

Employer factsheet: Abolition of contracting out on a defined contribution basis

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The Government is planning to abolish contracting out of the additional State Pension (also called State Second Pension) on a defined contribution basis from 6 April 2012.

This will mean that from 6 April 2012 affected employees will no longer be able to use a contracted-out money purchase (COMP) occupational pension scheme to contract out. They will automatically be brought back into the additional State pension system unless they become a member of a scheme which contracts out on a salary-related basis.

Defined Benefit schemes can continue to contract out on a salary-related basis.

What this means from 6 April 2012?

- You will not be able to use your COMP occupational pension (or a section of your scheme contracted out on a defined contribution basis) to contract employees out of the additional State Pension.
- Your employees may, depending on their level of earnings, start to build up entitlement to the additional State Pension instead.
- You will no longer be required to make the 'minimum payment' contributions into your contracted-out occupational pension scheme.
- Both you and your employees will pay the standard rate National Insurance contributions instead of the reduced contracted-out rate

You can start planning for the changes by:

- Considering how abolition will affect your scheme and how your scheme will continue to operate in the future.
 - You will need to decide whether, for example, your scheme continues or whether you need to make changes to take account of the fact that National Insurance rebates will no longer be paid.
 - You may also want to consider the impact of the Government's plans for employers

to automatically enrol eligible employees into qualifying workplace pension schemes when considering any changes to the design of your existing scheme. Automatic enrolment is due to begin from October 2012 with employers being phased in by size (largest first) from this date.

- You may want to discuss your options with your advisors. Any changes will also need to be discussed with appropriate parties: pension advisors, scheme trustees, members, etc.
- Preparing to pay the correct National Insurance contributions after the abolition date.
- Starting to think about how you will communicate the National Insurance contribution changes and any scheme changes to your employees. There is a fact sheet available on Directgov which you can give to employees to provide them with information on what the abolition of contracting out may mean for them.

Q&A on abolition of contracting out

Q. Does this affect the money that has already been saved into occupational pension schemes whilst employees were contracted out?

A. No. The money already held should remain in the scheme to provide members with a pension, on retirement, in accordance with scheme rules.

Q. What happens to 'protected rights' already accrued?

A. At the moment the rebates together with any investment return are known as "protected rights". There are currently statutory restrictions on how protected rights can be used.

This is because they are intended to be used to provide benefits in place of the additional State Pension.

However, from 6 April 2012 these restrictions will no longer be in force and former “protected rights” benefits can be treated the same as other pension benefits. They will be retained in the pension scheme unless a transfer request has been made.

HMRC currently holds records which show details of an individual’s membership of a contracted-out defined contribution scheme. Schemes have been able to check the accuracy of the information they hold against HMRC records. However, as all the rules around protected rights and the tracking of those rights are to be removed, the accuracy of HMRC’s records will decline over time. It is therefore important that schemes ensure that their records are up to date prior to abolition.

You may also wish to consider how the administrative easement of no longer having to track protected rights benefits separately is incorporated into the running of your scheme.

Q. What happens if I have a scheme that holds both a section contracted out on a defined contribution (money purchase) basis and a section contracted out on a defined benefit (salary related) basis (a Contracted-out Mixed Benefit (COMB) scheme)?

A. No further National Insurance rebates will be payable for the period beyond the abolition date for employees contracted out on a defined contribution (money purchase) basis. Members contracted out on a defined benefit basis are not affected.

The certificate for this scheme will remain valid only for the section of the scheme contracted out on a defined benefit basis. Your scheme will not need to apply for a new defined benefit contracting-out certificate as only the contracted-out defined contribution part of the COMB will be cancelled after abolition.

You may wish to discuss this with your professional adviser.

Q. Will I need to surrender my contracting-out certificate?

A. No, contracting-out certificates for defined

contribution schemes will be automatically cancelled from the date of abolition. You do not need to take any action.

If you have a contracting-out certificate that covers a contracted-out mixed benefit scheme (COMBS) i.e. covering both defined benefit (salary related) and defined contribution (money purchase) sections, this will remain valid only for the purposes of schemes contracted out on a defined benefit basis, post abolition. The scheme will not be required to reapply for a new defined benefit contracting-out certificate.

Where can I go to find out more?

Your professional advisors and your payroll provider/software provider

Your advisors can discuss the implications for your specific scheme with you. You may also wish to discuss the changes and how you will implement them with your payroll/payroll software provider.

[Her Majesty’s Revenue and Customs \(HMRC website\)](#)

[Employers’ Bulletin \(HMRC website\)](#)

Gives employers the latest information about payroll topics and other issues that may affect them. It also provides pointers to new procedures and initiatives which may be of interest and contains direct links to more detailed information allowing you to explore topics further.

[NISPI Countdown Bulletin \(HMRC website\)](#)

This bulletin keeps pension providers who are currently operating defined contribution contracted-out schemes updated on what is happening in the lead up to the change in April 2012.

[Pension Schemes Services \(HMRC website\)](#)

This provides information on administering the rules around how pensions are taxed.