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9 January 2015

Alison Evans
Department for Work and Pensions
Automatic Enrolment Programme
1st Floor Caxton House
London SW1H 9NA

Dear Alison

Technical changes to automatic enrolment

I am writing on behalf of the Association of Consulting Actuaries (ACA) in response to the above consultation document issued on 1 December 2014.

Our comments on the specific questions you raised are set out in three Appendices to this letter. From this you can see the following:

- **Alternative quality requirements for defined benefit schemes** – we support the intention behind the proposal in relation to section 23A(1)(b) of the Pensions Act 2008, although are surprised at the lack of detail in relation to the testing which we understand is deliberate. We have strong concerns over not proceeding with proposals under section 23A(1)(a).
- **Information requirements for employers** – we are supportive of the proposed changes but are not convinced that you will fully achieve two of your three stated policy objectives.
- **Exceptions to the employer duty** – we welcome all these changes and make some suggestions to improve them further.

We hope that you find our comments of assistance and would be happy to discuss them further if that is helpful. Please contact either me on 020 7432 6635 (david.everett@lcp.uk.com) or my colleague, Jane Beverley on 020 3327 5314 (jane.beverley@puntersouthall.com).

Yours sincerely

David Everett
Chairman
ACA Pension Schemes Committee

Sent by e-mail to: Automaticenrolment.consultation@dwp.gsi.gov.uk

APPENDIX 1

Alternative quality requirements for defined benefits schemes

We welcome the intention behind the proposal in relation to section 23A(1)(b) of the Pensions Act 2008, but are a little surprised at the lack of detail in relation to the testing which we understand is deliberate. Although this does present risks, we understand that you are of the view that they are unlikely to crystallise. The regulations will be subject to review in 2017 when this issue can be addressed if necessary.

We suspect that, from 6 April 2016, section 23A(1)(b) will be the route of choice for those schemes that class as defined benefit but which cannot pass on the test scheme standard without calculations (ie the nature of their benefits is such that a "documentation check" cannot be carried out by the employer). So the most important thing, to our mind, is that the regulations are finalised and in place by 6 April 2015.

We understand the reasons for not proceeding with proposals under section 23A(1)(c).

We have strong concerns over not proceeding with proposals under section 23A(1)(a).

We now turn to the proposal in relation to section 23A(1)(b).

The level of the cost of accruals test

***Question 1**: Does the level of the alternative test deliver broad equivalence with the Test Scheme?*

We have no reason to suggest that the proposed level does not deliver broad equivalence, for a typical membership profile on typical scheme funding (ie prudent) assumptions under current market conditions. We acknowledge that broad equivalence with the test scheme, rather than the money purchase quality requirements (which are likely to be weaker) is appropriate.

We note that unlike the test scheme there is no additional requirement for the revaluation requirements of the Pension Schemes Act 1993 to be applied in relation to those who leave service before normal pension age, nor do the indexation requirements of the Pensions Act 1995 have to be applied. We don't see this as a drawback as, where relevant, the scheme's benefits will be subject to these requirements in any event.

The definition of 'relevant earnings'

***Question 2**: Will these variations be helpful to employers? Are they still valuable even though they add some complexity to the test? How many employers do you think will take advantage of these variations?*

Yes. It is right that the same variations available in relation to money purchase schemes should also be available to defined benefits schemes. We do not see them adding any complexity to the test – rather they give appropriate choice to select which works best for a scheme, especially if the check can be carried out by reference to already determined figures. We think that most employers sponsoring defined benefits schemes will take

advantage of the variations, particularly the 11% of pensionable earnings test (where pensionable earnings are not less than basic pay).

The definition of 'relevant period'

***Question 3**: Does this definition meet the needs of schemes? Are there scenarios where this definition would create additional work for schemes/employers? Is the default period of 12 months an appropriate period for schemes which may not have an actuarial valuation or control period?*

We leave it to others to comment on the needs of public service pension schemes. In relation to other defined benefit schemes, linking to *"the most recent written report, prepared and signed by an actuary, valuing the scheme's assets and determining its liabilities"* will not necessarily pick up the latest report in which the cost of providing the benefits accruing has been determined. We ask that the regulations refer to this rather than where assets and liabilities have been valued.

