

## **Section 15 - National Insurance Contributions**

National Insurance contributions

Class 1 National Insurance contributions

Class 2 National Insurance contributions

Class 3 National Insurance contributions

Class 4 National Insurance contributions

Credits for Parents and Carers

Home Responsibilities Protection

Reduced Liability for Contributions for certain Married Women and Widows

## **NATIONAL INSURANCE CONTRIBUTIONS**

### **1. INTRODUCTION**

#### **1.1 GENERAL**

Most people who work have to pay National Insurance (NI) contributions. There are four classes of NI contributions (see below) and in the course of a person's working life they may need to change from one class to another or pay more than one class of contribution at the same time.

The level of a person's contribution and the rules regarding payment depend on the class of contribution they pay.

Class 1 - Paid by employed earners and their employers

Class 2 - Paid by self-employed earners

Class 3 - Paid voluntarily by persons not liable for any other class of contribution

Class 4 - Paid in addition to Class 2 contributions by self-employed people whose profits are above certain levels

Class 1, 2 and 3 contributions count for various National Insurance benefits. Class 4 contributions do not count for any benefits.

More information about each of the classes of NI contributions and what benefits they count towards is set out in the following pages.

#### **1.2 Leaflets NI1(IOM) and NI2(IOM)**

#### **1.3 Telephone contact - 685177**

### **2. EARNINGS FACTORS**

For a tax year to qualify for contributory benefit purposes, a person must achieve the required Earnings Factor for that year by paying sufficient Class 2 or 3 contributions or by having earnings from employed earner's employment at not less than the lower earnings limit (LEL) for that tax year (or by a combination of those situations).

An earnings factor is the figure which represents the amount of earnings on which contributions have been paid or treated as paid for any earnings period.

### **3. PAYMENT OF NI CONTRIBUTIONS**

Employed earners' Class 1 primary contributions are deducted from an employee's pay by their employer, and paid over to the Income Tax Division of the Treasury each month along with the employee's income tax instalment payments. Class 4 contributions are also collected by the Income Tax Division.

Class 2 and Class 3 contributions are collected by the Contributions Section of the Income Tax Division.

To count for contributory benefit purposes, contributions must be paid within strict time limits. Also, Class 1 and 2 contributions may not count for short-term benefit entitlement purposes where they are paid after the start of the benefit year relating to the claim for benefit.

Arrears of Class 2 contributions payable for the 2008/09 year and earlier years are now payable at a rate higher than the one at which they were originally due.

### **4. NATIONAL INSURANCE CREDITS**

To the extent necessary to make it a qualifying year, Class 1 credits may be awarded to a contributor instead of them having to pay contributions if they were:

- available for work and claiming Jobseeker's Allowance (even if they are not entitled to that benefit)
- sick and claiming Incapacity Benefit (even if they are not entitled to that benefit)

## Section 15

- entitled to
  - \* Maternity Allowance
  - \* Carer's Allowance
  - \* Disability Working Allowance
  - \* Family Income Supplement
- on an approved training course
- required to attend jury service and did not have earnings at or exceeding the Lower Earnings Limit from employed earner's employment
- a man aged over 60 who is not liable to pay contributions and who is present on the Isle of Man or in the UK for at least half the tax year
- a person who was imprisoned following a conviction which was subsequently quashed and then released from prison or a person who was otherwise detained in legal custody and later released – for that period of detention
- aged 16, 17 or 18 in that tax year.

### 5. CONTRIBUTORY BENEFITS

The Class of NI contributions paid affects the benefits a person can get. The benefits for which the fulfilment of contributory conditions is necessary are as follows:

Are contributions taken into account for benefit purposes?

<u>Benefit</u>	<u>Class 1</u>	<u>Class 2</u>	<u>Class 3</u>
Contribution-based Jobseeker's Allowance	Yes	*No	No
Incapacity Benefit	Yes	Yes	No
Maternity Allowance	Yes	Yes	No
Bereavement Payment	Yes	Yes	Yes
Widowed Parent's Allowance	Yes	Yes	Yes
Bereavement Allowance	Yes	Yes	Yes
Retirement Pension (basic)	Yes	Yes	Yes
Additional Pension	Yes	No	No

(\* Share Fishermen pay a special rate of Class 2 contributions which counts towards entitlement to Contribution based Jobseekers Allowance).

