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What does 2016 have in store for pay?

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Headlines

2016 is set to be another challenging year for reward practitioners.

- Against a very uncertain global economic backdrop, and amid the focus on fairness in pay and increased levels of regulation and governance, many companies are **planning detailed reviews of its compensation practices**.
- Renewed scrutiny on the link between pay and performance, as well as getting the maximum value for money from the reward spend as organisations adapt to new technology and ways of working.
- The impact of gender pay equality is another key focus and further generating the need to review practices.
- The impact of the **National Living Wage** will come into effect in April 2016 putting increased pressure on companies pay budgets.
- **Restraint** forecast for pay settlements and salary budgets are anticipated to be flat.
- Increased **decoupling** between UK inflation and pay settlement percentage, driven by:
 - increased mobility of talent causing greater competition
 - volatility of inflation
 - tension between RPI and CPI as an index for inflation and which is an appropriate metric to use.
- With the disconnect between pay increases and the traditional reference point of inflation, companies using a more diversified range of factors in shaping pay settlements as follows
 1. Company's ability to pay;
 2. Market pressures;
 3. Individual performance; and Cost of Living.

*Over the next few pages we will look at some key trends
drawn from the PwC Executive and Reward Management Survey:*



PwC Executive & Management Reward Survey

FTSE 100
58 companies

FTSE 250
72 companies

Private & Other
91 companies

CEO

Main Board

ExCo

Function head

Department head

Group other

Group other

Tier 1

Tier 2

Tier 3

Tier 4

Tier 5

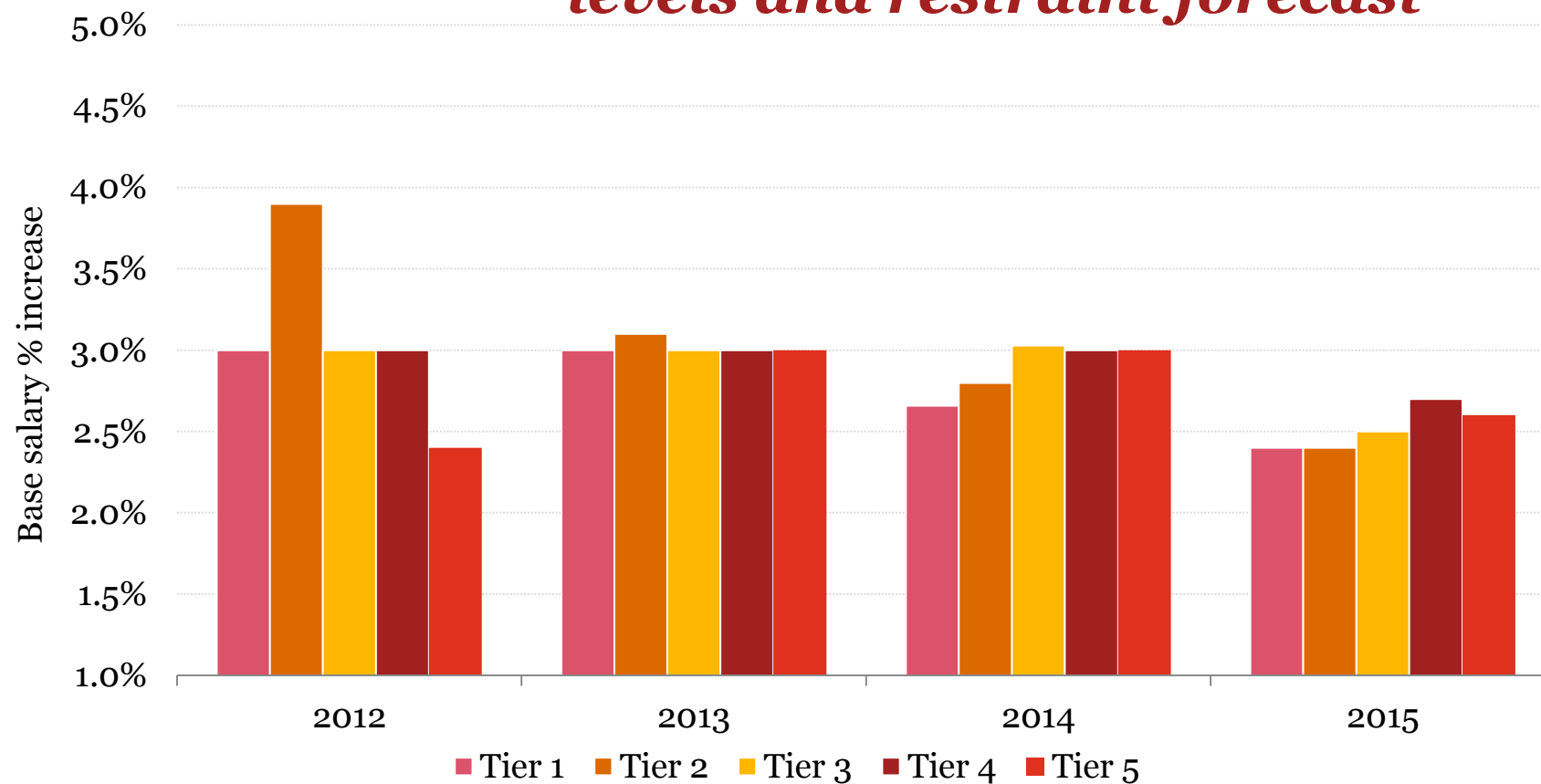
Tier 6

Tier 7



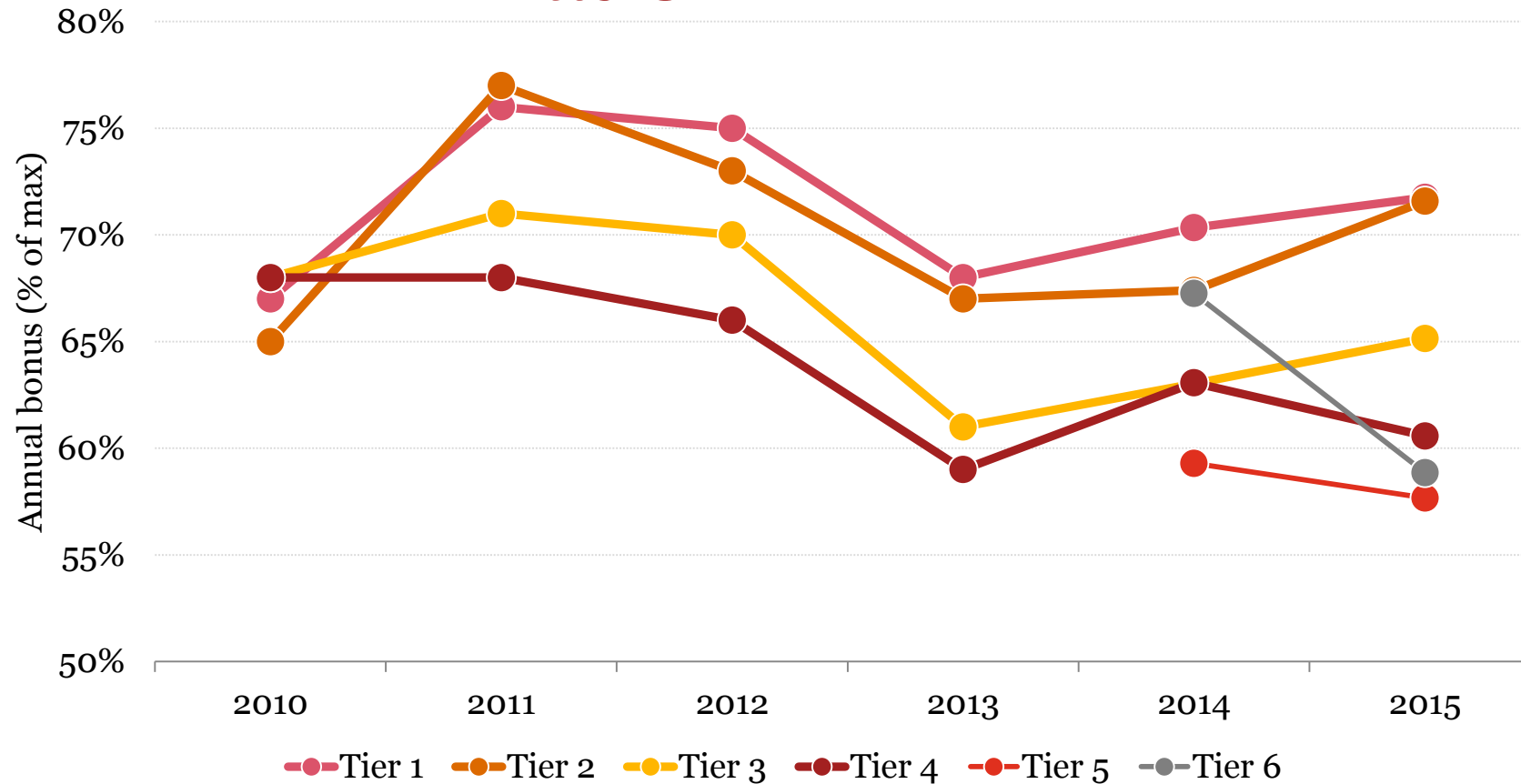
Actual base salary percentage increase

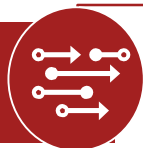
Lower salary increases at all levels and restraint forecast





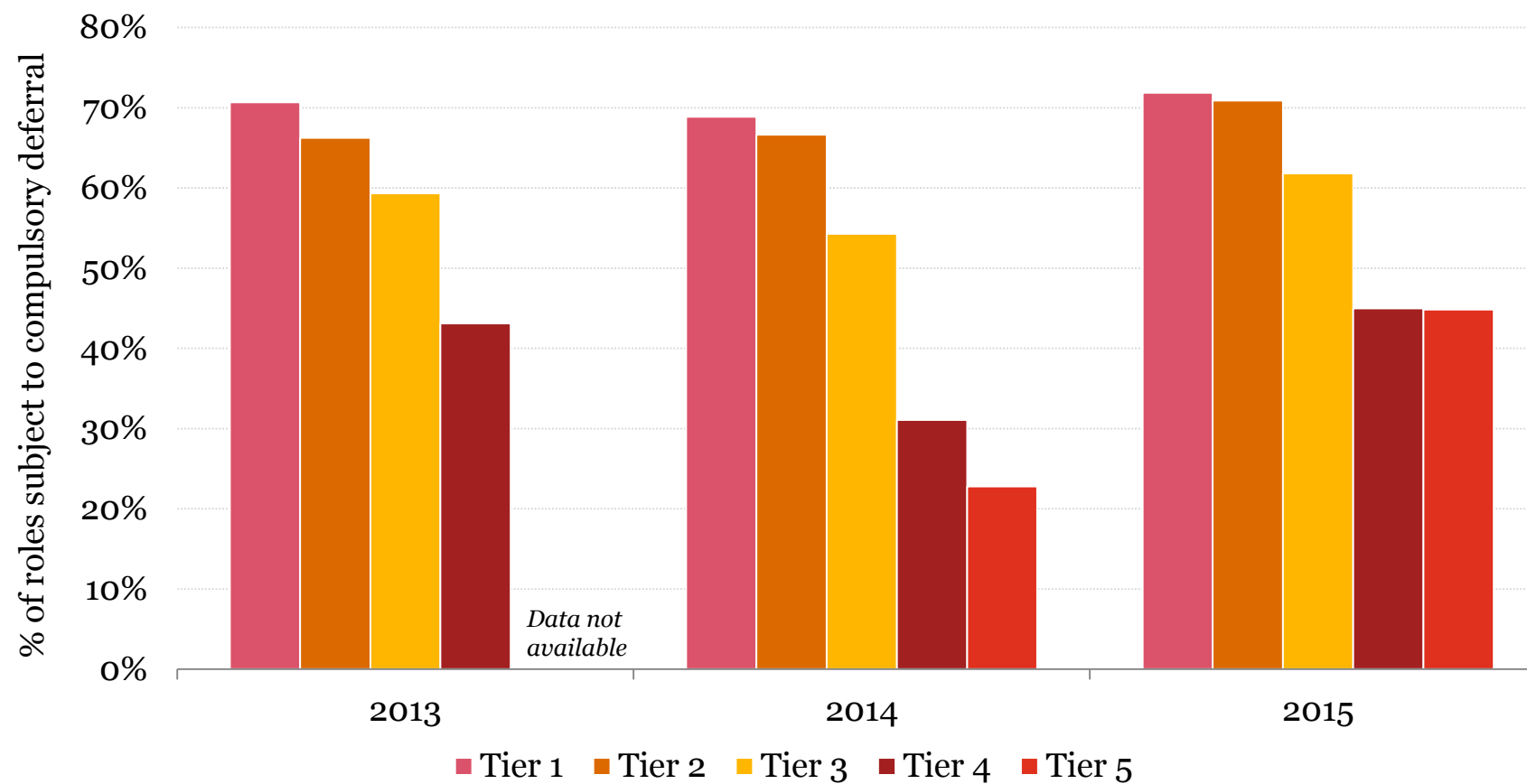
Actual annual bonus as % of max Bonus pay outs up for senior management but down for lower tiers





