# Summary: Intervention & Options

| Department /Agency: | Title: | |
|---|---|---|
| **HMT/HMRC** | **Impact Assessment of the National Insurance Contributions Bill 2007** | |
| **Stage:** Final Proposal | **Version:** | **Date: 5 November 2007** |
| **Related Publications:** | | |

**Available to view or download at:**

http://www.hmrc.gov.uk

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What is the problem under consideration? Why is government intervention necessary?

The Budget 07 announcement that National Insurance Upper Earnings Limit (UEL) is to be aligned with the income tax higher rate band from April 2009 will affect State Second Pension (S2P) and contracted out NICs rebates both in terms of impact on the public finances and the intention of the reforms to S2P in the Pensions Act 2007. The Act includes a proposal to introduce an Upper Accruals Point (UAP) in 2012 to achieve flat rating of S2P by around 2030. Without intervention the Budget 07 changes will delay flat rating of S2P, and increase contracted out rebates and future S2P liabilities.

What are the policy objectives and the intended effects?

To align the UEL for NICs with the higher rate threshold for income tax.

To ensure that flat rating of S2P and a simpler state pension is still achieved by around 2030.

To keep state pension outcomes consistent with those agreed under pensions reforms as set out in the Pensions Act and accompanying White Paper.

To avoid additional S2P and contracted out rebates as a consequence of the increases to the UEL announced at Budget 2007.

What policy options have been considered? Please justify any preferred option.

1. Do nothing.
2. Introduce the UAP in April 2009 at the level of the 2008/09 UEL to achieve a flat rate S2P in 2031/32 (Chosen Option).
3. Introduce the UAP in 2010 and set the UAP at a lower level than the 2009/10 UEL to achieve a flat rate S2P in 2031/32.
4. Introduce the UAP in 2012 (or the date at which other pension reforms are introduced) and set the UAP at a lower level than the 2011/12 UEL to achieve a flat rate S2P in 2031/32.

When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects?

We will carry out a review of the compliance costs after the changes have bedded in, probably 1-3 years after implementation.

**Ministerial Sign-off**

***I have read the Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) the benefits justify the costs.***

Signed by the responsible Minister:

Kitty Ussher Date: 5 November 2007

# Summary: Analysis & Evidence

| Policy Option: 2 | Description: Introduce the UAP in April 2009 at the level of the 2008/09 UEL to achieve a flat rate S2P in 2031/32 |
|---|---|

## COSTS

| ANNUAL COSTS | | Description and scale of **key monetised costs** by 'main affected groups' |
|---|---|---|
| **One-off** (Transition) | **Yrs** | There will be an increase in employer's compliance costs resulting from changes in the P11/P14 required for this option; and a one-off cost reflecting training required by employers to implement the system. |
| **£ 30 million** | 1 | |
| **Average Annual Cost** (excluding one-off) | | |
| **£ 1 million** | | **Total Cost** (PV) £ |

Other **key non-monetised costs** by 'main affected groups'

## BENEFITS

| ANNUAL BENEFITS | | Description and scale of **key monetised benefits** by 'main affected groups' |
|---|---|---|
| **One-off** | **Yrs** | See table 1 for Exchequer savings - these are costs that would have otherwise been incurred in respect of increased State Second Pension rights and contracted out rebates as a result of the increases to the UEL in 2008/09 and 2009/10 also included in this Bill. |
| £ | | |
| **Average Annual Benefit** (excluding one-off) | | |
| £ | | **Total Benefit** (PV) £ |

Other **key non-monetised benefits** by 'main affected groups'

Key Assumptions/Sensitivities/Risks

That employers and HMRC can implement the introduction of the UAP for 6 April 2009.