### 6. STATE ADDITIONAL PENSION

Since 6<sup>th</sup> April 2002, persons who are employed earners no longer build up entitlement to an additional pension under the State Earnings Related Pension Scheme (SERPS) (paid on top of any basic pension entitlement they might have when they reached State pension age), but instead do so under the State Second Pension (S2P).

The way in which people accrue entitlement to S2P differs from that under SERPS. In particular, persons with earnings in any tax year of at least the annual lower earnings limit (£5,044 for the 2010/11 tax year) but less than the S2P low earnings threshold (£13,900 for the 2010/11 tax year) will build up entitlement to S2P as if they in fact had earnings of £13,900.

## **CLASS 1 NATIONAL INSURANCE CONTRIBUTIONS**

### **1. INTRODUCTION**

#### **1.1 GENERAL**

Class 1 NI contributions are payable at a percentage of the amount of an employee's pay which exceeds the primary earnings threshold, which has been fixed at £110.00 per week for the 2010/11 tax year.

Class 1 NI Contributions comprise:

- Primary contributions and additional primary contributions, which are payable by the employee; and
- Secondary contributions, which are payable by the employer.

#### **1.2 Telephone contact - 685177**

### **2. WEEKLY EARNINGS LIMITS AND EARNINGS THRESHOLDS**

Lower and upper earnings limits and primary and secondary earnings thresholds are set for each tax year.

#### **Lower Earnings Limit (LEL)**

There is no liability for either Primary or Secondary contributions until a person's earnings exceed the primary and secondary earnings thresholds respectively for that year (which for the 2010/11 tax year are set at the same level, i.e. £110 per week). However, earnings falling between the LEL (£97 per week for the 2010/11 tax year) and the primary earnings threshold count towards a person's entitlement to contributory benefits as if contributions had in fact been paid on them.

#### **Earnings thresholds**

If an employee's earnings exceed the primary earnings threshold, primary contributions are payable on all earnings between that threshold and the Upper Earnings Limit (UEL) and additional primary contributions are also payable on all earnings that exceed the UEL.

Secondary contributions are payable on all earnings above the secondary earnings threshold. There is no UEL for secondary contributions.

### **3. CONDITIONS**

#### **Employees**

Employers are legally obliged to deduct Class 1 primary contributions from their employees' earnings if their employees are

- aged 16 or over and under State pension age (see paragraph 1.1 on page 79);
- living or present in the IOM at the time of their employment; and
- working under a contract of service.

Primary Class 1 contributions are not payable by an employee who has reached state pension age.

#### **Employers**

Employers are liable to pay secondary Class 1 contributions if

- their employees are aged 16 or over; and
- they live in the IOM; or
- they have a place of business in the IOM or Great Britain.

Secondary Class 1 contributions are payable in respect of employees who have reached state pension age in the same way as for employees who have not done so.

## *Section 15*

### **4. RATES**

The rate of Class 1 contributions payable in respect of an employee depends on whether the employee's employer has contracted out of the State Second Pension on behalf of the employee and instead allowed the employee to join their occupational pension scheme. If the employer has done so, both the employee and the employer will pay contributions at a lower, contracted-out rate.

Members of appropriate personal pension schemes pay contributions at the not contracted-out rate (as do their employers), but the Department of Social Care pays a rebate of contributions to the employee's pension scheme provider. They will receive a private pension in respect of those contributions (and any others made) rather than an additional State pension.

### **5. ABSENCES ABROAD**

There is a legal requirement for an employer to pay Class 1 NI contributions on all earnings paid to an employee during the first 52 weeks the employee is working abroad, provided the following three conditions are satisfied:

- (i) the employer has a place of business in the IOM;
- (ii) the employee is ordinarily resident in the IOM; and
- (iii) the employee was resident in the IOM immediately before starting work abroad.

### **6. DIFFERENCES BETWEEN THE IOM AND THE UK**

Except for the Upper Earnings Limit (see below) Class 1 earnings limits and thresholds in the Isle of Man are identical to those in the UK. Contributions paid by employees in either country give rise to the same contributory benefits.

