EXPLANATORY MEMORANDUM TO

THE FINANCIAL ASSISTANCE SCHEME (MISCELLANEOUS AMENDMENTS) REGULATIONS 2010

2010 No.

1. This explanatory memorandum has been prepared by the Department for Work and Pensions (DWP) and is laid before Parliament by Command of Her Majesty.

2. Purpose of the instrument

The Financial Assistance Scheme (FAS) provides help to members of certain occupational pension schemes who have lost part or all of their pensions as a consequence of their scheme winding up without having sufficient assets to pay full pension benefits. These Regulations complete the legislative implementation by allowing part of the funding of an enhanced level of the FAS to be achieved through the transfer of pension scheme assets to government and for the FAS to make payments to those pension scheme members whose assets are taken over by government and who would otherwise have been paid solely by their pension schemes.

3. Matters of special interest to the Joint Committee on Statutory Instruments

3.1 The Regulations (among other things) provide for transfer of assets from qualifying schemes that have not yet completed wind-up to the Secretary of State. Such provision is made under section 286(1) of the Pensions Act 2004. Section 286 confers a wide power on the Secretary of State to make regulations to provide a financial assistance scheme. Section 286(3) sets out some of the ways in which this power may be used. This includes (at paragraph (c)) for properties, rights and liabilities to be transferred to the scheme manager. Section 286(3) also provides that the regulations may include such incidental, supplementary and consequential provision as appears to the Secretary of State to be expedient.

3.2 The power was widely drafted because, at the time it was debated and enacted, it was not clear how best the FAS might be delivered. When the clause was debated in Parliament, it was made clear that there were a number of options which might need to be considered. The then Minister, Malcolm Wicks, stated that it would be necessary to explore "the options for operational delivery, on which a number of alternatives are available. Some alternatives involve running on schemes and topping them up, while others involve winding up schemes and providing assistance. Options for delivery might include that undertaken by the DWP, an industry-led body or a stand-alone trust."[1]. Regulations under section 286 were made subject to the affirmative procedure in order to give both Houses an opportunity to consider and debate the eventual operational and delivery structures.

3.3 Over the years since the Pensions Act 2004 was enacted, the Department has given a great deal of consideration to the ways in which the needs of those for whom the FAS is provided would best be met, while maintaining the balance of best value for the taxpayer. Following the Young Review (more detail of which is

[1] Hansard: 19 May 2004, column 984

given below), it was concluded that the best value would come from government absorbing all residual assets in the schemes (the second option suggested by the Minister in the debate cited above). It was also considered that the most efficient way of running the scheme would be for the Board of the Pension Protection Fund (PPF) to take on the role of scheme manager, a role which had previously been performed by the Secretary of State, given their expertise in this area and the similarities between managing the PPF and FAS. This change was made in the Financial Assistance Scheme (Miscellaneous Provisions) Regulations 2009 (S.I. 2009/1851) and the PPF has been in place as scheme manager since 10 July 2009.

3.4 As set out above, these Regulations make provision for assets to transfer to the Secretary of State rather than to the scheme manager. The Secretary of State retains responsibility for funding FAS payments made by the scheme manager and so it is right that assets that are to be used to fund those payments should be transferred to the Secretary of State.

3.5 The Department considers that making such provision falls well within the terms of section 286(1) as supplemented by section 286(3) and, indeed, within the expectation and intention of Parliament. It is clear that the list at section 286(3) both amplifies and illustrates the way in which section 286(1) can be used, giving as much of an indication of the scope of the broad power in section 286(1) as was possible at the time when it remained unclear as to how exactly it might need to be used.

3.6 The sub-paragraphs of section 286(3) do not simply provide a list of matters which a person would not usually expect a broad power such as section 286(1) to extend to. It is there to give as clear an indication as possible as to the types of provision regulations under that power could include. As a result, it makes reference to matters which would clearly fall within the expected scope of subsection (1), for example:

- prescribing the person who may manage the scheme (sub-paragraph (a))
- for the scheme manager to manage and apply a fund in accordance with the regulations or a deed of trust (sub-paragraph (b))
- circumstances in which payments are to be made (sub-paragraph (d))
- providing for review and appeals of determinations (sub-paragraph (g));

as well as including a provision which, because of the technical nature of the power, would not be possible under subsection (1) without that specific reference (sub-paragraph (j) - the power to apply any provision in Parts 1 and 2 of the Pensions Act 2004 with modifications).

3.7 Sub-paragraph (c) is not a provision which is technical in nature like sub-paragraph (j). Sub-paragraph (c) shows that the power in section 286(1) is broad enough to allow for pension scheme assets to be transferred so that they can be used in connection with assistance payments. It does not limit the Secretary of State's powers under section 286(1) to providing for transfer of assets to the scheme manager only.