| Price Base Year | Time Period Years | **Net Benefit Range** (NPV) £ | **NET BENEFIT** (NPV Best estimate) £ |
|---|---|---|---|

| | | | | |
|---|---|---|---|---|
| What is the geographic coverage of the policy/option? | | | GB &NI | |
| On what date will the policy be implemented? | | | April 2009 | |
| Which organisation(s) will enforce the policy? | | | HMRC | |
| What is the total annual cost of enforcement for these organisations? | | | £ N/K | |
| Does enforcement comply with Hampton principles? | | | Yes | |
| Will implementation go beyond minimum EU requirements? | | | N/A | |
| What is the value of the proposed offsetting measure per year? | | | £ | |
| What is the value of changes in greenhouse gas emissions? | | | £ N/A | |
| Will the proposal have a significant impact on competition? | | | No | |
| Annual cost (£-£) per organisation (excluding one-off) | Micro | Small | Medium | Large |
| Are any of these organisations exempt? | No | No | N/A | N/A |

| **Impact on Admin Burdens Baseline** (2005 Prices) | | | (Increase - Decrease) |
|---|---|---|---|
| Increase of £ 1 million | Decrease of £ Nil | **Net Impact** | £ 1 million |

Key: Annual costs and benefits: Constant Prices | (Net) Present Value

# Evidence Base (for summary sheets)

## NATIONAL INSURANCE CONTRIBUTIONS BILL

### Rationale for Government Intervention

1. The personal tax package announced at Budget 2007 was never intended to give more State Second Pension benefits to higher earners and/or increase the contracted out rebates to higher earners and their employers. However, without intervention the alignment of the UEL with the higher rate tax threshold would result in a corresponding increase in the amount of State Second Pension and contracted out rebates available to higher earners and their employers. The Government is now taking steps to keep in line with its stated objectives for pension reform and the timetable for a simplified flat rate State Second Pension by around 2030.

### Purpose and Intended Effect of Measure

#### *The Policy Objective*

2. To ensure that:-

   - the Upper Earnings Limit for Class 1 National Insurance purposes is aligned with the point at which, higher rate income tax becomes payable, as announced in Budget 2007.
   - the Government's proposals for State Pension reform and simplification (as contained in the Pensions Act 2007) are still on target to be achieved by around 2030.

#### *Background*

3. The personal tax package that was announced in the Budget on the 21 March 2007 includes measures to align the National Insurance Upper Earnings Limit (currently £670 per week) with the point at which higher rate income tax is payable by April 2009. However, in order to achieve the alignment it is necessary to remove the link that exists in the Social Security Contributions and Benefits Act 1992 and Northern Ireland equivalent between the Primary Threshold (currently £100 per week) and the Upper Earnings Limit (UEL). Currently primary legislation restricts the power of the Treasury to make changes that increase the UEL to a figure greater than 7.5 times the Primary Threshold (PT). In order to align by secondary legislation the UEL with the point at which higher rate tax becomes payable in 2009 this link has to be removed.

4. National Insurance Contributions (NICs) rates and thresholds which include the Upper Earnings Limit are reviewed and where appropriate changed each tax year by reference to prices. Employers expect these changes. Payroll software and HMRC guidance are changed as a matter of course to reflect the new National Insurance rates and thresholds. The changes to the UEL announced in the Budget will not impose any increased burdens on employers as the changes will be reflected in the routine changes that are made to

guidance and software. An impact assessment is not necessary for the changes to the powers relating to the setting of the UEL.

5. The second element of the National Insurance Bill is concerned with the interaction of the Budget announcement with the Pensions Act 2007. This Act received Royal Assent on 26 July 2007 and introduced legislation to flat rate the State Second Pension which is paid on top of the basic State Pension and currently linked to an employees earnings up to the UEL. This was planned to begin in 2012 (at the earliest) and would take until around 2030 to be achieved. It requires the introduction of a new Upper Accrual Point (UAP) for State Second Pension to replace the UEL as the cap on the portion of a person's earnings that are used to calculate State Second Pension. The UAP was to be fixed (in cash terms) in due course by secondary legislation at the level of the UEL in the year of introduction. The UEL will still be used in the calculation of NICs and could still rise according to the usual indexation arrangements. The National Contributions Bill brings forward the date for introducing the UAP, to April 2009, and makes amendments elsewhere consequent on that change.