We find it very strange that the only reference to an actuarial report in the draft regulations is in the definition of relevant period. There is no requirement to use this report for the actual numbers. It seems odd that the wording would allow you to use pretty much any cost of accrual number you would like (including those not found in any already issued report), but you would be tied to using the relevant period in the most recent written report. We say more about this in our response to Question 5.

We are content with 12 months as a period for schemes which may not have an actuarial valuation or control period, but the regulations also enable 12 months to be chosen for all non-public service pension schemes. We are not sure if this is intended but do not object to it.

The definition of 'relevant members'

***Question 4**: Does this definition fit with existing practice? Are there any circumstances in which it would cause problems or additional work?*

We are content that the definition of relevant members is set to be the active members of the defined benefits scheme. However, unlike the test scheme which must be passed in relation to the active members of the employer in question, it is not clear to us whether the test applies across all employers. As you will be aware, the cost of accrual tends to increase with age, so it might be possible that if one carried out the test at the employer level, an employer that had a very young workforce would fail, despite offering exactly the same benefit accrual as other participating employers. It seems to us that the test should be applied across all employers. If this is your intention, can you make this clear in your response to the consultation?

In relation to applying the test to parts of a scheme, whilst the policy intention is clear (to apply the test at the level of benefit scales) the wording in the draft regulations *("different benefits are calculated by different methods"*) does not seem to deliver the intention. So, for example, a scheme that has a 1/80ths and a 1/100ths benefit scale is delivering different benefits but by the same method and so each scale would not seem to need to

be assessed separately. We acknowledge that the wording you are proposing is similar to that for the Reference Scheme Test[1] but suggest that you use wording along the lines of *"different benefit scales are used"*. There would still need to be judgment as to when a different scale was being employed. Another possibility might be *"benefits are accruing on materially different terms"*.

Given that your intention is that the test is carried out by reference to already published material this may not be possible where the most recent scheme funding report did not identify the contributions theoretically required for each of the different benefit scales. As each scale would have passed the reference scheme test and the actuary is under a continuing duty to monitor this until 5 April 2016, a transitional arrangement under which the testing doesn't have to be carried out for each benefit scale until the next scheme funding report is available would be highly desirable.

The methods and assumptions to be used

***Question 5**: Are there any risks in not prescribing methods and assumptions? Does this provide an incentive to select methods or assumptions which enable a scheme to meet the test where it otherwise might not?*

There are risks if you don't provide, through the regulations, some more detail on the intended meaning of *"the cost of providing the benefits accruing for or in respect of the relevant members"*. Although your working assumption is that actuaries will use methods and assumptions already used for other purposes, such as in scheme funding, being silent within the regulations might create pressure to adopt an "actuarially strong" method and set of assumptions in order that a sub-standard set of benefits will pass. However, we understand that you are of the view that this risk will not materialise.

Given that your proposed percentages are based on typical scheme funding assumptions one possibility would be to regulate to ensure that the method and assumptions to be used are not "actuarially stronger" than those used in the most recent scheme funding report in order to value the scheme's assets and determine its liabilities. (The cost of accrual disclosed in the valuation report may have been determined on other assumptions.) This could be by making reference to the scheme's most recent Statement of Funding Principles, together with such further assumptions as are necessary, but also enable the calculations to be undertaken on the basis of appropriate updates – ie using the language that is used in the test scheme.

Although in theory the issue you have is the opposite of that in the Occupational Pension Schemes (Power to Amend Schemes to Reflect Abolition of Contracting-out) Regulations where you need to ensure that an "actuarially weak" set of assumptions is not used to validate an excessive reduction in benefit accrual / increase in member contributions, in practice we think it unlikely that existing schemes will game the system so that sub-standard benefits pass the test.

[1] At paragraph 5 of Schedule 3 to the Occupational Pension Schemes (Contracting-out) Regulations 1996.

Benefits to be included/disregarded

***Question 6**: Does this fit with existing practice and provide simplicity? Are there any circumstances in which it would cause problems or additional work?*

There are risks that in being silent in this area benefits may be included in order to achieve a pass for the benefit structure. There may also be legal uncertainty as to the meaning of *"benefits accruing"*. Does it include discretionary benefits for example? Does it include expenses? If you choose to regulate for some exclusions, then, if you look to the wording within the test scheme standard[2], lump sum death benefits and money purchase benefits are potential candidates for exclusion from the section 23A(1)(b) test.

We assume your intention is that the test reflects the intended benefits going forwards which might differ from those at the most recent scheme funding valuation. The regulations are silent on this.

