AUTOMATIC ENROLMENT FACT SHEET 4: ALTERNATIVE CONTRIBUTION BASES

THE STANDARD QUALITY TEST FOR AUTOMATIC ENROLMENT IS BASED ON QUALIFYING EARNINGS, HOWEVER MANY SCHEMES WILL PREFER TO USE A DEFINITION OF PENSIONABLE PAY FOR THE CALCULATION OF CONTRIBUTIONS. THE ALTERNATIVE CONTRIBUTION BASES ALLOW FOR THIS, PROVIDED THAT THE MINIMUM REQUIREMENTS ARE ADHERED TO.

When an employer's staging date is reached, eligible jobholders must be enrolled into an automatic enrolment scheme: either at the staging date, the deferral date if postponement is used or when the worker becomes an eligible jobholder.

One of the minimum requirements for an automatic enrolment scheme is that the employer must contribute a minimum amount in respect of each eligible jobholder or non-eligible jobholder that opts in. The standard contribution basis is a contribution of at least 3% of qualifying earnings from the employer, with the remainder – up to a total minimum contribution of 8% – paid by the employee. There is no minimum contribution for the employee, so the employer could pay 8% and the employee nothing.

Before October 2018, the minimum contributions are being phased in gradually. Before October 2017, the minimum total contribution must be at least 2% of qualifying earnings with at least 1% paid by the employer. From October 2017 to September 2018, this will increase to 5% of qualifying earnings with at least 2% paid by the employer.

WHAT ARE QUALIFYING EARNINGS?

This is a band of earnings determined each year by the Department for Work and Pensions (DWP) consisting of the following:

- salary;
- wages;
- commission;
- bonuses;
- overtime;
- statutory sick pay;
- statutory maternity pay;
- ordinary or additional statutory paternity pay;
- statutory adoption pay.

The assessment of whether a payment constitutes qualifying earnings is done by the employer.

The employer must assess the level of qualifying earnings of relevant staff in the pay reference period to determine what category of worker they fall into e.g. eligible jobholder, non-eligible jobholder or entitled worker.

If the employer is using qualifying earnings to calculate the contributions under the scheme, they must be based on earnings between the lower and upper limit of the qualifying earnings band or the equivalent figures for the pay reference period.

Employers that do not currently provide a pension scheme for their staff may want to provide a scheme using this standard contribution basis, although they could offer different schemes and possibly different contribution bases to different segments of their workforce. Employers with existing schemes may have difficulty meeting the standard contribution test as existing members may make contributions based on a definition of pensionable pay. In recognition of this, employers are able to certify their scheme as meeting one of three alternative contribution requirements or 'sets', all of which are based on pensionable pay.

The three sets are as follows:

Set 1. A minimum total contribution of 9% of pensionable pay, with at least 4% paid by the employer. Pensionable pay must at least equal basic pay. As with the standard contribution basis there is no specified minimum contribution for the employee, so the employer could pay the total minimum and the employee nothing.

The second and third sets allow lower minimum contributions but provided pensionable pay is equal (or at least equal) to a fixed percentage of earnings:

Set 2. A minimum total contribution of 8% of pensionable pay, with at least 3% paid by the employer. If this basis is used, pensionable pay must be at least 85% of earnings – either at member level or as an average across the scheme membership.

Set 3. A minimum total contribution of 7% of pensionable pay, with at least 3% paid by the employer. If this basis is used, all earnings must be pensionable, which amounts to a minimum contribution based on total earnings.

As with qualifying earnings, the minimum contributions under the alternative bases are being phased in before October 2018. Details may be found in The Pensions Regulator's detailed guidance: **http://www.thepensionsregulator.gov.uk/docs/dg-4-appendix-b.pdf**

There is also a fourth option. Employers using a basis different to those listed above can, through examination of pensionable pay and contribution data for its employees, certify that the scheme is at least as good as one based on qualifying earnings.

A contribution basis defined by reference to pensionable pay is a helpful alternative for employers who would otherwise have difficulty amending their existing scheme to ensure compliance with Pensions Reform legislation. However, amendments to an existing scheme may still be necessary (particularly to the definition of pensionable pay) to ensure the scheme meets at least one of the three sets, or the fourth option.

If more than one set is met (e.g. a required total minimum contribution of 9% of total earnings, which would meet all three sets) the scheme would certify their scheme against the set that is most appropriate to them. For example, if they would like flexibility to reduce minimum total contributions to 7% at some point in the future, they would choose set 3. If they plan to amend the definition of pensionable pay in the future to exclude some earnings, then set 1 may be more appropriate.

SEGMENTING THE WORKFORCE

Alternative contribution bases will also be relevant for employers who intend to offer membership of different schemes to different groups of workers.

Meeting automatic enrolment obligations is likely to result in increased costs for employers, in some cases ruling out the possibility of widening existing scheme membership to cover all jobholders. The use of an alternative scheme for those that do not qualify for membership of the existing scheme – perhaps on an alternative contribution basis – may help them to keep costs to a minimum. This could be done by segmenting the workforce and making contributions based on a definition of pensionable pay for members of the existing scheme and perhaps a GPP (using the standard contribution basis) for those who are not in the main scheme.

Example

Basso Ltd's staging date is 1 August 2014. It currently offers an occupational pension scheme to most of its staff requiring an employee contribution of 4% and an employer contribution of 5%. The contributions are based on the scheme's definition of pensionable pay, which includes almost all earnings (about 95%). The employer decides to retain the existing scheme and certifies it against Set 1.

Basso Ltd has a number of other eligible jobholders who must also be automatically enrolled on 1 August 2014. They decide to set up a GPP using the standard contribution basis and complete all the relevant agreements to ensure the regulatory requirements are met.

The company may alternatively decide to use another scheme such as The Peoples Pension for those members who do not go into the occupational scheme.

THE PHASING IN OF THE ALTERNATIVE CONTRIBUTION BASES

As with the standard contribution basis, the minimum contributions are to be phased in, allowing employers to adapt gradually to the increased costs:

	Set 1		Set 2		Set 3	
Time Period	Employer	Total	Employer	Total	Employer	Total
Until 30 September 2017	2%	3%	1%	2%	1%	2%
1 October 2017 – 30 September 2018	3%	6%	2%	5%	2%	5%
1 October 2018 onwards	4%	9%	3%	8%	3%	7%

Every care has been taken to ensure that this information is correct and in accordance with our understanding of the law and HM Revenue & Customs practice, which may change. However, independent confirmation should be obtained before acting or refraining from acting in reliance upon the information given.

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