Bonus deferral

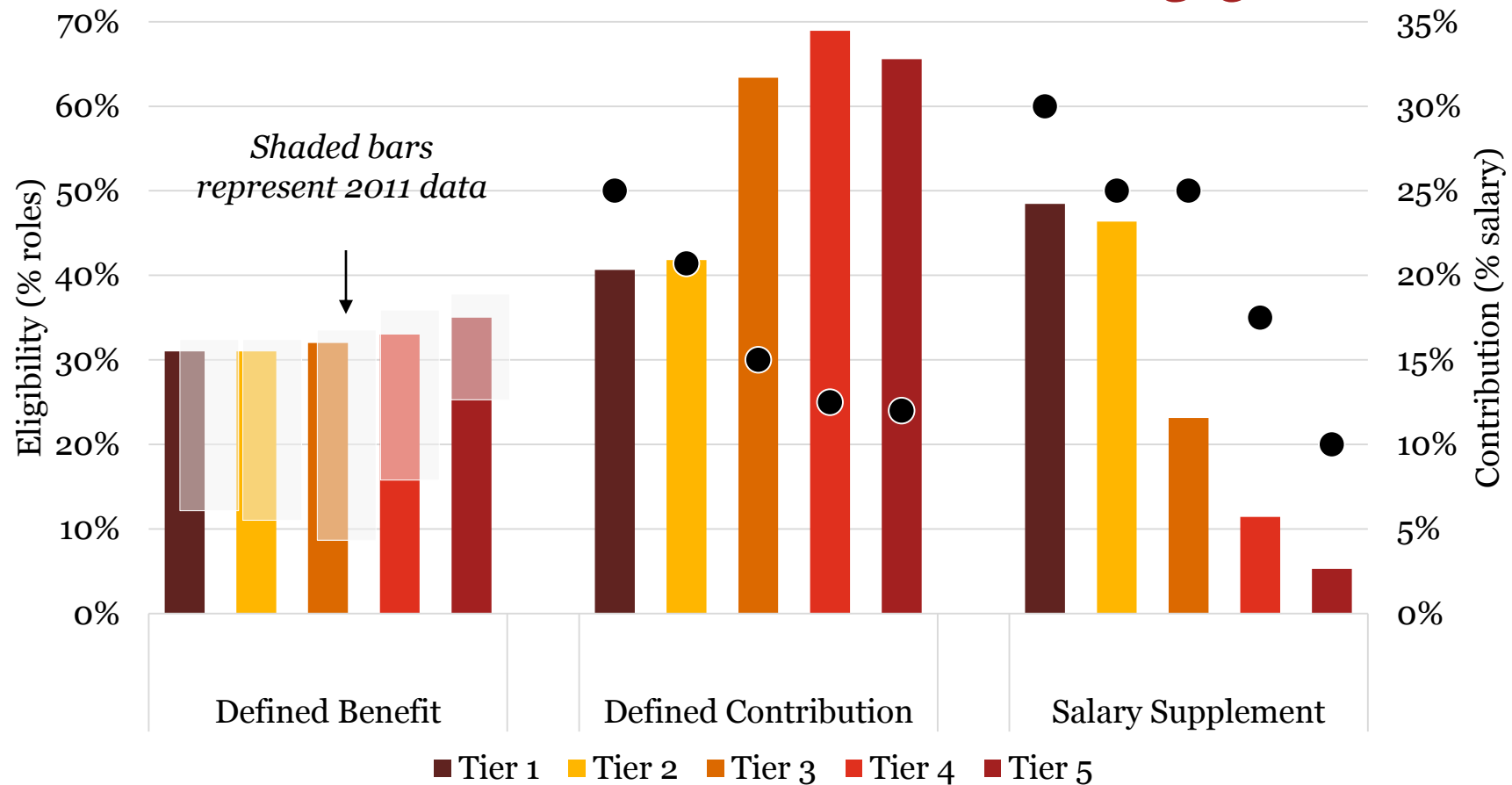
Increased use of bonus deferral, particularly at lower tiers





Pension eligibility and contribution

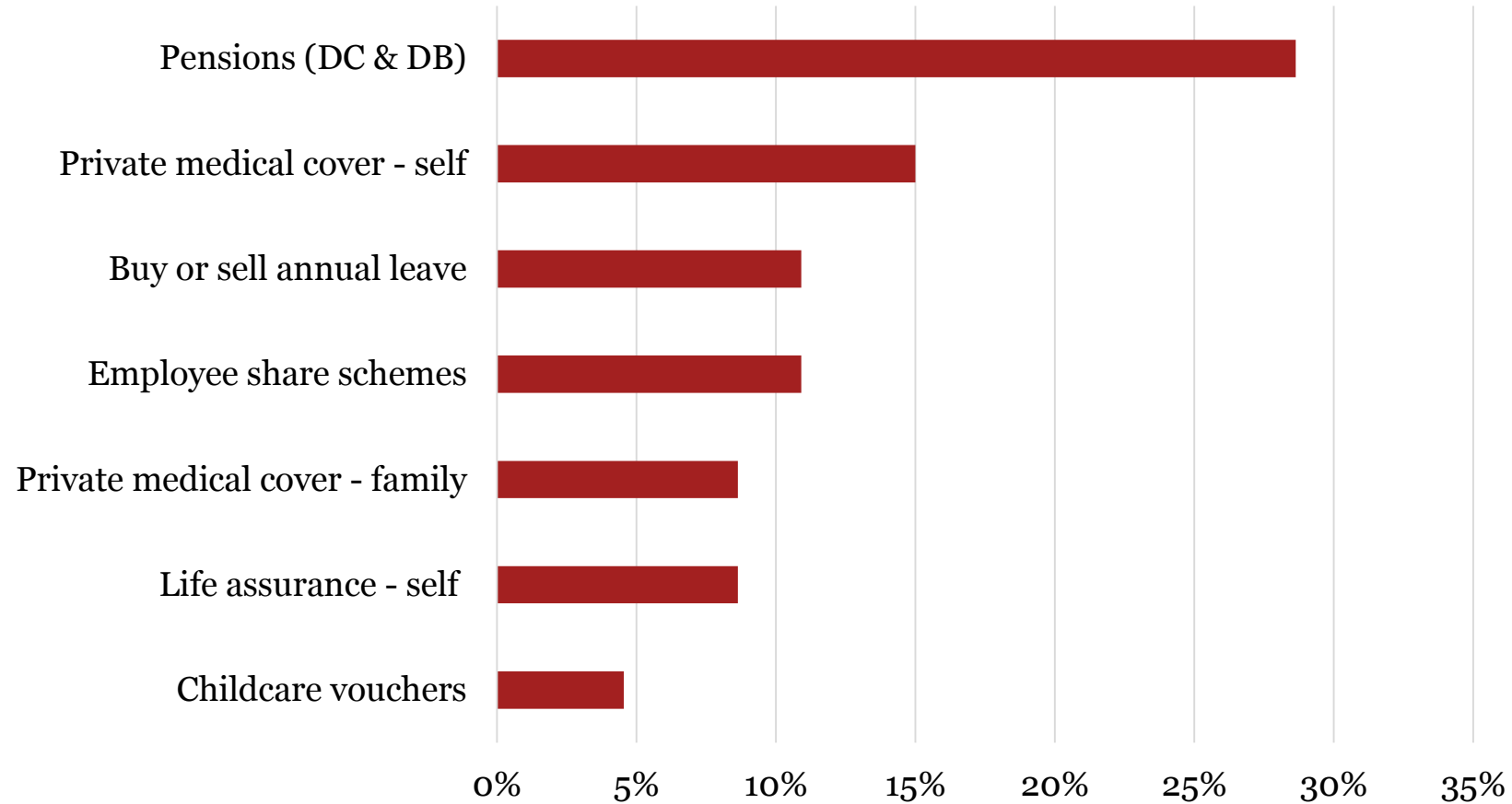
Salary supplement most common at Tiers 1-2 but defined contribution at Tiers 3-5





