Employee Benefits In The UK: Pensions

The UK employee benefits market has never seen as much change as it has over the last few years.

Compulsory employer pensions provision (which began in 2012 under the guise of automatic enrolment) has affected all employers, while taxation changes, legislation targeting higher earners, and new ways of saving are all making the employee rewards space an exciting place to be. Alongside this, there's an improving nationwide recognition of the importance of wellbeing both in the workplace as well as out of it.

For this first article, we are concentrating on pensions, and their role in UK employee benefits.

Auto Enrolment

Introduced in October 2012, initially for larger employers, The Occupational and Personal Pension Schemes (Automatic Enrolment) (Amendment) Regulations (2012), state any employer with one or more employees must enrol their staff into a qualifying workplace pension scheme within three months of them joining. Any new companies established in the UK now need to comply with this regulation as soon as they employ their first employee.

All companies, both existing and start-ups, need to make sure they understand their legal duties and comply with them on an ongoing basis to avoid any financial penalties being imposed from The Pensions Regulator (TPR). However, understanding which employees need to be automatically enrolled into the scheme has caused some confusion for multinational employers since this legislation came into effect.

Why? Well, The Pensions Act 2008 defines eligible jobholders as "ordinarily working in the UK". However, TPR says other factors should also be considered when considering whether an employee falls into the scope of this legislation, such as:

- Where the employee begins and ends their work
- Where their private residence is, or intended to be
- Where the employer's headquarters are
- Whether the employee pays National Insurance tax in the UK
- What currency the employee is paid in.

These factors are particularly important where employees are not based in the UK, or regularly move between countries.

Tax Reliefs

As this legislation has been phased in, we have also seen legislation introduced limiting some of the traditional pension tax reliefs for 'high earners'. For example, over the last few years, all individuals paying into a UK pension scheme have been able to claim tax relief on their contributions of up to £40,000 per annum, known as the 'annual allowance', subject to their having sufficient UK relevant earnings to do so.

However, since April 2016, individuals who have an 'adjusted income' (total taxable income plus the value of any employer pension contributions) for a fiscal year of more than £150,000 could have their annual allowance for that year restricted. That means for every £2 of income that exceeds £150,000, £1 of their annual allowance would be lost. Despite this, there is a cap on this reduction – if adjusted income exceeds £210,000, the minimum annual allowance will be no lower than £10,000.

Clearly, this complicates things for high earners, especially in assessing how much they can contribute in a tax-efficient manner to their pensions. It's even harder if their income varies or derives from multiple sources.

Pension Freedoms

Despite the introduction of mandated employer pension schemes, the single biggest change in recent times is the 'pension freedoms' legislation. Employees have the option of taking some of their pensions savings as a tax-free sum when they retire, while the rest can be used to create income. These new freedoms mean an individual can take any amount of their pension savings out when they reach the earliest retirement age – currently 55 – subject to relevant tax rules.

However, there is concern a lot of individuals do not understand the tax implications and long-term consequences of their actions. The Personal Finance Society, for example, warned in an interview last year that most pension drawdowns are being transacted before consulting a financial adviser, and that consumers are raiding their pension pots prematurely[1]. Further, the Financial Conduct Authority said 72% of pension pots have been accessed by the under 65s, with 55% of them being completely withdrawn[2].

This has resulted in some employers wanting to improve communication and support for the employees affected. For many employers, their pension scheme is their largest cost after base pay, yet, arguably, it has always been difficult in the UK to engage staff with it. Further, according to our own 2018 Employee Benefits Insight Report, an overwhelming 83% of employers said financial education was something their employees would value and benefit from, while 43% said they were concerned workers were not making adequate provision for retirement.

Conclusion

We all now have access to a diverse range of financial products, as well as those offered as part of an employee benefits package – but many people simply do not know their options or how best to manage their financial goals. With the increasing freedoms around pension monies and financial choice comes the need for more financial information and education so people can make the right decisions. EB packages need to understand that, too.

References:

1 *'Pension warning: Thousands 'at grave risk' of running out money in retirement', Daily Express, 5 June 2018*

2 *FCA, Retirement Outcomes Review, June 2018*

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