Actuarial certification

***Question 7**: Are there any particular risks in not requiring an actuary to explicitly certify that the scheme meets the cost of benefit accruals test?*

We do find it odd that you are not intending to legislate for a requirement to certify when the test scheme standard requires it. A possibility is that the regulations provide that if the test can be met by reference to already published material then the employer is able to certify; otherwise an actuary should certify. You could use the same language as set out in Regulation 39(2) and (3) of the Occupational and Personal Pension Schemes (Automatic Enrolment) Regulations 2010 (which relates to the test scheme).

Other comments on the proposed section 23A(1)(b) test

Most schemes that wish to take advantage of this test will not class as a "defined benefits scheme" as not all the benefits provided under them will be defined benefit. We have not examined whether the Hybrid Schemes Quality Requirements Rules 2012 under which such schemes will be tested can be read so that where there are references within these Rules to applying the defined benefit quality requirements, they will also pick up the section 23A(1)(b) test. Hopefully this has already been achieved through section 24(1)(b) making reference to section 23A, but the Rules need to be checked.

We find it odd that there is no requirement to keep any "pass" under section 23A(1)(b) under review. On the face of it, benefit accrual could be severely cut back without any need to retest. This is unlike the test scheme where the review requirement is set out in the statutory guidance. You may wish to include something along the lines of this review requirement within the regulations if you feel that this is a risk.

[2] at regulation 39(4) of the Occupational and Personal Pension Schemes (Automatic Enrolment) Regulation s 2010

Other alternative quality requirements

***Question 8**: Are there schemes which: cannot use the alternative proposed; could not demonstrate appropriate quality via the shared risk route; and should be allowed to satisfy the money purchase quality requirement? If so, what are they and how could they be prescribed?*

There are some money purchase-like schemes that class as defined benefit under the auto-enrolment legislation, but which find it difficult to use the test scheme standard and are likely to find it difficult to use the alternative now being proposed. It is not possible to comment on whether they will be able to demonstrate the required quality under the shared risk route because you have yet to develop it (this presumably requiring the complete reworking of the Hybrid Schemes Quality Requirement Rules 2012 in which there will no doubt be other issues to address). Furthermore, our understanding is that your aim is to commence this part of the Pension Schemes Bill (and associated regulations) by 6 April 2016. So even if once developed, the shared risk route can be used, it will be too late for those employers who need to stage by 6 April 2016 (broadly employers with less than 30 employees). As a result, they may have moved away from their existing scheme, quite possibly to an inferior one. We are aware of at least one multi-employer organisation that has been put in this position over the last year and whose larger employers, on reaching their staging dates, have had to go forward with a scheme that is inferior to the one in which they were participating, in order to be compliant with the auto-enrolment legislation.

There are a number of reasons why the alternative proposal is unlikely to be of assistance to money purchase-like schemes. The most fundamental of course is that it is not being designed with these schemes in mind. Also, the price is significantly higher than 8% of qualifying earnings.

There are two types of money purchase-like schemes affected (with any doubt as to their status being removed on 24 July 2014 by the Bridge Regulations):

- a scheme providing conversion terms for contributions, such as through running an internal “with profit” deferred annuity structure; and

- a scheme providing a guarantee on investment performance during the accumulation phase.

Whilst they are subject to the scheme funding requirements, the nature of such valuations is very different to that of a final salary pension scheme. There is no concept of benefit accrual in these money purchase-like schemes to which can be attached a cost of accrual. Instead there is an agreed level of contributions and the purpose of the valuation is to determine whether a surplus or deficit has arisen in relation to the benefits awarded from the past payment of contributions. Such schemes are likely to be designed and managed in such a way that they should generate a surplus, so the decision for the trustees following the valuation is what bonus can be safely awarded on accrued benefits and for this purpose, valuation results may be produced on a variety of bases.

It might be possible for such schemes to work out a notional cost of accrual. In the deferred annuity structure the scheme actuary could place a value on the amount of the deferred annuity bought by the agreed annual contribution, making prudent assumptions as to future investment returns, but allowing for the possibility of not receiving bonuses. This would then be compared against (say) 11% of pensionable earnings. But such an approach would be rather circular and at best could end up with a contribution rate greater than that required of money purchase schemes. It would certainly not fall out of existing calculations as is the intention for a final salary pension scheme.