Benefits

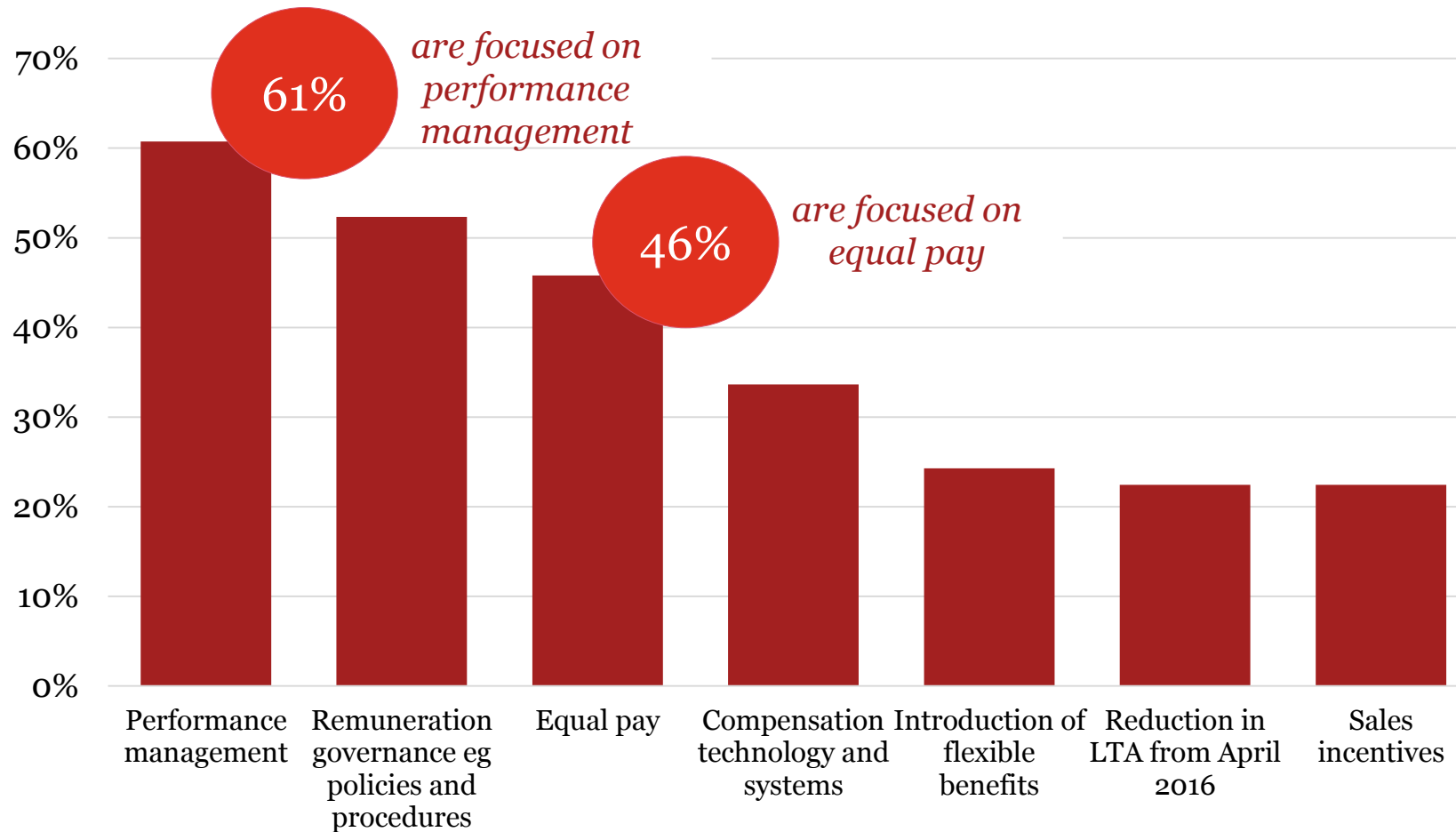
Companies identify the usual benefits as the most popular



Looking forward to 2016

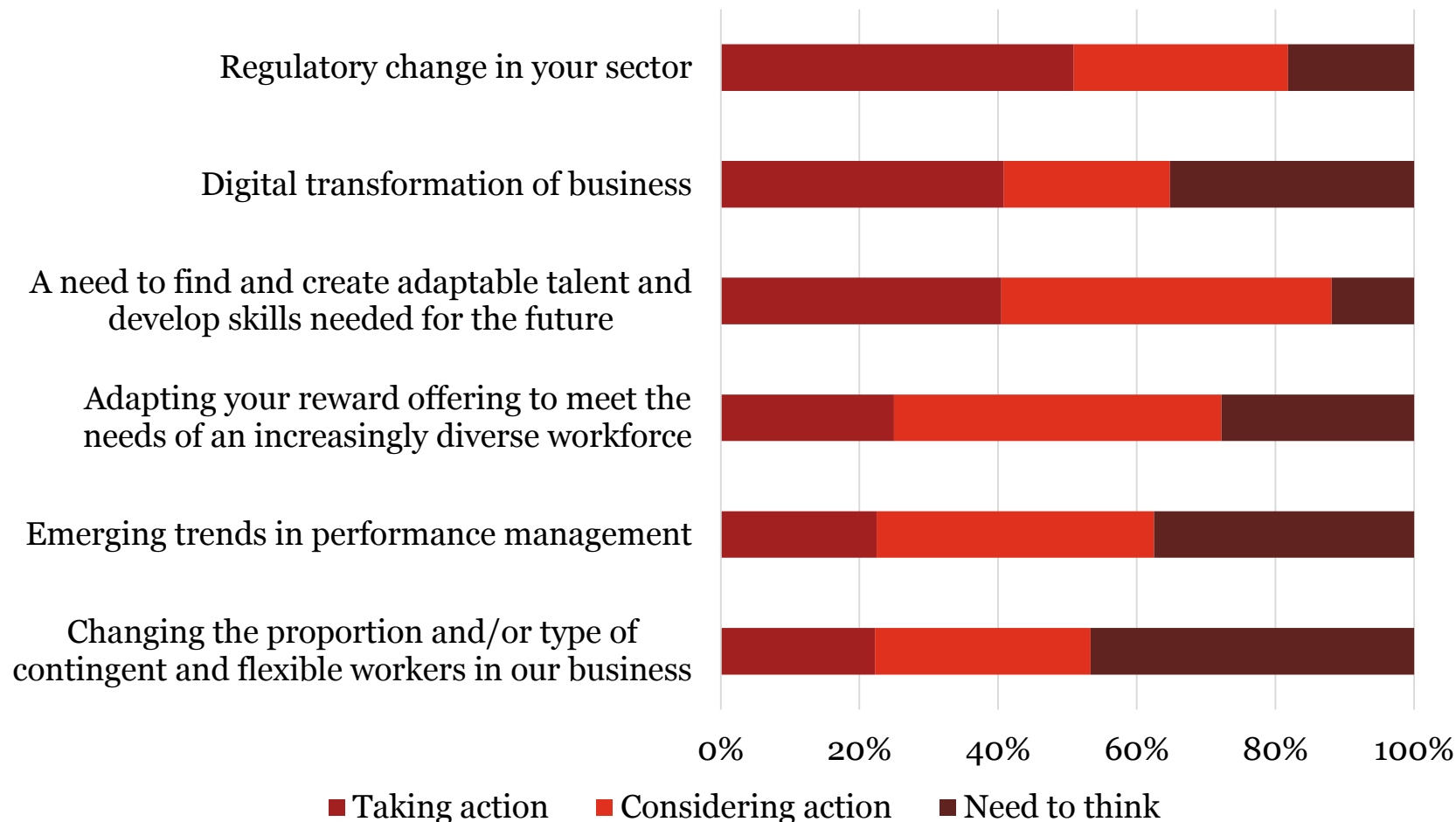


Which of the following best summarises your reward priorities for the next 12 months?