However, there are some differences between the two countries' systems of contributions, for example

- the weekly upper earnings limit for 2010/11 is £730 in the Isle of Man but £844 in the UK;
- unlike in the UK, Class 1A and Class 1B (secondary contributions only) are not payable by employers in the IOM;
- the Inland Revenue "IR 35" provisions regarding workers supplied to clients by their own service company do not operate in the IOM; and
- Class 1 contributions payable in respect of certain items provided to employees (such as share options) are calculated in a different way in the IOM than in the UK.

## **CLASS 2 NATIONAL INSURANCE CONTRIBUTIONS**

### **1. INTRODUCTION**

#### **1.1 GENERAL**

Class 2 contributions are paid by self-employed earners. A person is self-employed if he is gainfully employed in the IOM other than as an employed earner. In practice this generally means a person who has his own business or is engaged in a series of separate contracts for services.

Class 2 contributions are payable at a weekly flat rate.

#### **1.2 Leaflet – NI2(IOM)**

#### **1.3 Telephone contact - 685177**

### **2. CONDITIONS**

Class 2 contributions are paid for every week in which a person is self-employed (including holiday periods) if they are:

- aged 16 or over; and
- under state pension age (see page 79).

There is no liability to pay Class 2 contributions if the self-employed person

- is granted Small Earnings Exception (SEE) because they anticipate they will have only a small amount of profits for that period (see paragraph 5);
- is a married woman or widow (see page 107) with a valid certificate of election not to pay Class 2 contributions;
- is, for a complete contribution week,
  - \* sick and claiming Incapacity Benefit;
  - \* available for work and claiming Jobseeker's Allowance; or
  - \* in legal custody; or
- receives, for a complete contribution week,
  - \* Carer's Allowance;
  - \* Unemployability Supplement; or
  - \* Maternity Allowance.

### **3. RATES OF CLASS 2 CONTRIBUTIONS**

Class 2 contributions are payable at a flat rate (£2.40 per week for the 2010/11 tax year).

There is a special, higher rate for share fishermen which enables those contributions to count towards entitlement to Contribution-based Jobseeker's Allowance.

### **4. PAYMENT**

There are two methods of paying Class 2 contributions:

- monthly by cash or cheque at Markwell House, Market Street, Douglas IM1 2RZ or any other Social Security office; or
- monthly by direct debit

#### **Direct debit**

An automatic deduction from a bank or building society account is made on the second Friday of each month. The month starts on the Sunday of the week when the self-employed person signs the direct debit form.

## *Section 15*

### **5. SMALL EARNINGS EXCEPTION**

A self-employed person can apply to the Department to be excepted from paying Class 2 contributions if they expect their net profits in that year to fall below a set amount. This excuses them from a legal obligation to pay Class 2 contributions. However, as the person will not be awarded NI credits for the period, the granting of exception could affect their future contributory benefit entitlement. Applications for small earnings exception can also be backdated for up to 13 weeks from the date of claim.

### **6. ABSENCES ABROAD**

Class 2 contributions can be paid on a voluntary basis if a person has no liability to pay contributions while they are working abroad.

They can be paid whether the person is working abroad as an employed earner or a self-employed earner provided they satisfy the following conditions:

- they lived in the IOM for a continuous period of at least 3 tax years at any time before the period for which the contributions are to be paid; or
- before going abroad they paid NI contributions for three whole tax years or more; and
- they are working abroad but are not liable to pay Class 1 contributions; and
- either they were an employed or self-employed earner immediately before going abroad, or would ordinarily have been an employed or self-employed earner, however were unemployed immediately before going abroad.

### **7. DIFFERENCES BETWEEN THE IOM AND THE UK**

No differences exist other than the differences in the methods of payment of Class 2 contributions in the two countries.

## **CLASS 3 NATIONAL INSURANCE CONTRIBUTIONS**

### **1. INTRODUCTION**

#### **1.1 GENERAL**

Class 3 contributions are known as voluntary or non-employed contributions and may be paid in order to count towards entitlement to long-term contributory benefits, such as Retirement Pension and Bereavement Benefits, if a person does not have a sufficient earnings factor from NI contributions or credits to make it a qualifying year.

**1.2** Telephone contact - 685177

### **2. CONDITIONS**

Class 3 contributions may be paid if a person

- is aged 16 or over and under State pension age (see page 79)
- satisfies the prescribed conditions of residence and presence in the IOM; and
- does not have a married woman's reduced rate election in force for the tax year concerned.