As this matter is not straightforward there might need to be guidance to explain how the regulations expect non-final salary pension schemes to be treated.

If (in relation to a particular contribution scale) the section 23A(1)(b) test needs presumably to be passed in relation to an employer's active members, rather than in relation to the active members of all the participating employers taken together, there is a possibility that as the sort of calculation we have outlined above might produce different results at different ages, some employers might fail whilst others may pass despite the contribution rate actually paid being the same. This is illogical. This issue would be resolvable if it were possible to use the conversion basis to work out the cost of accrual – a 10% contribution would then have a 10% cost of accrual. This, of course, would be possible if you choose to remain silent on the method and assumptions (but see our answer to Question 5).

Section 23A(1)(b) also does not enable these money purchase-like schemes to benefit from the phasing of contributions allowed to money purchase schemes.

Our concern is that, following informal consultation, through the Pensions Act 2014 you have legislated under section 23A(1)(a) of the Pensions Act 2008 for schemes of a prescribed description to pass so long as they meet one of the money purchase quality requirements. We think that you should now deliver on this promise by specifying these prescribed descriptions, rather than asking such schemes to go down the potentially more onerous and certainly non-intuitive section 23A(1)(b) route.

We believe that the language would be relatively simple and look something like the following:

(1) For the purposes of section 23A(1)(a) of the Act (alternative quality requirements for UK defined benefit schemes), the following schemes are prescribed:

(a) A scheme that provides conversion terms for contributions either as the sole basis of benefit calculation, or in combination with other interest or bonus payment terms; or

(b) A scheme that provides a guarantee on investment performance during the accumulation phase.

We ask that at the very least you legislate along these lines for a holding period (ie until at least 6 April 2016 by when you should have developed the shared risk approach).

***Question 9**: Are there circumstances in which an individual level cost of accrual test would provide a simpler way to demonstrate compliance with the DB quality requirement?*

We understand your reasons for not proceeding with an individual level cost of accrual test as provided for in section 23A(1)(c) of the Pensions Act 2008.

Information requirements for employers

We are supportive of the proposed changes. The Pensions Act 2008 delivered a complex web of employer duties on which the information requirements were built on a piecemeal basis. Some while ago these requirements were consolidated within Schedule 2 to the regulations which was welcome in itself. It now makes sense to revisit the information requirements in order to simplify them further, particularly in the light of small and micro-employers staging. However, we are not convinced that you will fully achieve the first two of your three stated policy objectives (reducing the employer's obligation to make an assessment of all categories of employees and facilitating one individualised communication which suits all circumstances). Although you say that employers will be able to continue with the existing information requirements if they wish to, we suspect that the effect of your changes will be such that many employers will wish to revisit and potentially adjust their communication materials and processes.

Amending existing regulations

***Question 10**: Does revoking regulation 17 and amending regulation 21 reduce the practical burden of information requirements for employers?*

Amalgamating (and reducing) the information requirements so that there no longer needs to be a distinction between the information sent to jobholders that have not been auto-enrolled and workers without qualifying earnings is useful, but employers will still need to be able to distinguish between the two types of worker who may potentially opt in given that the employer duty varies between them.

It may well be useful for an employer to issue information to these workers at the same time as its auto-enrolment duties arise in relation to other employees, but this is possible under the current regulations.

***Question 11**: Will these amendments enable the employer to combine the information to employees within a single communication and remove the need to assess on a continuous basis?*

It would seem possible under the current regulations to issue a single communication that encompasses the enrolment information and that which must be supplied to those who have a right to opt in. But in this event the precise nature of the employer duty to the recipient would need to be signalled as it could vary between recipients.

Although under the proposals it would be possible to issue a single communication, we feel that many employers will wish to continue to distinguish between those for whom they are under an immediate duty to auto-enrol and those who have a right to opt in.

We don't understand the reference to removing the need for the employer to assess his employees on a continuous basis. As far as we can see the employer duty will need to be applied to all new recruits and so is continuous in this respect. Those who have the right to opt in, but have not done so, will need to be subject to continuous monitoring to the extent that they might in future meet the conditions for the employer duty to apply.

***Question 12**: Will employees receive the information that they need at the right time?*

The proposals don't seem to prevent employees from receiving the information they need at the right time.