3.8 The provisions within these Regulations are directly analogous to the illustrative example provided in sub-paragraph (c) and in that context are within the terms of the power.

3.9 Provision is also made at regulation 31 allowing the Secretary of State to modify terms of contracts transferred. This provision is made under the general power in section 286(1) as supplemented by the provision in section 286(3) in relation to transfer of assets and incidental, supplementary and consequential provision. The Committee's attention is drawn to the powers at section 161(6) of the Pensions Act 2004 in relation to the PPF under which regulation 2 of the Pension Protection Fund (General and Miscellaneous Amendments) Regulations 2006 (S.I. 2006/580, Board's power to modify relevant contracts) is made. The Committee will note that the power under section 161(6) is framed broadly, simply providing that regulations may make provision regarding transfers and that regulation 31 of these draft Regulations is made in almost identical terms to regulation 2 of the 2006 Regulations. The provision is necessary to ensure that the scheme manager and Secretary of State are not required to honour terms of a contract which are unusually onerous. These might be terms agreed by a particular scheme in anticipation of transfer and discharge from liabilities. The provision will not used lightly. The scheme manager, as a public body, is bound by the Human Rights Act 1998 (c.42) and is also subject to judicial review in relation to any of its decisions. The Committee may wish to note that the equivalent power in the 2006 Regulations has not so far been invoked although its application has been discussed with schemes and the power remains a necessary protection.

4. Legislative context

4.1 In April 2007 the Government asked Andrew Young to carry out the 'Financial Assistance Scheme Review of Assets'[2] (the 'Young Review'). The review concluded that, to provide a guaranteed benefit level, the best value would come from government taking in all remaining assets in FAS qualifying schemes and taking responsibility for making all associated payments to scheme members.

4.2 On 17 December 2007, in response to the Young Review, the Government announced (Written Statements 17 December 2007; Hansard Columns 100WS to 102WS[3]) a package of measures to extend the FAS and its intention to part fund those extensions by taking in the remaining assets of FAS schemes.

4.3 The extensions have been introduced through a series of affirmative Statutory Instruments, prioritised to ensure that increases in benefits were introduced as quickly as possible. In addition, in preparation for the transfer of pension scheme assets and making the payments associated with that transfer, responsibility for the management of the FAS was transferred to the Board of the Pension Protection Fund (PPF), which became the FAS scheme manager on 10 July 2009.

5. Territorial extent and application

This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

[2] See DWP website at: http://www.dwp.gov.uk/policy/pensions-reform/fas-review-of-scheme-assets/ .

[3] http://www.publications.parliament.uk/pa/cm200708/cmhansrd/cm071217/wmstext/71217m0007.htm#07121714000025

The Minister of State for Pensions and the Ageing Society has made the following statement regarding Human Rights:

"In my view the provisions of the Financial Assistance Scheme (Miscellaneous Amendments) Regulations 2010 are compatible with the Convention rights."

7. Policy background

- ***What is being done and why***

7.1 The FAS deals with pension schemes that wound up underfunded during particular dates (generally between 1 January 1997 to 5 April 2005), and provides assistance by way of a top-up to a scheme member who receives a pension below 90 per cent of their accrued pension at the commencement of wind up, from their pension scheme.

7.2 In broad terms pension schemes offer 2 types of benefits:

- money purchase benefits, where essentially all member and employer contributions are collected in an individual pot for the member. The final pot together with investment returns are used to secure a pension for the member at retirement;

- defined benefits, where the calculation of benefits do not relate to the value of the member's pot but instead are calculated according to a formula generally taking account of the member's length of service and final salary.

The FAS provides assistance in respect of defined benefits but does not provide assistance in respect of money purchase benefits.

7.3 Under current arrangements, schemes typically discharge all member liabilities by buying annuities from insurance companies. In line with recommendations in the Young Review, the Government intends to take in the defined benefit assets remaining in FAS qualifying schemes which have not yet completed wind up, in order to partly fund an extension to FAS benefits. In doing so, those members who would have received more than 90 per cent of their expected pension from their scheme, and who therefore would not have previously qualified for a FAS top-up payment, should now become qualifying members of, and paid from, the FAS. It is intended that these members will receive payments equivalent to those they could have expected to receive had their scheme continued to wind up and buy an annuity for them.

7.4 Certain members will be able to commute part of their assistance for a lump sum, which will be calculated broadly in line with tax rules on pension commencement lump sums. Where the member's share of scheme assets is less than this amount, the maximum lump sum which can be taken will be the amount of the member's asset share.