Class 3 contributions cannot be paid

- for a tax year which includes the 60<sup>th</sup> birthday of a woman or the 65<sup>th</sup> birthday of a man;
- in respect of a woman, if she is aged 50 or over and receives Widow's Pension, unless the Department advises her to pay Class 3 contributions;
- in respect of a woman, if she receives Widowed Parent's Allowance and will still receive it when she reaches age 50, unless the Department advises her to pay Class 3 contributions;
- for a tax year prior to April 2010 in which a person was entitled to Home Responsibilities Protection (HRP – see page 105);
- for a tax year in which a person was awarded 52 carer's credits
- in respect of a woman, if she is a married woman or widow with a certificate of election for reduced rate liability (see page 107);
- by a person who is an employed or self-employed earner in the same tax year as the one for which they want to pay Class 3 contributions, before the end of that tax year; or
- by a man, if he is aged 60 or over and qualifies for credits by virtue of his age for the deficient tax years (however, men aged 60 to 64 may wish to pay Class 3 contributions to satisfy the contribution conditions for the Pension Supplement (if they are permitted to do so)).

### **3. PAYMENT**

Class 3 contributions can be paid

- monthly by direct debit; or
- monthly by cash or cheque at Markwell House, Market Street, Douglas IM1 2RZ or any Social Security office

The cost of Class 3 contributions for the 2010/11 tax year is £12.05 per week.

Class 3 contributions must be paid before the end of the sixth tax year after the one in which they were due.

### **4. ABSENCES ABROAD**

Class 3 contributions can be paid whilst abroad - whether the person is working or not - but not for a period for which liability for Class 1 contributions exists (which will be for at least the first 52 weeks if working abroad).

To be able to pay Class 3 contributions whilst abroad, either of the following 2 conditions must be satisfied:

- the contributor was resident in the IOM for a continuous period of three tax years at any time before the period for which the contributions are to be paid; or



## *Section 15*

- before going abroad they paid NI contributions for at least 3 whole tax years.

### **5. DIFFERENCES BETWEEN THE IOM AND THE UK**

No differences exist other than the differences in the methods of payment of Class 3 contributions in the two countries.

## **CLASS 4 NATIONAL INSURANCE CONTRIBUTIONS**

### **1. INTRODUCTION**

#### **1.1 GENERAL**

Class 4 contributions are profits-related contributions payable by the self-employed (including share fishermen) in addition to Class 2 contributions, but do not count towards entitlement to any Social Security benefit. They help to share the cost of financing the contributory benefits paid to all equitably between employed earners and self-employed earners.

They are paid at a given percentage on the amount of a person's annual net profits or gains exceeding a lower limit.

Married women and widows with a reduced rate election who are entitled not to pay Class 2 contributions must nevertheless pay Class 4 contributions in the normal way.

#### **1.2 Leaflet – NI2(IOM)**

#### **1.3 Telephone contact - 685177**

### **2. CONDITIONS**

Class 4 contributions are payable by self-employed people whose net profits or gains for an accounting year are above the annual lower profits limit.

Class 4 contributions are not payable by a person

- whose profits or gains are at or below the lower annual profits limit; or
- who is over state pension age (see page 79) at the beginning of the tax year of assessment equivalent to the person's accounting year; or
- who is not resident in the IOM for income tax purposes; or
- who is a diver or diving supervisor on the UK continental shelf or in UK territorial waters.

### **3. ACCOUNTING YEAR**

The accounting year is the 12-month period covered by the person's accounts. It can start on any day and may not be the same period as any tax year.

### **4. RATES OF CLASS 4 CONTRIBUTIONS**

The lower profits limit for the 2010/11 tax year is £5,715 whilst the upper profits limit is £37,960. Class 4 contributions are payable between these limits at the rate of 8%. From April 2010 Class 4 contributions at the rate of 1% are also payable on all profits above the upper profits limit of £37,960.

The Income Tax Division calculates and collects the amount of Class 4 contributions payable for any tax year, together with any income tax due, when a person submits their trading and profit and loss accounts with their tax return.

Interest is payable on outstanding Class 4 contributions as it is in respect of unpaid tax.