***Question 13**: Does amending these regulations reduce the practical burden of information requirements for employers?*

The current information requirements for postponement of auto-enrolment are unnecessarily complex, containing as they do slight variants on the information being required in four situations. Requiring the same four pieces of information to be supplied across all the situations is a very welcome simplification and should go some way to reducing the practical burden of information requirements for those employers who choose to postpone.

***Question 14**: Will employees receive the information that they need at the right time?*

The proposals don't seem to prevent employees from receiving the information they need at the right time.

***Question 15**: Would the removal of the notice under regulation 33 reduce the practical burden of information requirements for employers?*

Yes. The need to communicate auto-enrolment related information to those workers who are already a jobholder and an active member of a qualifying scheme is unproven and so the revoking of this information requirement should be most welcome, especially for those employers who already operate a scheme of sufficient quality. It is a shame that this requirement has been in place during the period in which the employers of many employees already in pensionable employment have reached their staging date as work-arounds have had to be explored.

***Question 16**: Is it agreed that the notice under regulation 33 serves little purpose and can be removed without any risk to employees?*

We agree that the current requirements are superfluous.

Amendment of the detailed requirements in Schedule 2 to SI 2010/772

***Question 17**: Would the removal of paragraphs 2 and 3 be welcome and help get away from individualised communications thereby reducing administrative costs for employers?*

We think that it is the reworking of paragraph 1 and the removal of paragraph 2 that will make possible the provision of enrolment information on a standardised basis (which is welcome). The information in paragraph 3 would appear to only need to be individualised to the extent that the employer intends to auto-enrol workers into one of a number of qualifying schemes.

***Question 18**: Are there any risks to the employee in not receiving the information in paragraph 2?*

No – we agree that the employee does not need to know the date of enrolment as part of the enrolment information, but only so long as his or her enrolment date is communicated to him or her at a later date.

***Question 19**: Is there a risk that the employee may not receive the information in paragraph 3 from another source?*

Not really – this scheme information is likely to be contained within a scheme booklet that is typically supplied to the new member in order to meet the Basic Scheme Information requirements of the Disclosure Regulations. However, we note that these regulations do not in fact require the name, address, telephone number and electronic contact details of the scheme to be supplied.

***Question 20**: Although the draft regulations make no change to paragraph 10 of schedule 2, would further details of where the opt out notice may be obtained be useful for employees?*

We are not aware that there is a need to bolster this provision. Knowing from where the opt out notice can be obtained should be sufficient.

***Question 21**: Does amending these paragraphs of schedule 2 reduce the practical burden of information requirements for employers?*

Whilst we don't object to any of the proposed changes mentioned immediately before this question was posed in the consultation document, we don't believe they will deliver much by way of reduction in the burden of information requirements for employers.

***Question 22**: Is the new consolidated paragraph 18 clear enough to both types of employee (jobholder and worker) who will need to distinguish whether they fit into paragraph 18(a) or 18(b)?*

It is clear enough for the purpose. If there is any confusion, it can be picked up as part of the opting in process.

***Question 23**: If the actual figure for qualifying earnings under section 13(1)(a) PA 2008 is not provided in the statement in paragraph 18, is there a risk that employees will not understand the requirements and may stay out of pension saving?*

There is clearly a danger that not supplying the current level of the lower limit of the qualifying earnings band could lead to confusion and for this reason we suggest that the amount should continue to be stated.

***Question 24**: Does the removal of this paragraph strike the right balance between reducing the load on employers and placing the onus on the employee to find out more information about pension saving?*

In the context in which it is being supplied it is not clear what purpose is served by having a requirement to state where to obtain further information about pensions and savings for retirement, nor is it clear how far an employer has to go to meet this obligation, so we welcome its removal.

Reducing the pieces of information coming from an employer

***Question 25**: Is the aspiration of 3 communications realistic and workable?*

We cannot reconcile your proposals with the three types suggested – in particular we are not sure what you intend falls under (iii), you have not counted the jobholder information that the employer must supply to the trustees, nor the information that must be supplied on deferral for employers with defined benefit or hybrid schemes. And we have doubts as to whether the enrolment information would be combined with that which needs to be supplied to those who can opt in, but are not being enrolled.

***Question 26**: Will the overall proposed changes to the information requirements bring simplicity to the automatic enrolment process and with it a reduction in administration and costs for employers? If so, what is the average saving for an employer due to a reduction in the administrative burden?*

The proposals will lead to some simplification and as such should reduce administration and employer costs in the long term, but in the short term there will be costs incurred in simplifying processes that have already been put in place. However we are unable to provide you with any cost estimates.