How do you plan to react to the following reward issues in 2016?





Looking forward to 2016

- Focus on fairness
- Focus on target-setting and link between pay and performance
- Managing the risks and costs around increased regulation of pay and benefits

REBA – Pay Governance

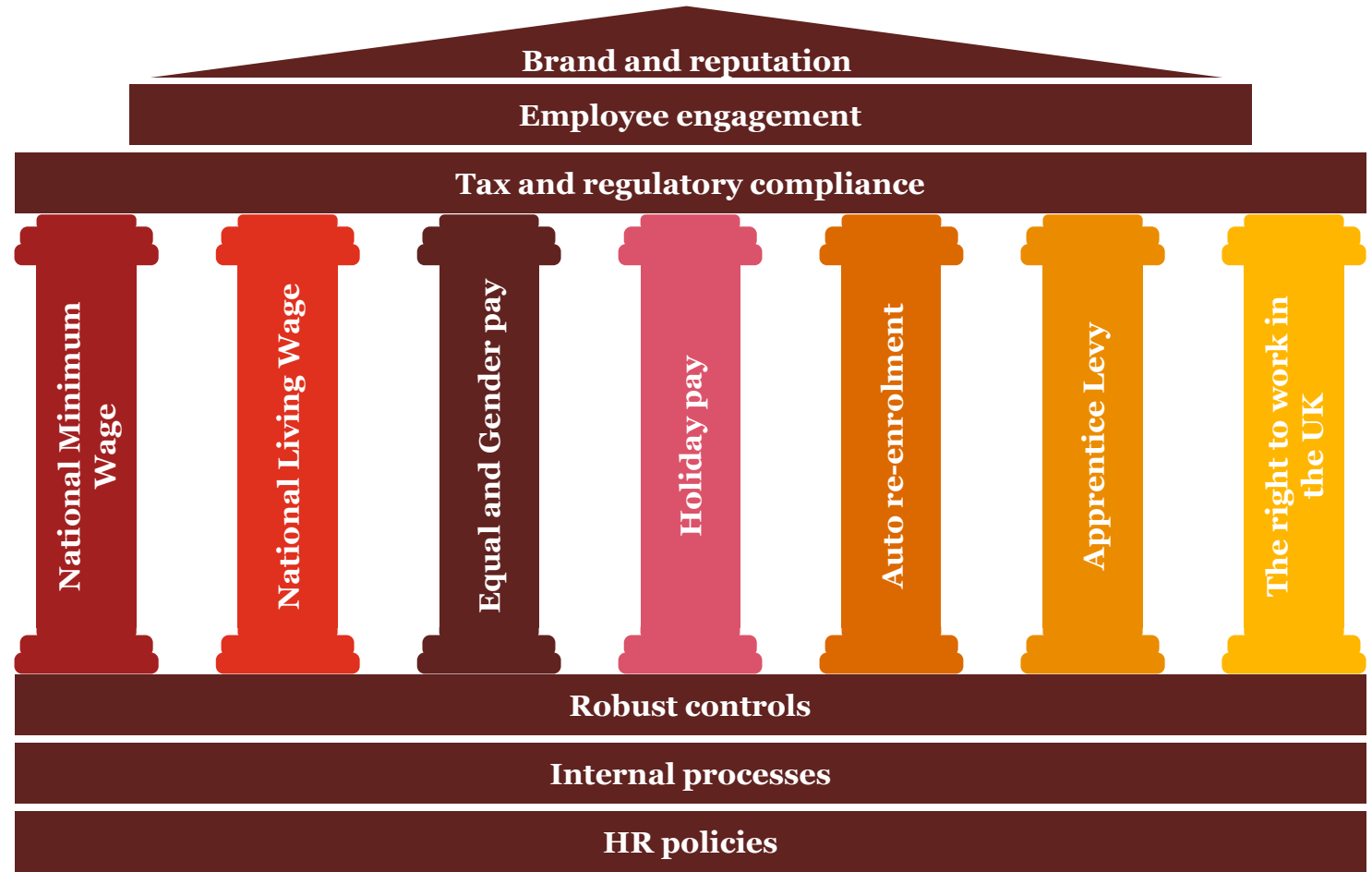
February 2016

Why is Pay Governance an issue?

- Recent and upcoming legislative changes
- Stronger enforcement by Government in relation to pay and HR aspects.
- PwC have responded to 12 consultations in this area in the last six months.

These areas will impact on:

- Employment cost
- Compliance risk
- Operational challenges
- Reputational risk
- Colleague engagement



National Living Wage – the basics

What to look out for ahead of April 2016...

The NLW will be a single statutory hourly rate for the whole of the UK.

NLW rate of **£7.20 per hour** from April 2016, representing a **7% increase** from the current NMW of **£6.70**.

Average annual uplift of between **5% and 6% each year until 2020** when the rate reaches

A compulsory level of the National Minimum Wage (NMW) for those aged 25 and over.

Significant reputational and financial risks if an employer fails to comply.

Compliance will be enforced by HMRC, measured by reference to worker categories and the specific pay elements they are paid on a pay period by pay period basis.

Separate to the voluntary Living Wage which is expected to continue at a higher rate of pay and with different rates for London and the regions.

Full details to be confirmed around how the NLW might be introduced and applied in conjunction with the NMW.

Compulsory Naming and Shaming if total underpayment exceeds £1000 and penalty increasing to 200% maximum.

NLW Survey results: let us know if you'd like further insight

National Living Wage – things to consider

Quantify total cost and identify options to manage increase

- Forecast of cost impact now as well as through to 2020.
- Costs will include pay, NICs, pension contributions and the impact on Auto Enrolment.
- Potential modelling of the impact on pay differentials.
- Assessing the impact on pensions, pay and benefits.