### **5. DIFFERENCES BETWEEN THE IOM AND THE UK**

A deduction of 20% is made by the Assessor of Income Tax in the amount of Class 4 contributions payable. Equivalent tax relief was granted to those liable to pay Class 4 contributions in the UK until the 1996/97 tax year when the rate of Class 4 contribution was reduced. Despite the same lower rate of contribution also being payable in the IOM, the Assessor of Income Tax has maintained a deduction in the amount of Class 4 contributions payable (which was 20% at that time).

The upper profit limit in the UK is £43,875 for the 2010/11 tax year.

## **CREDITS FOR PARENTS AND CARERS**

### **1. GENERAL**

Weekly NI credits for parents and carers have been introduced from 6<sup>th</sup> April 2010 to help them build up qualifying years for the basic State Pension and additional State Pension, as well as Widowed Parent's Allowance and Bereavement Allowance. These credits replace Home Responsibilities Protection (HRP), which was previously awarded to parents and carers (see page 105).

For people reaching State pension age on or after 6<sup>th</sup> April 2010, complete tax years of HRP built up before 2010 have been converted into qualifying years for pension purposes, up to a maximum of 22 years.

### **2. WHO IS ENTITLED TO CREDITS FOR PARENTS AND CARERS?**

Credits will be awarded automatically to a person for each week they

- are awarded Child Benefit for a child under the age of 12; or
- are entitled to Carer's Allowance.

A person can also qualify for Carer's credits for any week throughout which they are

- an approved foster carer;
- looking after one or more persons for a total of 20 hours or more per week (but not receiving Carer's Allowance);
- in receipt of Income Support because they are looking after a sick or disabled adult or child; or
- although not the person awarded Child Benefit for a child under the age of 12, they wish to transfer credits from the Child Benefit claimant's National Insurance account to their National Insurance account

however in these circumstances a person will have to make a written application to the Department for Carer's credits.

## **HOME RESPONSIBILITIES PROTECTION**

### **1. INTRODUCTION**

#### **1.1 GENERAL**

Since April 1978, Home Responsibilities Protection (HRP) has existed to protect contribution records of those persons unable to work as they have to care for someone at home. This means that they will not be liable to pay contributions. This is specifically for the purposes of entitlement to the basic State Retirement Pension, Widowed Parent's Allowance and Bereavement Allowance, all of which rely on contribution conditions being satisfied.

HRP is awarded for complete tax years only and reduces the number of tax years in a person's working life for which they must satisfy contribution conditions in order to gain entitlement to any of the 3 long-term contributory benefits referred to above.

#### **1.2 HRP AND THE STATE SECOND PENSION**

With the introduction of the State Second Pension (S2P) from 6<sup>th</sup> April 2002, persons who are not in employment will also be able to build up entitlement to an Additional Pension in certain circumstances.

Those persons are:

- persons caring for others who are entitled to Carer's Allowance throughout any tax year;
- persons unable to work because they are responsible for bringing up a child under 6 years of age or are otherwise regularly and substantially engaged in caring for another person and who are awarded HRP; and
- registered foster carers (from 6<sup>th</sup> April 2003 only).

#### **1.3 Leaflet - CF 411**

#### **1.4 Telephone contact - 685177**

### **2. QUALIFYING CONDITIONS**

A person can qualify for HRP for any tax years from April 1978 if, throughout the year

- they are the main payee getting Child Benefit for a child under 16;
- they have been regularly caring for someone for at least 35 hours a week who has been getting Attendance Allowance, Constant Attendance Allowance, or the highest or middle rate of the care component of Disability Living Allowance for at least 48 weeks in any tax year from April 1988 onwards;
- they have been getting Income Support and looking after a sick or disabled person at home; or
- they have satisfied a combination of the above conditions in any tax year.

HRP

- can be given for years for which a self-employed Small Earnings Exception certificate is held;
- cannot be given for years in which a married woman's reduced rate election is in force;
- cannot be given for years already qualified for long-term contributory benefit (Retirement Pension, etc.) purposes; and
- cannot be given for any period prior to 6<sup>th</sup> April 1978.