***Question 27**: How many employers do you think will take advantage of these changes?*

We are unable to answer this question.

***Question 28**: Can these changes be communicated to employees within existing material?*

Yes, if you mean existing material that is compliant with the current requirements of the regulations.

***Question 29**: Is there any risk that the overall consequence of these amendments may cause confusion or detriment to the employee?*

We see no reason why this should be so.

Exceptions to the employer duty

The Pensions Act 2008 presents the employer duty in very stark terms and with the benefit of hindsight as well as operational running it is clear that the Act needed amendment to provide for exceptions. We welcome the proposal to turn the employer duty into a power in certain situations and acknowledge the need for such a power to be subject to limitations.

Jobholders leaving employment

***Question 30**: Do you think that this will be a helpful exception, particularly for small and micro employers? If not, why not?*

It is clearly helpful to turn a current employer duty to apply the auto-enrolment requirements to those leaving employment into a power to apply these requirements, thus enabling employers to do whatever is appropriate, which in most cases will be not to auto-enrol, or to stop an auto-enrolment process that has yet to complete. It enables the employer to do the sensible thing, rather than be hamstrung by regulations.

***Question 31**: How many employers do you think will take advantage of this exception?*

We suspect that the vast majority of employers will take advantage of this exception.

***Question 32**: Can this exception be communicated to employees within existing material?*

We would envisage the exception being incorporated within the employer's normal communications to employees who are leaving employment and in any Staff Handbook.

***Question 33**: Can you foresee any difficulties with removing opt-in rights during notice periods for either employers or individuals?*

No.

***Question 34**: In your experience, how frequently is notice withdrawn? Do you think that turning the duty back on in withdrawal cases will cause any problems for employers or employees? If not, why not?*

Whilst the withdrawal of notice is not uncommon we are unable to give an indication of its frequency. We welcome the proposal that the duty is turned back on from the date that the withdrawal of notice is agreed between employer and employee, thus avoiding the need to rush through an auto-enrolment process.

***Question 35**: Do you think that this exception should be extended to other 'end of employment' situations, for example where a fixed term contract is coming to an end? What do you think the advantages or disadvantages would be to this approach?*

We are not persuaded that there is a need to extend the exception to where a fixed term contract is coming to an end and note the potential use to which postponement can be put. If you were to extend to fixed term contracts you would need to set a cut off within which the duty would turn into a power, such as within three months of the contract end date.

Cancelling membership of a scheme prior to automatic enrolment

***Question 36**: Do you think this exception will help to simplify the automatic enrolment process for employers, particularly small and micro employers?*

It is inappropriate for the legislation to subject an employee to an auto-enrolment process if only recently they have cancelled their scheme membership following a contractual enrolment process. So we welcome the proposal to turn the employer duty into a power in this situation. However, it won't necessarily simplify the automatic enrolment process as such individuals will still need to be identified in order to establish whether the power applies to them.

***Question 37**: Do you agree that applying this exception to all people who have left a qualifying scheme (as opposed to just contract joiners) will simplify the process for employers?*

Yes.

***Question 38**: Can you foresee any negative consequences for employers or employees?*

No.

***Question 39**: Do you think that 12 months is a suitable timeframe for restricting the exception?*

If you take the view that contractual enrolment is broadly equivalent to auto-enrolment and that opting out would generally take place very quickly, given that automatic re-enrolment would occur, broadly speaking, after a further three years, 12 months seems to be an unnecessarily short time frame. As no justification has been put forward for 12 months, we suggest that you increase it. Such an employee will still have the right to opt in.

***Question 40**: How many employers do you think will take advantage of this exception?*

Although we cannot estimate how popular this exception will be, we suspect that it will be attractive to employers.

***Question 41**: Can this exception be communicated to employees within existing material?*

Existing contract joining material would need to be adjusted. Alternatively it could be signalled to an employee when they cancel their scheme membership.

***Question 42**: Do the benefits of this exception outweigh the risks of people being left out of pension savings for up to 3 years?*

We do not see a risk as such given that the power only applies where an individual has elected to leave a scheme. Moreover, we understand that the right to opt in remains but this needs to be clearly communicated to affected individuals.