6. The remainder of this IA covers the impacts of the early introduction of the UAP announced by the Chancellor on 9 October 2007 in the Pre Budget Report and now included in this Bill.

**Class 1 NICs and State Second Pension – glossary**

7. Class 1 NIC are paid by employers and employees on earnings from employment and provide entitlement to the full range of contributory benefits. They also help fund the NHS. Class 1 contributions are calculated and paid over to HMRC by employers. They are made up of two elements. Primary contributions are payable by employees and secondary contributions are payable by employers. Employers deduct primary contributions from the earnings of their employees. There are various limits and thresholds that are used to determine the amount of NICs due on earnings and benefit entitlement. These include the following:-

   **Lower Earnings Limit (LEL)** is currently £87 per week and is the point at which the earnings count for benefit purposes. Those who earn below the LEL do not build up any entitlement to contributory benefits.

   **Primary Threshold (PT)** is currently £100 per week and is the point above which employees begin to pay Class 1 primary NICs. Although no primary Class 1 NICs are payable at or below the PT, those whose earnings are not less than the LEL but not more than the PT, are treated as having paid Class 1 NICs for contributory benefit purposes.

   **Secondary Threshold (ST)** is currently £100 per week and is the point at which employers begin to pay Class 1 NICs. The secondary threshold and the primary threshold are fully aligned.

   **Upper Earnings Limit (UEL)** is currently £670 per week and is the point at which primary Class 1 NICs cease to count for benefit purposes.

   Employers pay secondary NICs at a rate of 12.8% on all earnings above the ST. Employees pay primary NICs at a rate of 11% on earnings between the PT and UEL and at a rate of 1% on earnings above the UEL.

   Where an employer makes alternative arrangements for the provision of an earnings related pension to his employees through an occupational pension scheme, his employees are contracted-out of the State Second Pension. Since earnings between the Lower and

Upper Earnings Limit are linked with S2P entitlement that a contracted-out earner forgoes, primary and secondary Class 1 contributions are reduced. The reduction is currently applied by reference to the same LEL to UEL band of earnings.

**Upper Accrual Point (UAP)** prior to the introduction of the UAP, the upper earnings limit was the end point for state pension accruals. The UAP will replace the UEL as the new upper limit of State Second Pension accruals from April 2009. It will also be the point at which the contracted-out reduction ceases. Once set the UAP will not be up-rated.

**Lower earnings threshold** (**LET)** is currently £13,000 per year and relates to the State Second Pension only. It is the level of earnings up to which, under the current regime, State Second Pension accrues at the 40% rate and, under the simplified scheme as set out in the Pensions Act 2007 State Second Pension will accrue at the flat rate; and the amount of earnings a person is deemed to have if they earn above £4,524 but below the LET (£13,000) or they are accruing state second pension because they are a carer or are sick or disabled. The LET is increased annually in line with the growth in average earnings.

**White Paper** – referred to in this Impact Assessment is the Government White Paper published on 26 May 2006 *Security in retirement: towards a new pension system.* The White Paper set out the proposals that were taken forward in the Pension Act 2007.

## Options

8. We have considered four options in detail;
    1. Do nothing.
    2. Introduce the UAP in April 2009 at the level of the 2008/09 UEL (£770 per week) to achieve a flat rate S2P in 2031/32.
    3. Introduce the UAP in 2010 and set the UAP at a lower level than the 2009/10 UEL to achieve a flat rate S2P in 2031/32 (£775 per week under current projections).
    4. Introduce the UAP in 2012 (or the date at which other pension reforms are introduced) and set the UAP at a lower level than the 2011/12 UEL to achieve a flat rate S2P in 2031/32 (£775 per week under current projections).

