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Employer Briefing - Proposed UK Pension changes from 2012

Although 2006 saw significant changes in pension legislation, there are more major reforms on the horizon which will affect everyone in employment whether or not they are currently in a pension scheme. There are also cost implications for employers and the aim of this briefing is to provide an overview of the proposals as they currently stand.

Automatic enrolment

From 2012 the Government intends ensuring that every employer provides a company pension for their employees.

The proposals are intended to encourage employees to save for a pension on top of what the State provides. At present, many employers do not offer a pension scheme, and even where they do, many employees choose not to join.

As an employer it is likely that you will have to pay pension contributions for more staff members which will increase your costs. Every employee aged between 22 and State Pension Age who earns more than around £5,000 a year will be automatically enrolled in either the company scheme or the Personal Account (see below) when they begin working.

These contributions will be made via a new national pension scheme known as the “Personal Account”. It is intended that this will be a low-cost scheme offering a limited fund choice.

Employees will have the right to opt out of the scheme, but they will be automatically re-enrolled after 3 years unless they elect to opt out again. Evidence shows that automatic enrolment will lead to a far higher take-up of pension membership even if only through inertia. Automatic enrolment will not occur for anyone over the State Pension age, and all employees will have the right to join the scheme up to age 75.

Personal Accounts

- 8% of pay between around £5,000 and £33,000 would go into the scheme.
- 3% from the employer,
- 4% from the employee
- 1% from basic rate tax relief.
- Either party would be free to contribute more – up to certain limits which are yet to be announced.

Employer contributions will be phased in from 2012 to 2014 and small employers will get help with the costs in the early years.

Self-employed people will also be able to save into the Personal Account, as will non-earners to a limit of £3,600 a year.

State Pension Scheme

Changes are also proposed to the state pension scheme. Some of these (such as the equalisation of state pension age for men and women) are already enacted and there remains a number of further proposals still in the planning phase.

Changes to State Pension Age ("SPA")

State Pension Age is currently 65 for men and 60 for women.

However, SPA for women is changing - it will rise gradually from age 60 to 65 from 2010 to 2020. From 6 April 2020, the SPA for both men and women will be 65.

It is proposed that the SPA for both men and women will increase from 65 to 68 between 2024 and 2046, with each change phased in over two consecutive years in each decade.

- *First increase:* from 65 to 66, will be phased in between April 2024 and April 2026
- *Second increase:* from 66 to 67, will be phased in between April 2034 and April 2036
- *Third increase*: from 67 to 68, between April 2044 and April 2046

The changes to the State Second Pension ("S2P")

S2P could provide someone retiring this year with an additional weekly pension of £146. Most people however, only received a fraction of that.

It is intended that it will be changed from an earnings-related pension to one that is flat-rate. This change will be phased in gradually but should be completed by 2030.

The earnings link

It is proposed to restore the link between State Pension and annual earnings rather than increasing the pension in line with inflation. As earnings have historically risen faster than prices, this should lead to a real increase in value of the State Pension.

The Government has set a target date to make this change of April 2012, "subject to affordability", but warns that it might be delayed to "the end of the next Parliament", which could be as late as 2015.

Pension credits

Whilst these are controversial, it is not at present intended to replace the system of topping-up inadequate state pension benefits. This has implications for older employees who have made little of any personal provision for old age. In a significant proportion of cases auto enrolment may not be to their advantage.

This briefing is intended for information purposes only. It does not constitute advice and should not be relied upon in isolation. The opinions and views herein are based on our understanding of the proposals at the time of writing [June 2008].

Reference to taxation is based on our understanding of current HMRC law and practice. Taxation law is subject to change. The value of any relief or benefit is dependent upon individual circumstances. Past performance must not be taken as an indication of future performance. We strongly recommend you seek independent financial advice before taking, or refraining from taking action.