Individuals with tax protected status

***Question 43**: Do you think the exception should be this wide or restricted to certain protections, for example only where further pension accrual could jeopardise an employee's tax status?*

Our priority concern is that the new provisions cover the cases where the nature of the Lifetime Allowance protection held by the individual is one which can be jeopardised by accrual – so currently Enhanced Protection (EP), Fixed Protection (FP) or Fixed Protection 2014 (FP14) – because the sums put at risk for such members just by their doing nothing under the current auto-enrolment mechanics can be substantial.

However, we see no harm in the regulations covering individuals with the other Lifetime Allowance protections listed and the proposed approach may be simplest to manage.

But the exception list does need to be kept under review and will need to be added if in future there are further changes to the pension tax regime and new types of (vulnerable) tax protections arise. Is there any way a power can be put in now to enable that to be done easily?

We also suggest a further widening of the regulations as worded. Could *"where the employer has reasonable grounds to believe that one of the following provisions applies"* have the last word replaces with *"has ever applied"*? The current wording means the employer looks at the current status of the individual's protection, and if there is some reason to believe that the member may have lost the protection already then the employer power doesn't exist. That brings complexity and extra work to the test. Our proposal would mean that the employer can simply rely on information as to whether the member registered for protection (this seems a good enough test for policy intent as it suggests the member had large enough pension savings at that point to want to protect them). If it transpires that the member has already lost protection and might then be happy to be enrolled, then they can make this clear to the employer.

We very much support the wording using its current broad phrases *"reasonable grounds to believe"* as this ought to mean that the duty does not apply (being replaced by a power) even where the employer is not in possession of a copy of any tax protection certificate –

for example, where the employer has been informed by the employee that there is a tax protection certificate, or an application has been made for one.

***Question 44**: Will the proposed exception as drafted help reduce the administrative burden and costs for employers by allowing these employees to be kept out of the automatic enrolment process altogether? If so, what is the average saving for an employer due to a reduction in the administrative burden?*

Employers who have already reached their staging date may well have introduced procedures to manage people with tax protection to ensure they are not accidently auto-enrolled. These have not been simple – they have had to be carefully managed in order to ensure the employer is not seen as inducing the individual not to join the pension scheme – and with the prospect of re-enrolment creating this issue again.

Handling the auto-enrolment and immediate opting out of senior employees with tax protections is a time intensive process because of the need to communicate complex pension rules to senior people who are very short of time and the need to get those senior people to comply with strict deadlines that may clash with urgent business activities such as overseas business trips. The proposals would mean a useful saving of management time by pension managers who would probably welcome the extra time to spend on making the auto enrolment process and the employer's retirement schemes better for the other 99% of the workforce at whom auto-enrolment is aimed.

And also what is saved is the potential for ill-feeling at the beginning of an employment relationship and the amount of management time that might be needed to address a case where there is a failure to stop/unwind an auto-enrolment process in time.

We are unable to provide an estimate of the average saving for an employer.

***Question 45**: How many employers do you think will take advantage of this exception?*

It may be that relatively few employers employ affected individuals – but the number has grown since the first designs of auto-enrolment because the 2014 tax law changes brought in a whole new tranche of individuals with vulnerable protections.

We would expect **all** employers who do have such employees to take advantage of this exception for the reasons stated above.

***Question 46**: Can this exception be communicated to employees within existing material?*

There is likely to be a strong desire to communicate the exception within whatever material is used to commence a pension scheme joining process and we believe that it would be relatively easy to do so.

***Question 47**: Is the proposed exception a welcome easement for employees who have tax protected status?*

Yes, because the tax consequences for individuals with EP or FP12/FP14 who are auto-enrolled and do not take action to opt-out in time are likely to be substantial.

***Question 48**: Does the benefit of having this exception for employers outweigh the risk to employees receiving no information about their right to opt in?*

The principal benefit is to the employee rather than the employer. Such individuals will already have significant pension savings and are likely to be in a position to make their own choices about retirement provision, so if it is in their interests to opt in they may well still do so, notwithstanding their not receiving any communication about this.

On joining a company, employers would provide employees (or prospective employees) with details of the pension plan and how they can opt-in/out, etc. We would expect a reasonable employer to keep their employees informed of their benefit options frequently throughout their employment, but we do not feel that it should be a legislative requirement to continually inform employees (with tax protection) of their right to opt-in.

However, having said this we cannot see where you are removing the information requirement for such individuals. It seems to continue to apply via the amended Regulation 21.