<u>Option 1: Do Nothing.</u>

9. Doing nothing would mean the State Second Pension outcomes for some groups of future pensioners, in particular higher earners (those earning above the 2007/08 UEL of £34,840 in todays prices), would be higher than those intended under White Paper reforms to state pensions. Linked to this there would be anomalous gains in the contracted out rebates paid to employees and employers (or direct into pension schemes) as a consequence of the changes to the UEL also contained in this Bill. It would take until 2034/35 to achieve a simplified flat rate State Second Pension (under the White Paper this was set to be simplified by 2031/32).

10. There would be no impact on the exchequer costs of the State Second Pension and the Contracted Out rebates compared to the announcement at Budget 2007 to increase the Upper Earnings Limit, however significant Exchequer costs in relation to state pensions would be incurred compared to the White Paper package of reforms included in the RIA for the Pensions Act 2007 (www.dwp.gov.uk/pensionsreform/pdfs/pensions-bill-ria.pdf).

11. This option has been rejected on the basis that it would take longer to achieve a simplified State Second Pension and that it would incur exchequer costs above the White Paper package of reforms.

Option 2. Introduce the UAP in April 2009 at the level of the 2008/09 UEL (£770 per week) to achieve a flat rate S2P in 2031/32.

12. Bringing forward the introduction of the UAP to 2009/10, and fixing the UAP at the level of the UEL in 2008/09 (£770 per week) would bring the timescales for a simplified State Second Pension back in line with the White Paper (a simplified flat rate S2P by 2031/32 under current projections).
13. On the basis of the current RPI projections the value of the UEL would have been £775 per week in 2012/13 in the absence of the Budget 2007 announced increases to the UEL. This is sufficiently close to the 2008/09 value of the UEL to make a strong case for fixing the UAP at the 2008/09 level of the UEL to provide certainty for employers and software providers going forward. Delaying the introduction of the UAP beyond 2009/10 would require a reduction in the UAP compared to the previous years UEL to meet the White Paper timescales for a simplified flat rate S2P by 2031/32. Therefore introduction of the UAP in 2009/10 reduces potential disruption for individuals and employers that could arise from the value of the contracted out rebates needing to be reduced year on year.
14. Some individuals are likely to still see additional rights to State Second Pension (or higher contracted out rebates) built up between 2008/09 and 2012/13 as a result of the increases in the UEL announced at the Budget 2007.
15. This Option has been chosen as the most suitable option to meet timescales for state pension simplification whilst minimising disruption for individuals and employers. See Table 1 for impacts on Exchequer costs/savings for this option.

Option 3. Introduce the UAP in 2010 and set the UAP at a lower level than the 2009/10 UEL to achieve a flat rate S2P in 2031/32 (£775 per week under current projections)

16. This Option brings forward the introduction of the UAP to 2010/11. This would provide additional time for HMRC and employers to implement the necessary changes. However on the basis of current projections if the UAP were implemented from 2010/11 it would have to be set at a lower level than the 2009/10 UEL in order to meet the timescale for a simplified, flat rate State Second Pension by 2031/32. This could create disruption for individuals and employers as they could experience a reduction in the value of the contracted out rebates year on year.
17. Some individuals would still see additional rights to State Second Pension (or higher contracted out rebates) built up between 2008/09 and 2012/13 as a result of the increases in the UEL announced at the Budget 2007.
18. This option has been rejected on the basis that it would require the UAP in 2010/11 to be set below the level of the 2009/10 UEL when introduced.

Option 4: Introduce the UAP in 2012 (or the date at which other pension reforms are introduced) and set the UAP at a lower level than the 2011/12 UEL to achieve a flat rate S2P in 2031/32 (£775 per week under current projections).

19. This Option does not bring forward the introduction of the UAP but would require a reduction in the UAP at the time of introduction compared to the previous years UEL. Depending on the start date for other state pension reforms (including the earnings linking of the basic State Pension and the abolition of contracting out for members of defined contribution pension schemes) this could require an even larger reduction in the UAP compared to the previous years UEL to keep to timescales for a simplified State Second Pension by 2031/32.