### **3. Home Responsibilities Protection after April 2010**

With effect from the 6<sup>th</sup> April 2010 Home Responsibilities Protection (HRP) has been replaced by Carers Credits. For complete tax years prior to April 2010 that you were awarded HRP you will now be awarded 52 credits. These credits will continue to help protect a persons entitlement to State Retirement Pension, Widowed Parent's Allowance and Bereavement Allowance. The maximum number of years of HRP you can be credited with is 22.

## *Section 15*

### **4. NOTES**

HRP cannot reduce the number of tax years in a person's working life for which they must have had (or been credited with) sufficient earnings or paid contributions to make that year a qualifying year for entitlement to long-term contributory benefits to below 20 (for a woman) or 22 (for a man) or half the number of years in a person's working life if it is less than 44 years for a woman or 49 years for a man.

## **REDUCED LIABILITY FOR MARRIED WOMEN AND WIDOWS**

### **1. INTRODUCTION**

#### **1.1 GENERAL**

A married woman under State Pension age (see page 79) will generally have to pay standard rate NI contributions when she is working. However, a woman who married before 6<sup>th</sup> April 1977 could have elected both to pay reduced rate Class 1 NI contributions (as an employed earner) and not to pay Class 2 (self-employed contributions) for the rest of her working life.

Reduced rate contributions give entitlement only to Industrial Injuries benefits.

#### **1.2 Telephone contact - 685177**

### **2. QUALIFYING CONDITIONS**

A woman may be eligible to pay reduced rate contributions and not to pay Class 2 contributions if she

- was married before 6<sup>th</sup> April 1977 and elected to pay at the reduced rate before 11<sup>th</sup> May 1977;
- was widowed before 6<sup>th</sup> April 1978 and already had the right to reduced liability; or
- was widowed on or after 6<sup>th</sup> April 1978 and had reduced rate liability immediately before widowhood.

### **3. CERTIFICATE OF ELECTION**

A married woman or widow holding a certificate of election pays primary Class 1 contributions at a reduced rate of 4.85% on all her earnings falling between the primary earnings threshold and the Upper Earnings Limit.

### **4. REDUCED RATE ELECTION**

Reduced rate election means

- Class 1 contributions are payable at a reduced rate;
- if the woman is self-employed, she is not liable to pay Class 2 contributions;
- credits cannot be awarded to her during the period of reduced rate election;
- HRP cannot be awarded for any year in which there is reduced rate liability

Reduced rate contributions do not count towards entitlement to contributory benefits. The woman would instead have to rely on her husband's contribution record for long-term contributory benefit purposes; and

Class 3 contributions cannot be paid for any tax year throughout which the election continues in force.

Reduced rate election does not affect:

- an employer's liability to pay secondary contributions in respect of the woman;
- the woman's liability to pay Class 4 contributions; or
- the woman's entitlement to Industrial Injuries Disablement Benefit.

Entitlement to pay reduced rate contributions and not to pay Class 2 contributions ends:

- when the woman revokes her election to pay reduced rate contributions;
- when the marriage ends in divorce or annulment;
- at the end of the tax year in which the widow ceases to satisfy the conditions for entitlement to bereavement benefits (but not by virtue of getting remarried); or
- if there is a period of two consecutive tax years after 5<sup>th</sup> April 1978 during which the woman has not been

- \* liable to pay Class 1 contributions; or

## *Section 15*

- \* self-employed.

### **5. CHANGING TO FULL RATE CONTRIBUTIONS**

Before changing to full rate contributions, a woman should remember that she

- cannot subsequently reinstate her reduced rate election, and
- may not pay enough full rate contributions before the tax year in which she reaches the age of 60 (after which she cannot pay contributions) to gain entitlement to a full basic pension based on her own contribution record. However, even if she may not qualify for a basic pension in respect of those full rate contributions, she might nevertheless qualify for additional pension (the State Second Pension) in respect of such contributions.

Any woman considering a change to full rate contributions should get a Retirement Pension forecast from the Retirement Pension Forecast and Advice Unit, 2<sup>nd</sup> Floor, Markwell House, Market Street, Douglas or any district office (see page 125) before coming to a decision.

Note: The UK Pensions Act 2007 provides, inter alia, that for those who will attain state pension age on or after 6<sup>th</sup> April 2010 every qualifying year will provide some pension entitlement. This change will also apply in the Isle of Man.