***Question 49**: Does placing the onus on the employee and the proposed changes to HMRC and TPR guidance sufficiently deal with the practical problem of the employer knowing of the individual tax status as well as what the employee needs to do?*

We support the fact that the legislation relies on the employer having reasonable grounds for belief rather than the actual fact of protection – the latter would place an unworkable and disproportionate burden of investigation on the employer. The consultation note helpfully confirms that the construction means that it is "for the employee to make the fact known to the employer".

The changes in HMRC and TPR material will be essential. In practice some employers may be proactive in asking about protection status at key moments such as recruitment. Although individuals with protection should be aware that it is valuable and that certain actions can lose them protection, our experience is that there are often misunderstandings or lack of awareness unless individuals are helped/reminded/warned at vulnerable times. (That is why continuation of the power to opt out is so key for individuals with protection who may not have informed their employer of their protection status or whose employer may for some reason still choose to enrol the member.)

The construction of the provision appears specifically such that where the employer chooses still to exercise the power and so an individual with EP etc is auto-enrolled, that would count as a statutory enrolment such that the member can opt out within one month and count for tax law (and indeed all other purposes) as not having joined the scheme so that the EP etc is not compromised. It would be helpful if this could be explicitly confirmed in all guidance material.

Winding up lump sums (WULSs)

***Question 50**: Do you think this exception provides a useful easement for employers as well as a sensible protection from unwanted tax charges for the employee?*

Draft regulation 5E para 1(b) appears incorrectly written. The WULS is paid by the pension scheme, which is not the *"person mentioned in sub-paragraph 1(c) of paragraph 10"* [of Schedule 29 to Finance Act 2004]. The person in referred sub-paragraph 1(c) is the employer. So this needs change – perhaps replace the start of (b) with *"at the time of the payment, there was an entity that counted as a person …"*.

It is a shame that the issue cannot be solved by changing some of the tax law conditions (we have lobbied for this with HMRC); but, subject to the above point, the proposal is helpful in allowing the employer to fulfil the undertaking made to HMRC when the WULS was paid and hence maintaining the WULS as an authorised payment.

***Question 51**: How many employers do you think will take advantage of this exception?*

We are unable to answer this question.

***Question 52**: Can this exception be communicated to employees within existing material?*

It could be something trustees can include in the material sent when the WULS is paid, as to what might apply if the individual happens to leave and be re-employed in the next 12 months. Employers may choose to remind individuals at re-employment why they are not being sent a joiner pack etc – also mentioning that although they do still have the choice to opt-in early there will be tax implications for their WULS.

***Question 53**: Does the benefit of having this exception for both the employer and employee outweigh the risk of some people being left outside of pension saving for a period of what could be 3 years?*

The employee will have the right to opt in after the 12 months period has elapsed (when the risk of the WULS being unauthorised disappears) which can be made clear in the communication material.

***Question 54**: Does the benefit of having this exception outweigh the risk to employees receiving no details or confirmation of their employer's lawful decision not to automatically enrol them?*

Given the circumstances we suspect that the employer would wish to communicate the position to the affected employees.

***Question 55**: To what extent are WULSs being paid out by employers to employees who continue to be employed by them? If they are why, having regard to the tax rules on paying WULSs?*

Yes. It is common for trustees to pay WULS to members who are still employees of an employer which was in the past a contributing employer. There are many schemes that

are no longer appropriate for accrual and are closed and eventually wound up, with the intention perhaps that other pension arrangements are set up instead. Provided the wind-up is more than five years after closure, WULS can be offered to all members (and potentially less than five years in some cases). On wind-up, paying a WULS can generate some cost saving compared to eg persuading the member to accept a transfer to the new proposed arrangement (or one of their choice) or if not arranging transfer to a buy-out.

So the present tax rules (intended to stop abuse) means that WULS can sometimes only be used for this innocent purpose if wind-up is delayed for five years after closure. It would be helpful if HMRC could soften their WULS conditions in cases where it is clear abuse is not intended.

Taking a pension income using Flexible Drawdown

***Question 56**: Do you think an exception for employees who flexibly-access their pension rights would be welcomed by employers or considered appropriate given the proposed changes to the tax rules from next April?*

We suspect that this issue will need to be addressed at some future point, but suggest that the regulations are not held up on account of seeking to build in an exception for flexible drawdown.

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