20. If the UAP was introduced at the same time as contracting out for Appropriate Personal Pension and Defined Contribution schemes were abolished it may have been possible to have introduced amended P11 and P14 forms for employers with defined benefit pension schemes only at the point of introduction.

21. Some individuals would still see additional rights to State Second Pension (or higher contracted out rebates) built up between 2008/09 and 2012/13 as a result of the increases in the UEL announced at the Budget 2007.

22. This option has been rejected on the basis that it would require the UAP in 2012/13 (or the point of introduction) to be set below the previous years UEL when introduced.

**Table 1- Projected Exchequer Costs / Savings from introduction of UAP in 2009 (Option 2) compared to Do Nothing (Option 1).**

| | 2008/09 | 2009/10 | 2010/11 | 2020/21 | 2030/31 | 2040/41 | 2050/51 |
|---|---|---|---|---|---|---|---|
| Introduce the UAP in April 2009 at the level of the 2008/09 UEL | | | | | | | |
| Contracted Out Rebates | 0 | -300 | -430 | -890 | -920 | 0 | 0 |
| S2P | 0 | 0 | 0 | -30 | -130 | -320 | -540 |

Notes: £ million - 2007/08 prices (rounded to the nearest £10m). Figures for 2008/09-2012/13 are generated by HMRC medium-term model. Figures for 2020/21-2050/51 are generated by DWP long-term model. Underlying assumptions may differ slightly between models. For the April 2009 introduction the UAP is assumed fixed from there onwards at £770 per week (the announced level of the UEL for 2008/09). The savings shown are relative to a baseline where the UEL would have been increased above indexation in 2008/09 and 2009/10 as announced at Budget 2007, and indexed by RPI thereafter, with the UAP then introduced in 2012 and cash fixed (at the 2012/13 level of the UEL) as announced under White Paper pension reforms. The longer-term savings relate to the fact that the UAP then introduced in 2012 would have been at a higher rate than intended under pension reforms in each year until 2034/35 as a result of the Budget 2007 increases announced in the UEL.

## Sectors and Groups Affected

23. Ministers have announced that Option 2 (introduce the UAP in April 2009 at the level of the 2008/09 UEL) is to be implemented. Under current projections for earnings growth a simplified flat-rate State Second Pension will be achieved in 2031/32 once the LET reaches the UAP.

24. All employers will need to be aware of the introduction of the UAP because the P11/ P14s will be changed to include an additional earnings column. If the employer has employees earning below the new UAP whilst the P11/ P14 will look different it will not have any material effect on what information the employer needs to record.

25. The introduction of the UAP will require changes to the current design of the P11/ P14s or electronic equivalents which, in part, is used by employers to record earnings for National Insurance contribution and contracted-out employment purposes. The changes are required because changes are being made to the maximum level of earnings on which contributory benefit entitlement and contracted-out rebates are available. Currently the maximum level is set at the UEL but from April 2009 the maximum level will be set at the new Upper Accrual Point.

26. From 2009 employers that are:-

- Not contracted out employers will need to record and report earnings between the UAP and UEL separately for S2P calculation purposes. The additional information will also enable HMRC to calculate and pay over minimum contributions in respect of those employees who hold Appropriate Personal Pensions (APP).
- Contracted out employers will need to report earnings between the UAP and the UEL separately as those earnings will no longer attract a contracted-out rebate. Instead employees will be required to pay NICs at the not contracted-out rate of 11% on earnings between the UAP and the UEL and at the additional rate of 1% on all earnings above the UEL. Employers will be required to pay NICs at the not contracted-out rate of 12.8% on all earnings above the UAP. The additional information will also enable HMRC to calculate and pay over age related rebates to contracted-out money purchase schemes based on earnings up to the UAP.

The revised P14 will enable HMRC to undertake these calculations without the need to contact the employer for further information. It will also allow HMRC to validate that the correct amount of contributions have been paid.

