quarter (26 per cent) of individuals belonging to the eligible target population is aged 22 to 29 under either the £9,440 or the £10,000 earnings trigger. Around one in twenty (4 per cent) is aged 60 to 64.

Table 3: Age breakdown of the eligible target population under different earnings triggers

	2014/15earnings trigger	
Age	**£9,440**	**£10,000**
22 – 29	26%	26%
30 – 39	26%	27%
40 – 49	26%	26%
50 – 59	18%	18%
60 - 64	4%	4%

Notes:

1. Figures are for all private sector workers aged between 22 and the state pension age.
2. Figures are rounded to the nearest 1 per cent, and therefore may not sum exactly.

The changes under consideration for the 2014/15 review are not expected to particularly affect individuals according to their sexual orientation, religion or belief.

Impact of changing the lower limit of the qualifying earnings band in 2014/15

Table 4 shows the impact on employers, individuals and Government associated with retaining the 2013/14 lower limit of the qualifying earnings band in 2014/15 and various options considered for the value of the 2014/15 qualifying earnings band lower limit.

Increasing the lower limit of the qualifying earnings band to the 2014/15 level of the National Insurance Contributions Primary Threshold of £7,956 would reduce the level of pension saving in 2014/15 by around £190 million when compared to the baseline lower limit. Around £90 million of this reduction would be due to reduced employer contributions; around £70 million would be due to reduced contributions from individuals; and around £20 million would be due to reduced tax relief on individuals' contributions.

Increasing the lower limit of the qualifying earnings band to £5,732 (broadly in line with the growth in average earnings) would reduce the level of pension saving in 2014/15 by around £5 million when compared to the baseline lower limit of £5,668.

Table 4: Estimates of the impact of changing the lower limit of the qualifying earnings band on employers, individuals and Government (£ million, in 2014/15)

Lower limit of the QEB (in 2014/15 terms)	Factor	Employer Contributions	Individual Contributions	Individual Tax Relief	Level of Pension Saving	Employer Tax Relief
£5,668 (baseline)	2013/14 National Insurance Contributions Lower Earnings Limit; current qualifying earnings band lower limit	£690m	£550m	£160m	£1,390m	£60m
£5,772	2014/15 National Insurance Contributions Lower Earnings Limit	-£6m	-£5m	-£1m	-£10m	£0m
£5,732	2013/14 threshold increased by estimated earnings inflation (AWE)	-£3m	-£2m	-£1m	-£5m	£0m
£7,956	2014/15 National Insurance Contributions Primary Threshold	-£90m	-£70m	-£20m	-£190m	-£7m
£5,882	2014/15 Basic State Pension	-£9m	-£7m	-£2m	-£20m	-£1m

Notes:

1. Source: DWP Modelling.
2. Estimates are expressed in 2014/15 earnings terms.
3. Scenarios after the baseline present the change in costs as compared to the baseline.
4. Figures are rounded to the nearest £10 million and £1 million, as appropriate to reflect uncertainties associated with the modelling approach used, and therefore may not sum exactly.
5. The earnings trigger and the upper limit of the qualifying earnings band are held constant at their 2013/14 levels of £9,440 and £41,450 respectively.
6. Pension saving is the sum of employer contributions, individual contributions, and individual tax relief.

Impact of changing the upper limit of the qualifying earnings band in 2014/15

Table 5 shows the impact on employers, individuals and Government associated with retaining the 2013/14 upper limit of the qualifying earnings band in 2014/15 and various options considered for the value of the 2014/15 qualifying earnings band upper limit.

Increasing the upper limit of the qualifying earnings band to the 2014/15 level of the National Insurance Contributions Upper Earnings Limit of £41,865 would add around £3 million to the level of pension saving in 2014/15 when compared to the baseline upper limit of £41,450.

Increasing the upper limit of the qualifying earnings band to £42,569 (in line with consumer price inflation) would add around £8 million to the level of pension saving in 2014/15 when compared to the baseline upper limit of £41,450.

Table 5: Estimates of the impact of changing the upper limit of the qualifying earnings band on employers, individuals and Government (£ million, in 2014/15)

Upper limit of the QEB (in 2014/15 terms)	Factor	Employer Contributions	Individual Contributions	Individual Tax Relief	Level of Pension Saving	Employer Tax Relief
£41,450 (baseline)	2013/14 National Insurance Contributions Upper Earnings Limit; current qualifying earnings band upper limit	£690m	£550m	£160m	£1,390m	£60m
£41,865	2014/15 National Insurance Contributions Upper Earnings Limit	£1m	£1m	£0m	£3m	£0m
£41,919	2013/14 threshold increased by estimated earnings inflation (AWE)	£2m	£1m	£0m	£3m	£0m
£42,569	2013/14 threshold increased by estimated price inflation (CPI)	£4m	£3m	£1m	£8m	£0m

Notes:

1. Source: DWP Modelling.
2. Estimates are expressed in 2014/15 earnings terms.
3. Scenarios after the baseline present the change in costs as compared to the baseline.
4. Figures are rounded to the nearest £10 million and £1 million, as appropriate to reflect uncertainties associated with the modelling approach used, and therefore may not sum exactly.
5. The earnings trigger and the lower limit of the qualifying earnings band are held constant at their 2013/14 levels of £9,440 and £5,668 respectively.
6. Pension saving is the sum of employer contributions, individual contributions, and individual tax relief.

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