Mattinson Ginty & Partners (Employee Benefits) Limited

A Guide to...

Personal Accounts - 2012 - Update 1

Special points of interest:

- Auto-enrolment
- Employer Contribution of 3%
- Employee Contribution of 4%
- Tax Relief of 1%
- Penalties for Non-Compliance

This is our second guide to Personal Accounts following the one issued in November 2008.

The Pensions Act 2008 put into law the reforms to the private pension system set out in the White Paper "Personal Accounts : a new way to save" published in December 2006.

From 2012 it will be COMPULSORY for all EMPLOYERS to contribute to a pension scheme for eligible employees.

All eligible workers, who are not already in a qualifying scheme, will have to be automatically enrolled into either their employers' pension scheme or a new 'national' pension scheme, currently known as "Personal Accounts".

To encourage participation, employee pension contributions will be supplemented by contributions from their employer and also an element of tax relief.

From 2012, all employees will be eligible for auto-enrolment unless:

they are already in a qualifying workplace pension scheme,

they are under the age of 22, or

they earn less than £5,035 a year (in 2006/2007 tax year)

Employees can 'opt-out' but only once they have been auto-enrolled and the process is quite complex. Any employee who opts-out must be auto-enrolled again 3 years later.

Auto-enrolment is the responsibility of the employer and not the Government. A Government body with substantial powers is being set up to ensure employer compliance.

Employer Pension Compulsion from 2012

Non-compliance could lead to a fine of up to £50,000 and a possible 2 year prison sentence.

Employers will be required to provide eligible employees with sufficient information about the pension scheme at the same time as auto-enrolling them into the scheme. Employers must not, however, give any advice to employees.

It will be the employer's responsibility to check which employees are eligible on a continuous daily basis.

Contribution Levels

The contribution levels have now been confirmed and are:

A minimum of 8% of qualifying (band) earnings

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This is made up of:

3% Employer

4% Employee, and

1% from the Government in the form of tax relief

It is proposed that contributions will be phased in as follows:

Year 1
1% Employer
1% Employee
0.25% Tax Relief
Year 2
2% Employer
3% Employee
0.75% Tax Relief
Year 3
3% Employer
4% Employee
1% Tax Relief

Tax relief at source will be added to all employee contributions at basic rate. In year 3, this will amount to 1% of band earnings.

In reality, the seemingly even handed '8% of band earnings' is anything but, as the first £5,035 p.a. is ignored.

If you earn £33,540, the 8% equates to 6.8% of actual earnings. If you earn £5,036 p.a., however, the 8% equates to 0.000016%

The Options

Employers will have three options in terms of a qualifying scheme.

Option 1 Personal Accounts Scheme

This will be the default scheme should an employer not have a qualifying workplace scheme.

The scheme will be run by a Government appointed body - yet to be decided - but in the process of being set up by PADA (Personal Accounts Delivery Authority).

The scheme will be an Occupational Pension Scheme with low charges - level yet to be confirmed - with a minimum contribution of 8% of band earnings as explained above.

Contributions will be limited to £3,600 per annum (based on 2005 earnings levels) and transfers in and out will not be permitted. This could be a problem for higher earners or people with other paid-up pensions.

Automatic enrolment applies to all employees over 22 with earnings over £5,035 per annum.

It is not yet clear which types of funds will be available for investment and what choice employees will have. It is thought they will be basic and restricted in number.

At retirement only a lifetime annuity with an Open Market Option is likely to be available.

Due to the low charging structure it is not clear how employers and employees will be able to receive assistance and/or advice in relation to Personal Accounts.

Option 2 Qualifying Workplace Scheme

Employers will be able to self-certify their own scheme as a qualifying scheme if it can pass a quality test. The scheme can be an Occupational or Personal Pension based scheme.

The minimum contribution will again be 8% of band earnings but there is nothing to stop an employer funding this in full. The maximum an employee can be asked to pay is 4% of net banded earnings.

The scheme must be available to all employees aged between 22 and State Pension Age with earnings above £5,035.

Automatic enrolment applies on the day an employees becomes eligible and the cost of advice can be factored into the scheme.

Investment funds and options can be tailored to the scheme and transfers in and out will be permitted.

Contributions will only be limited by the Annual or Lifetime Allowances.

At retirement, all the flexible options will be available.

Option 3 Quality Qualifying Workplace Scheme

This type of scheme will enable an employer to postpone the auto-enrolment process by 90 days.

The minimum contribution will be set at 11% of banded earnings with at least 5% coming from the employer. On full earnings of £33,540, the minimum contribution will be 9.35% with the employer paying at least 5.1% of full earnings.

Investment funds and options can be tailored to the scheme and transfers in and out will be permitted.

Contributions will only be limited by the Annual or Lifetime Allowances.

At retirement, all the flexible options will be available.

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MGP's View

You cannot afford to ignore these changes.

The Government has taken on board the lessons of Stakeholder where employers set up arrangements that were not promoted and people did not join. The Government will not allow Personal Accounts to suffer 'death by apathy' as happened with Stakeholder.

If you have a scheme already in place you should take steps to ensure it is at least a Qualifying Workplace Scheme and where possible we would recommend a Quality Qualifying Workplace Scheme as this will ease the administrative burden that would otherwise exist.