27. We have not been able to identify an alternative other than to make changes to the P11/P14s in order to deliver the early introduction of the UAP. This change will require employers to provide the UAP information.

28. The format of form P11/ P14 will need to be changed from:-

**Current Layout of P11/P14**

| 1a | 1b | 1c | 1d | | 1e |
|---|---|---|---|---|---|
| Earnings at LEL( where earnings are equal to or exceed the LEL) | Earnings above the LEL , up to and including the ET | Earnings above the ET, up to and including the UEL | Total of employee's and employer's contributions | If amount in column 1d is a minus amount enter 'R' here | Employees Contributions due on earnings above the ET |

**New Layout of P11/P14**

| 1a | 1b | 1c | 1d | 1e | | 1f |
|---|---|---|---|---|---|---|
| Earnings at LEL( where earnings are equal to or exceed the LEL) | Earnings above the LEL , up to and including the ET | Earnings above the ET, up to and including the UAP | Earnings above the UAP, up to and including the UEL | Total of employee's and employer's contributions | If amount in column 1d is a minus amount enter 'R' here | Employees Contributions due on earnings above the ET |

## HMRC Costs

29. The introduction of the UAP is part of the wider state pension reforms included in the Pensions Act 2007 and was due to occur in 2012/13 or the date at which the basic State Pension is first linked to earnings. We now estimate that the earlier introduction of UAP in April 2009 will lead to HMRC IT costs of around £10 million based on having to have an additional column on the P14 and will require changes to the National Insurance Recording System and the online interface with employers as well as other system changes.

Additional staffing costs to handle guidance, queries and errors in completing the new forms are estimated at £650,000.

## Equity and Fairness

*Employers*

30. As the UAP will be a constant figure in cash terms it will serve over time to reduce the earnings on which entitlement to State Second Pension accrues. Therefore, initially the introduction of the UAP will only affect those businesses that have contracted out employees earning at or above the UEL because it will limit the amount available in contracted out rebates (Table 2 provides an illustration of the change in the contracted out rebates for an employer with a defined benefit pension scheme in respect of an employee). However the new UAP is also reflected in the State Second Pension so there will be no requirement for employees and employers to increase the benefits paid by their pension schemes in future in respect of higher State Second Pension contracted out equivalent rights. Typically around two thirds of the contracted out rebate savings will relate to rebates to employers and around one third to rebates to employees.

31. The change will affect all employers because all employers will need to be aware of the UAP and will need to record and report additional information in order that HMRC can make minimum payments for any employee who holds an APP (this is because the employer would not generally be aware of this fact).

32. For those employers using payroll software, the software will need to be changed to accommodate the additional information that needs to be recorded. The HMRC CD-ROM in the employer packs will include an updated P11 Calculator enabling employers not using payroll software to automate the necessary decisions and calculations, and this will help ameliorate the impact of this change on these employers. For those employers who are still using a manual payroll the employer will need guidance on completing the new amended P11 and P14s.

33. We estimate that there will be a one-off cost to employers of implementing these changes of around £30 million. There will be ongoing compliance cost increases for employers of £1 million (including manual payroll calculations in some cases) and acquainting themselves with the changes.

*Employees*

34. Bringing forward the introduction of the UAP to 2009 will only affect future rights to State Second Pension yet to be accrued. There is no impact on current pensioners or on State Second Pension rights already accrued. According to the latest Annual Survey of Hours and Earnings (2004) (ASHE) data the number contracted out with earnings above the UEL is estimated at 2.1 million. Based on the ASHE data we estimate that, of those;

- Around 88% are members of salary related (defined benefit) schemes
- Around 5% are members of money purchase schemes
- Around 7% are members of personal pension schemes

35. These individuals will either see a reduction in their take home pay (as they will get a lower rebate on their NICs than would otherwise have been the case) or a reduction in the money that goes into their pension scheme compared to not introducing the UAP until 2012/13. Although this represents a reduction in rebates compared with the post Budget 2007 position, individuals are still likely, in the period up to 2012/13, to receive more generous rebates than intended under the White Paper reforms. Table 2 below

shows that compared to the White Paper outcomes previously expected higher earners are still expected to receive higher contracted out rebates in the early years.