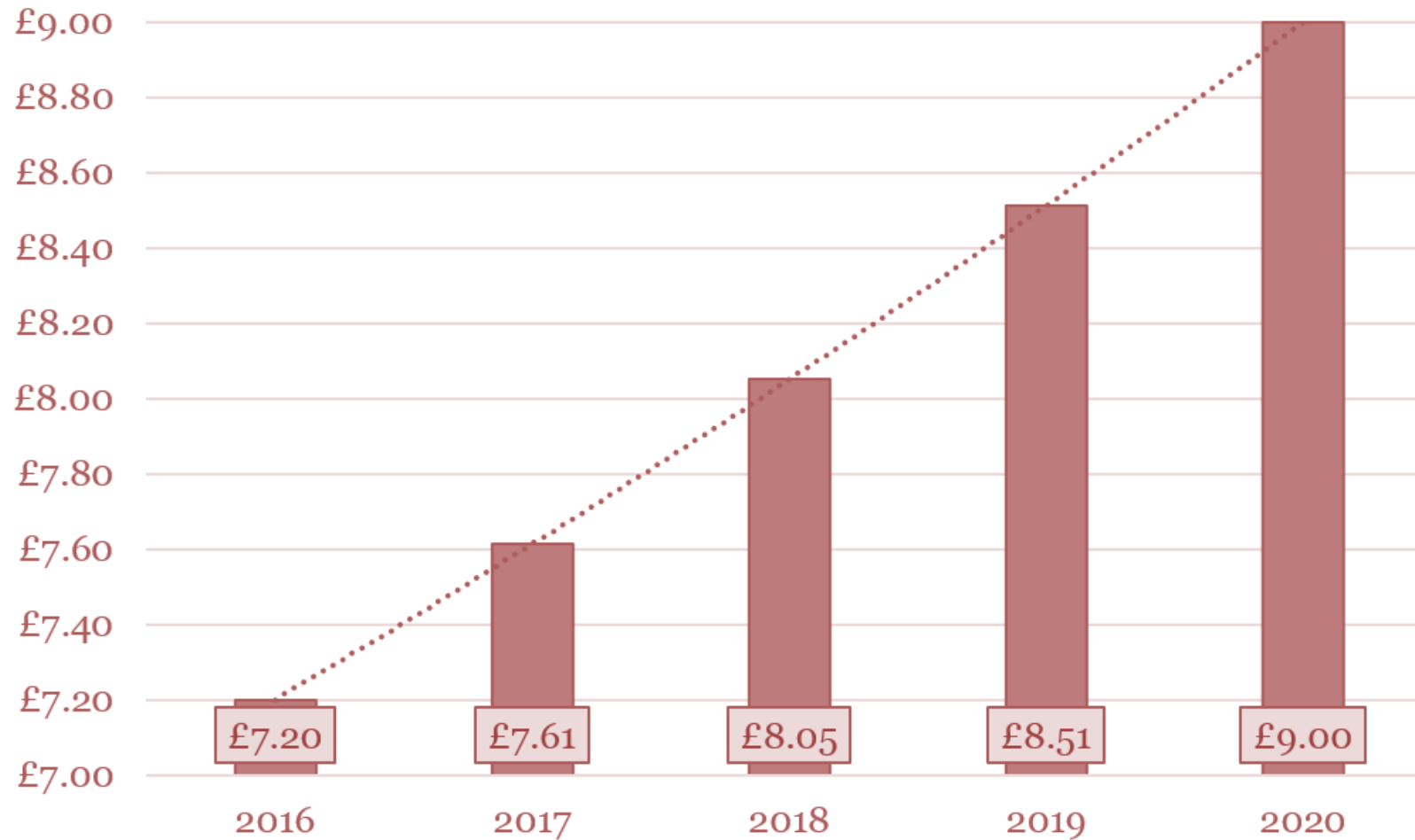
Remain compliant by strengthening policies and procedures

- Ensuring compliance and avoiding breaches that would lead to fines and the reputational damage caused by mandatory 'Naming and Shaming'.
- Identifying the wider impact on risks around:
 - Hourly rates and time and attendance
 - Pay elements
 - Holiday pay

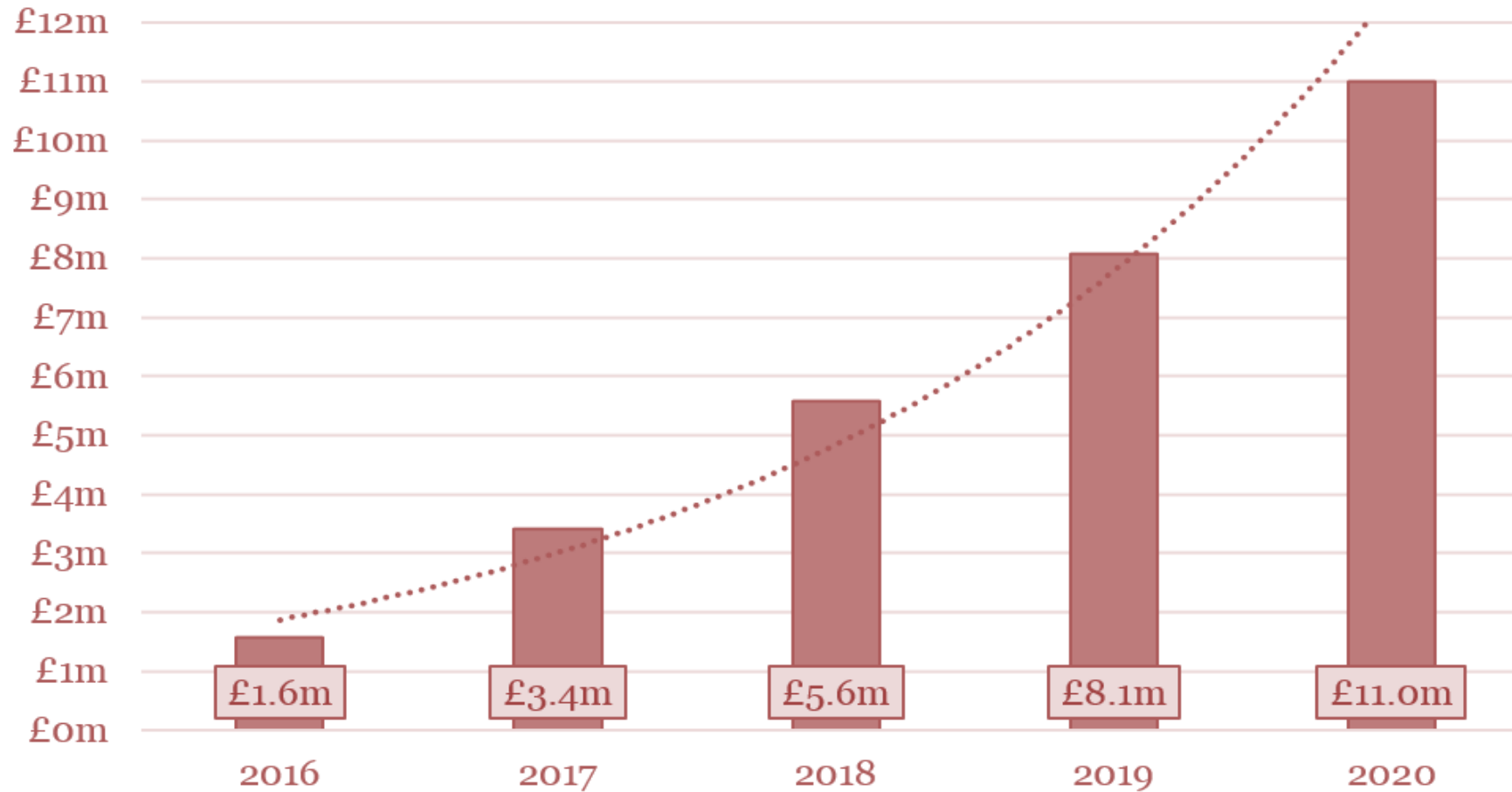
Manage the impact on broader benefits and pay differentials

- Reviewing pay and grading structures, bonuses, commissions, overtime and allowances.
- Communicating the impact of these changes internally.
- Reviewing the impact on all salary sacrifice and 'Flex' schemes and identifying the actions required.
- Revising annual pay review and the relationship between performance and reward.
- Workforce planning.




