Description of policy
To reduce the automatic enrolment (AE) earnings threshold from £10,000 to the Lower Earnings Limit (£5,772 for 2014-15). This policy proposal is taken from a speech given by Rachel Reeves, Shadow Work and Pensions Secretary, at the Resolution Foundation on 29 May 2014 in which she said: '… *But this government have been unpicking this consensus in various ways. One way is by raising the qualifying threshold to £10,000, meaning that workers have to earn over £4,000 more in order to be automatically included. The result is a growing gap in the coverage of auto-enrolment and a significant compromise to the system's inclusiveness and integrity. It means that 1.5 million workers are being left out – a fall of around 10 per cent in the number of people the scheme was intended to cover, carving out from the system a large number of low paid and part time workers and those doing more than one job – precisely those whom the system was originally intended to help.'* *'…When it comes to the auto-enrolment threshold, the government say that people with low earnings would save too little for it to be worthwhile and this is the basis of Steve Webb's argument today that joining a workplace pension scheme "would not be the right option" for people in this position. I have to say it is quite a state of affairs when we have a pensions minister who says that 1.5 million low paid workers should not be saving for a pension*.' '*So Labour wants to bring those 1.5 million workers back into workplace saving. We will consult with employers, trade unions and pensions experts about the best way of doing it - including whether any change should be phased in, and how best to minimise administrative complexity. Any additional costs in pension tax relief resulting from this move, which the House of Commons Library estimates to be in the region of £20m a year, will be covered by savings found elsewhere in the social security budget, for example, the reduced cost of appeals that we expect to result from the reforms to the Work Capability Assessment that Kate Green and I set out last month.'*
Additional policy assumptions
Special Advisers have asked officials to make the following assumptions for the purpose of costing this proposal: - that the proposal is to lower the earnings threshold for automatic enrolment in a workplace pension scheme; - that the threshold would reduce from its current level of £10,000 to the Lower Earnings Limit for National Insurance which is currently set at £5,772; and - to provide a costing based on a range(s) between £5,772 and £10,000 as appropriate

Additional technical modelling assumptions or judgements required
To model the impact on the Exchequer of this proposal we have assumed that the opt-out rate (the number of those eligible for automatic enrolment who opt-out of their workplace scheme) is 28%. This is the basis on which all automatic enrolment programme costings have been made to date. Note that on 11 April 2014 DWP published a revised opt-out assumption of around 15 per cent over the lifetime of the programme, along with revised high level estimates of the numbers of people they anticipate to be newly saving or saving more as a result of automatic enrolment. However, the cost model is currently under development to incorporate the revised opt-out assumption. This work is not likely to be completed before the autumn, and the model (including this costing) will need to be quality assured in line with Departmental guidelines before any robust results can be published.
If needed, information required on distributional effects of the policy
No assumptions on the distributional effects are required to cost this policy.

Cost/Revenue to the Exchequer over five years

Additional annual costs for £5,772 trigger vs £10,000 trigger[1]

	Exchequer cost (£ million)	Employer contribution (£ million)
2015/16	3	9
2016/17	4	12
2017/18	10	26
2018/19	21	47
2019/20	26	56

The table above sets out the estimated annual costs to the Exchequer, and the total value of employers' contributions, associated with the mandatory contributions in each tax year up to 2019/20 (when the programme reaches steady state) from reducing the automatic enrolment earnings threshold from £10,000 to £5,772.

Note that DWP have assumed that employers will offset 50% of the costs arising from additional pension contributions for employees automatically enrolled. This is set out in DWP's impact assessment which was published in 2012[2].

The costs rise for two reasons: i) because of the staged implementation of automatic enrolment and; ii) increases in the minimum contribution rates from both the worker and the employer (which both attract tax relief). Auto-enrolment is being rolled out up until 2018 from the largest employers to the smallest so the number of people saving in to a pension scheme (and attracting tax relief on contributions) will increase up to 2018. In addition, contributions are currently set at a total of 2% of qualifying earnings with at least 1% from the employer. From October 2017, this will increase to a total of 5% of qualifying earnings with at least 2% from the employer. From October 2018, the minimum contribution will be 8%, with 3% from the employer.

These costs are based on the latest available version of the DWP's cost model. Results from this version of the cost model have been published in the past, most recently on 17 December 2013 as part of the annual review of automatic enrolment thresholds.

Distributional effects (if none requested, any significant):

Reducing the automatic enrolment earnings threshold from £10,000 to £5,772 would mean that an additional 1.7 million workers would become eligible to be *automatically* enrolled in to their employer's workplace pension scheme, of which 1.2 million would be women.

Comparison with current system (if applicable):

The Current System

Under the current system, the earnings trigger for automatic enrolment in to a workplace pension is £10,000 for 2014-15. At this level, a worker is eligible to be

[1] 2013-14 terms

[2] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/220202/ia-workplace-pension-reform-july-2012.pdf

automatically enrolled in to their employer's workplace pension scheme. However, anyone earning below this level but above the Lower Earnings limit (LEL) can ask to be enrolled and receive an employer contribution to their pension – they are just not *automatically* enrolled. The DWP Secretary of State is required to carry out a review in each tax year and may then revise the trigger by Order taking into account: the prevailing thresholds for National Insurance contributions; PAYE personal allowance; basic state pension, inflation and any other factors that the Secretary of State considers relevant. So far, the annual reviews have concluded that the earnings trigger should be aligned to the income tax Personal Allowance. It is important to note that the new State Pension will mean that the majority of people working today can expect to receive around £7,700 in retirement from the state. The Pension Commission benchmark replacement rate for people earning less than around £10,000 is 80%. The majority of people earning below £10,000 will therefore meet the Pension Commission's benchmark replacement rate. Automatically Enrolling workers who earn less than £10,000 would mean that many would be foregoing income in working life only to exceed the benchmark in retirement. <u>The Proposed System</u> Under the proposed system, the earnings trigger for automatic enrolment in to a workplace pension scheme would be set at £5,772. Minimum contributions only begin from earnings over £5,772 which would mean employers deducting trivial sums, literally in the pennies, to send over to the pension scheme. Automatically enrolling someone with earnings of £6,000, for example, would mean their qualifying earnings would be £228 – leading to minimum savings of around £5 per year or less than 10p a week (while minimum contributions are 2% in total).
Other comments (including other Departments consulted):
This policy proposal has been costed by DWP who are the departmental lead on automatic enrolment, and has been cleared by Jeremy Moore, Director General.

To be completed by Permanent Secretary's Office Date costing signed off:	6 June 2014
[If applicable] Date revised costing signed off:	