**Table 2 – Annual Contracted Out Rebates in 2009/10 for a higher earner in a defined benefit pension scheme (individual earning above the UEL/UAP so illustrating maximum impact of the changes)**

| | Net Employer NICs | Net Employee NICs |
|---|---|---|
| White Paper | £1,190 | £510 |
| Do Nothing | £1,420 | £610 |
| Introduce UAP in 2009 | £1,310 | £570 |

Notes: 'White Paper' figures are consistent with those used during the passage of the Pensions Act 2007 and would mean a UAP in 2012/13 of £763. 'Do Nothing' would mean a UAP of £899 in 2012/13 whilst 'Introduce UAP in 2009' would mean a UAP of £770 from 2009/10 onwards. Values for the UAP are given in cash terms. Annual contracted out rebates are in 2007/08 earnings terms (to nearest £10).

36. Over the longer term the early introduction of the UAP in 2009/10 would affect anyone who would have been building up higher S2P rights (or contracted out rights within their pension schemes) following the Budget 2007 announced increases to the UEL. The impact is likely to be very small, and individual outcomes will be similar to those intended under the White Paper reforms. Table 3 below shows that compared to the White Paper outcomes previously expected higher earners are still expected to see higher accruals in the early years and will see similar accruals over the longer term. The Do Nothing option would lead to anomalous gains in S2P accruals for higher earners.

**Table 3 – Annual State Second Pension Accruals for a higher earner (individual earning above the UEL/UAP so illustrating maximum impact of the changes).**

| | 2008/09 | 2009/10 | 2010/11 | 2020/21 | 2030/31 | 2040/41 | 2050/51 |
|---|---|---|---|---|---|---|---|
| White Paper | £2.18 | £2.14 | £2.00 | £1.88 | £1.52 | £1.50 | £1.50 |
| Do Nothing | £2.48 | £2.58 | £2.22 | £2.04 | £1.62 | £1.50 | £1.50 |
| Introduce UAP in 2009 | £2.48 | £2.38 | £2.09 | £1.88 | £1.52 | £1.50 | £1.50 |

Notes: 'White Paper' figures are consistent with those used during the passage of the Pensions Act 2007 and would mean a UAP in 2012/13 of £763. 'Do Nothing' would mean a UAP of £899 in 2012/13 whilst 'Introduce UAP in 2009' would mean a UAP of £770 from 2009/10 onwards. Values for the UAP are given in cash terms. Annual S2P accruals are in 2007/08 earnings terms.

## Social

37. There are no major social impacts, although the changes we are making will ensure that the reforms in the Pension Act 2007 (making State Second Pension flat rate from around 2030) can be met.

## Environmental

38. No environmental benefits are anticipated.

## Small firms Impact Test

39. Small employers will be affected by these changes. They will need to acquaint themselves with the new information required to complete the P11/ P14s especially if they choose not to use payroll software or the P11 Calculator on the CD-ROM. Small employers with staff earning below the current UAP will not be affected they will just need to be aware of the UAP and that if earnings of employees increase above the UAP they will need to use the additional column on the P11/ P14s for earnings between the UAP and UEL.

40. Of the annual increase in administrative burdens, the table below shows how this estimate is split between forms of different sizes. The distribution of administrative burden reflects the fact that micro-sized businesses make up the vast majority of employers and so they also bear the largest share of administrative burdens for measures such as this where the impact is per employer.

| Business size | Percentage of total admin burden |
|---|---|
| Micro | 87% |
| Small | 8% |
| Medium | 4% |
| Large | 1% |

**Competition Assessment**

41. We have applied the competition filter to the early introduction of the UAP and concluded that the policy is unlikely to raise any competition concerns.