Possible phasing of the National Living Wage (£9.35)



Average cumulative annual cost increase



Average cumulative annual cost increase

	<i>2016</i>	<i>2020</i>	<i>2020 vs 2016</i>
 Hospitality & Leisure	£2m	£13m	x 6.5
 Healthcare	£2m	£14m	x 7
 Retail	£4m	£26m	x 6.5

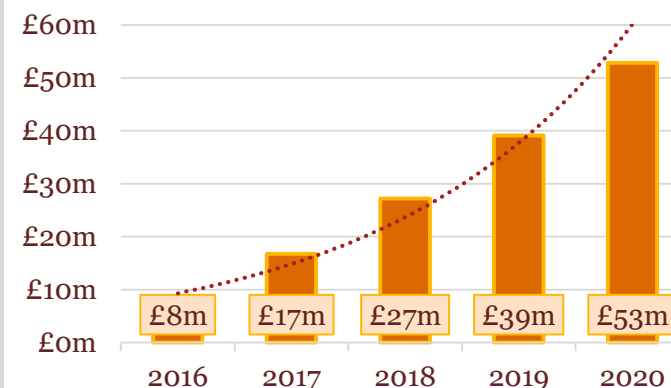
Reactions to the National Living Wage in the retail sector

1	Changing pay and grading structures	61%
2	Communicating these changes to your impacted employees	45%
3	Reassessing pricing model / passing costs on to customers	37%
4	Amending overtime / allowance policies	37%
5	Reducing / restructuring headcount	34%
6	Consolidation of pay elements into hourly pay rate	29%

Currently expected hourly rates for supermarkets in April 2016

Aldi	£8.40
Lidl	£8.20
Morrisons	£8.20
Marks & Spencer	£7.41
Tesco	£7.39
Sainsbury's	£7.36
The Co-operative	£7.28
Iceland	£7.26
Asda	£7.20+ (tbc)
Waitrose	£7.20+ (tbc)

Average annual cost for large retailers



Responses

Deniers



Budgeters



Adapters



Gender/Equal pay – Mandatory pay gap reporting

What's changed?	What's the impact?	What are the risks?
<p>Regulations are coming into effect making it mandatory for employers of 250 or more employees to publish their gender pay gap presumably on an annual basis.</p> <p>Pay still to be determined but bonuses have been specifically referenced</p>	<p>Employers' pay structures will be under scrutiny, with inequalities with pay and bonuses being open for both employees and the wider public to see.</p>	<p>Financial penalties of up to £5,000.</p> <p>Impact on employee engagement, talent and attraction.</p> <p>Negative external publicity and reputational damage.</p> <p>Increased risk of equal pay claims.</p>
<p>What action to take</p> <p>Consider undertaking an early review of Pay across workforce to better understand the extent of any discrepancies and formulate action plan to address and how these might be best communicated and explained</p>		

What do we mean by Equal Pay?

Key principle is Equal Pay for women and men doing “equal work”



Potential justifications for a gap in pay include...



Holiday pay – update on the current position

- Calculation should be based on “normal remuneration” – i.e. should include all non guaranteed overtime and any other intrinsically linked payments
- Applies to workers’ four weeks’ holiday entitlement under European law
- Series of deductions broken where more than three months has elapsed between deductions
- Regulations introduced to limit claims after 1 July 2015 to two years’ back payment

***Bear Scotland
case -
Overtime***

- Commission determined with reference to sales achieved “or other similar payments” should be included in calculation
- As with Bear Scotland, decision only applies to workers’ four weeks’ holiday entitlement under European law
- Issues such as whether discretionary bonuses must also be included in the calculation are not yet resolved

***Lock case -
Commission***

- British Gas appealing the decision to the EAT on the basis that:
- Non-guaranteed overtime and commission are dealt with under separate provisions and that the ET therefore incorrectly concluded that the Bear Scotland impacted the outcome of the Lock case.
- Even if Bear Scotland was applied correctly, the EAT in Bear Scotland incorrectly concluded that UK domestic legislation can be interpreted purposively to give effect to EU law.

Lock - Appeal

- Northern Ireland Court of Appeal ruled that 'voluntary overtime' may in some cases have to be taken into account in calculating holiday pay.
- Court of Appeal decision is in line with recent European decisions on holiday pay in that “normal pay” (i.e. pay that an employee would normally expect when at work) should be included in the calculation.
- Decision only binding in Northern Ireland and not the rest of the UK, although it will be persuasive authority.

***Patterson vs
Castlereagh
Borough
Council***

Automatic Enrolment – the current position

- Smaller employers currently staging
- Larger employers facing re-enrolment process (3 year anniversary)

Automatic re-enrolment considerations:

- Consider which date will be selected for automatic re-enrolment as only one date can be chosen which may impact employers with multiple payroll cycles – weekly and monthly
- Consider technological solution(s) and whether they can support with re-enrolment
- Consider whether existing pension contribution structure is still fit for purpose given the increases to statutory minimum contribution levels in auto enrolment schemes – can costs be reduced?
- Consider the changes to the regulations since initial staging – can these simplify your current costs, processes and administration?
- Re-enrolment process, issuing of communications and re-declaration process (former registration)
- **Consider use of salary sacrifice to manage costs although beware NLW restrictions**

Apprenticeship Levy

What is it?

Initially announced in the 2015 summer budget

When



*Starting in April
2017*

Who



*Applies to all UK
employers. The
£15k allowance
means impacts
where total 'pay
bill' exceeds £3 m*

Cost



*Levy will be 0.5%
of total 'pay bill'
and collected and
operated via RTI
and PAYE system*

Relief



*Employers will
receive an
allowance of
£15,000 to offset
against the Levy*

Apprenticeship Levy

How will it operate?