**Equality Impact**

42. We have screened this change for equality impacts and do not believe that there are any adverse impacts that would require a full equality impact assessment. We are also confident that the measures do not impact on any of the equality based legislation such as the Human Rights Act or any of the Race Relations legislation (Race Relations Act 1976 & The Race Relations Amendment Act 2000). We are confident that there are no implications on Section 75 and 76 of the Northern Ireland Act 1998 which guarantee equality of opportunity in the Province.

**Securing Compliance**

43. Employers will be required to pay NICs based on the introduction of the UAP in April 2009 through changes to primary and secondary legislation. Guidance will be prepared by HMRC to inform employers of the changes in time for the April 2009. The Employer CD-ROM includes a payroll calculator which will be updated so that employers will be able to use this to calculate NICs due post April 2009.

**Consultation**

44. The Pension Act 2007 enacted the Government's proposals to reform the State Pension. Under these new arrangements, the State Second Pension is intended to become a simple flat rate weekly top up to the basic State Pension by around 2030, providing a clearer and more generous foundation to private saving. Budget 2007 announced the harmonisation of the National Insurance Upper Earnings Limit with the threshold at which higher rate income tax becomes payable to promote the Government's stated objective of improving tax and NICs alignment. These steps ensure that the changes announced to the State Second Pension under pensions reform take place as originally envisaged. The proposals in the Pensions Act were fully consulted on and therefore further consultation is not necessary.

45. In order for the changes to be introduced from April 2009 employers and software developers need certainty about the format of P11/ P14. Consultation would delay the

process of developing software and changing guidance necessary for smooth implementation of the UAP.

**Monitoring and Evaluation**

46. HMRC engages in regular forums with employers and their representatives as well as the software industry. These will provide a valuable source of the feedback for issues arising from the introduction of the UAP from April 2009. In addition we will carry out a review of the compliance costs after the changes have bedded in probably 1 to 3 years after implementation of the UAP.

**Summary**

47. The Pensions Act 2007 puts in place proposals to reform the State Second Pension so that it becomes a simple, flat rate weekly top up to the basic State Pension by around 2030. The above indexation increases to the Upper Earnings Limit announced at the Budget will delay this timetable without further action. The Government proposes to forward the introduction of the upper accrual point already agreed under pension reforms to 2009 ensure that it can still achieve our objectives for state pensions reform - in this case the need to make changes to the State Second Pension and contracting out to ensure that the NICs changes do not impose unintended costs elsewhere.

48. To achieve this objective we need to make changes to the information reported by employers which is used to calculate State Second Pension and contracted our rebates. It will also mean that employers and employees in contracted occupational pension schemes will only receive contracted out rebates between the LEL and UAP (employers and employees will pay NICs at 12.8% and 11 % respectively on earnings between the UAP and UEL).

49. The extent of the impact on employers depends on whether they have computerised or manual payrolls but it is estimated at £30 million for implementation with annual costs of £1 million thereafter. The cost to HMRC of implementing the UAP is estimated to be £10.65 million.

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# Specific Impact Tests: Checklist

Use the table below to demonstrate how broadly you have considered the potential impacts of your policy options.

**Ensure that the results of any tests that impact on the cost-benefit analysis are contained within the main evidence base; other results may be annexed.**

| **Type of testing undertaken** | ***Results in Evidence Base?*** | ***Results annexed?*** |
|---|---|---|
| Competition Assessment | Yes | No |
| Small Firms Impact Test | Yes | No |
| Legal Aid | No | No |
| Sustainable Development | No | No |
| Carbon Assessment | No | No |
| Other Environment | No | No |
| Health Impact Assessment | No | No |
| Race Equality | Yes | No |
| Disability Equality | Yes | No |
| Gender Equality | Yes | No |
| Human Rights | Yes | No |
| Rural Proofing | No | No |