The Levy will be payable at 0.5% of the 'pay bill' through RTI; alongside Income Tax and National Insurance Contributions with employers receiving a £15,000 allowance to offset against the Levy

There will be complexity around the calculation as a result of location of employers and employees e.g. England compared to the rest of the UK

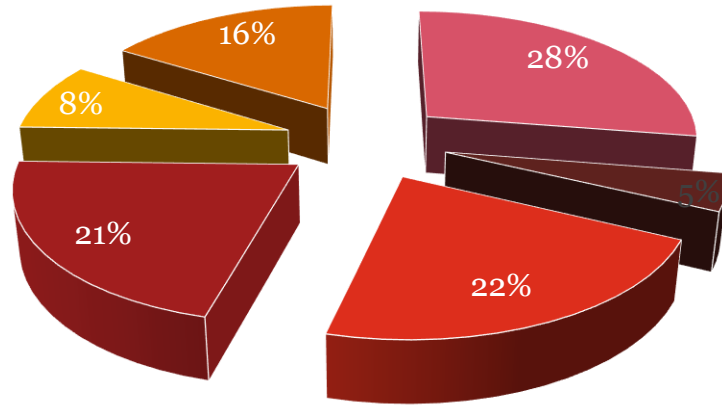
The Levy is expected to raise £3bn a year. The Levy paid by employer will be held in a digital account and in England will be able to direct funding for training through a new Digital Apprenticeship Service (DAS)

Employers are likely to be subject to an initial 2 year time limit to utilise their funds for qualifying apprenticeship training

Unused Levy will be recycled and depending on the final decision made by BIS, employer digital accounts may be topped up by the Government for the first 2 years

Tax and regulatory compliance

Total Tax Receipts



■ PAYE ■ Income Tax ■ NIC ■ VAT ■ CT ■ Other

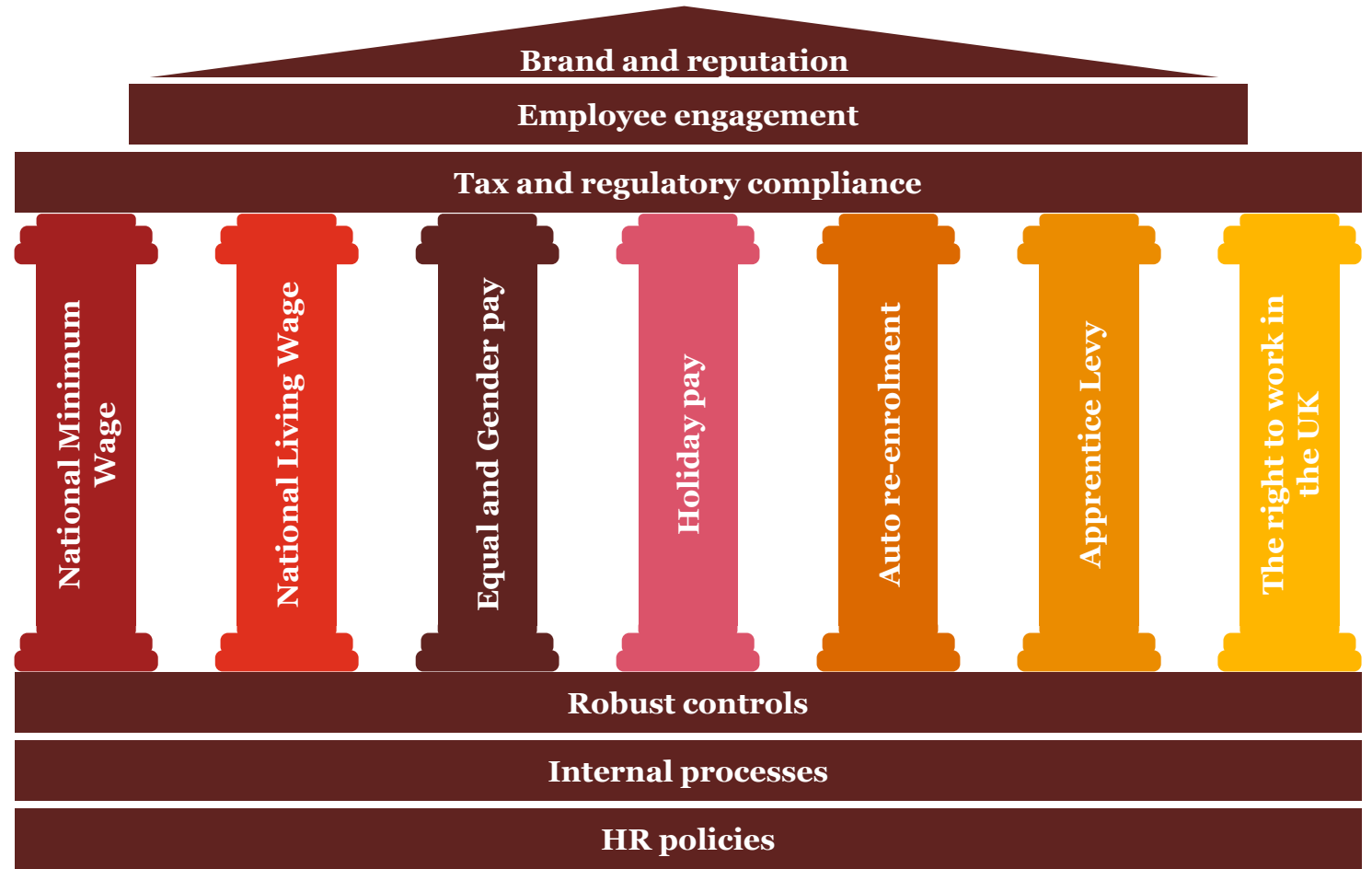
- PAYE/NIC account for 50% of Government receipts in 2013-14 – an area of increasing focus
- Ever increasing complexity for employers – exacerbated by dealing with major change (RTI, Auto-enrolment, introduction of SRIT etc.)
- Increasing change – significant numbers of consultations directly affecting payroll operations
- An area which has had limited risk profile in organisations until recently
- An area which has been gently policed over the last 5 years

Tax and Reward

- Income Tax and NIC have increased focus at Board Level given headlines in the Press
- Know Your Customer Initiative covering largest 2,100 private sector employers looks at process controls and procedures around how you pay your people
- Increased HMRC interest in, and scrutiny of, salary sacrifice arrangements
- “The Good, the Bad and the Ugly” salary sacrifices
- HMRC recent stakeholder workshops on salary sacrifice – undertake health checks now
- Restrictions in Pension Tax relief for those with “High Incomes” (possibly impacts those with salaries from £80k p.a.) from April 16
- Speculation of a Flat Rate Tax Relief on pension contributions in Budget and a corresponding Income Tax Charge and Anti Forestalling legislation
- SVRIT what does it mean going forward?
- Is the Apprenticeship Levy an Employment Tax?
- HMRC’s role in National Living Wage compliance
- Trivial Benefits exemption from April 2016

Actions?

- Establish level of impact of each of these issues and ensure potential risks and costs are understood by key stakeholders?
- Are controls and processes fit for purpose?
- Engage with your colleagues from Tax, legal and Finance
- Speak with professional advisers
- Scenario analysis and action plan agreed (eg. Holiday Pay, National Living Wage, Equal Pay etc)
- Understand options and plan now to minimise costs and adverse impact on reputation



SUMMARY

- Reward is increasingly complex- benchmarking and trends can help
- Regulation is increasing both cost and risk in your business
- Often the reputational damage can be the most important risk

Questions?

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