7.5 In taking in scheme assets and making payments to the new category of member, additional information will be needed from scheme trustees in order to value scheme assets and pay the new category of members.

- ***The changes***

Restrictions on trustees or managers of FAS qualifying schemes in providing their members with transfers out, winding up lump sums and trivial commutation payments.

7.6 In order to preserve the residual assets of FAS qualifying schemes, Regulations already place restrictions on the discharge of members' pensions through the purchase of annuities. In order to further preserve the assets, these Regulations also place a halt on such schemes providing members with other relevant types of discharge payments (including transfers of pension rights into other pension scheme arrangements). However, in recognition that some members may have applications for transfers in the pipeline before the restrictions come into force, the Regulations include provisions to allow transfer applications to be honoured where members have -

- received statements of entitlement from their schemes; and
- made a valid application to take up payments.

7.7 The Regulations also provide for relevant transfer or lump sum payments to be payable in the following circumstances:

- in respect of any money purchase rights (money purchase rights are disregarded by the FAS);
- in respect of the discharge of benefits deriving from voluntary contributions;
- in respect of any pension sharing order (made by the courts as part of divorce settlements) ; and
- where trustees make applications for payments that are approved by the FAS scheme manager.

Identifying those schemes and members whose assets will be transferring to government

7.8 Not all FAS qualifying schemes will be transferring assets to government. Some schemes will already have fully wound up or will fully wind up; for example, if they are exempt from the current restriction on the purchase of annuities for FAS qualifying schemes. The Regulations ensure that such schemes are not subject to the valuation and transfer requirements necessary for schemes transferring assets to Government.

7.9 Some FAS schemes will contain a mix of beneficiaries, some of whom will have had their liabilities discharged and some who have not. The Regulations provide that the valuation and asset transfer provisions only relate to beneficiaries who will not have their liabilities otherwise discharged.

The FAS Valuation

7.10 Under the transfer arrangements described in this memorandum, defined benefit pensions in respect of relevant beneficiaries will be replaced by assistance payments for those with immediate entitlement under FAS rules or prospective assistance payments for those not yet entitled, where beneficiaries are not yet entitled to receive payment) on the transfer of the scheme's assets to government.

7.11 The Regulations set out that schemes will carry out a calculation to determine the value of the scheme's assets which are available to discharge liabilities in respect of relevant beneficiaries. This asset share will enable a 'notional pension' to be calculated, which will be used by the FAS scheme manager to determine whether a person stands to receive payments higher than would otherwise be payable by the FAS. The level of a beneficiary's asset share may also affect the amount of assistance they are able to take as a lump sum.

7.12 The Regulations provide that the FAS scheme manager must instruct the trustees or managers of relevant schemes to obtain a valuation and allocation of assets for FAS purposes.

7.13 Under the Regulations, the valuation will be undertaken by an actuary – the 'valuation actuary' – who will be approved by the FAS scheme manager. The valuation actuary will usually be the scheme actuary, but there is flexibility in the Regulations for the FAS scheme manager to appoint another actuary where, exceptionally, it is considered that they are more suited to the task.

7.14 The Regulations provide that the valuation actuary should be responsible for producing a valuation that establishes:

- the value of the assets of the scheme;
- the value of the liabilities of the scheme for relevant members; and
- relevant members' asset shares.

The Regulations provide that guidance may be published by the Secretary of State for actuaries calculating asset shares and valuing certain assets. Draft guidance will be published for consultation in January 2010 and will be available on the DWP website at http://www.dwp.gov.uk/consultations/.

Placing a value on the assets of the scheme

7.15 Scheme accounts should generally provide the starting point for the valuation actuary's valuation of the assets of the scheme for FAS purposes.

7.16 However, the Regulations also set out circumstances in which assets and liabilities can be disregarded in the valuation – for example those in respect of money purchase pension benefits which are not intended to transfer to government.

7.17 The Regulations also set out how certain assets should be valued, including debts owed to the scheme. Provisions also allow for asset values to be adjusted by the valuation actuary or the FAS scheme manager in certain circumstances. Throughout, the Regulations provide for the valuation of assets and any adjustments to those values to be undertaken in line with guidance provided by the Secretary of State.

Establishing liabilities and allocating assets

7.18 The guidance will set out how the asset share in respect of each beneficiary is to be calculated. The Government intends that assets should be allocated in line with the appropriate priority order. This will be either under section 73 of the Pensions Act 1995 in force at the time wind up began or, where wind up began before these provisions came into force, in line with scheme rules.

7.19 Under certain statutory priority orders made under section 73, certain pension benefits are valued on a 'full buy-out basis' reflecting the cost of purchasing annuities from insurers to secure benefits. As most transferring schemes will not have such quotes available and in order to ensure consistency between FAS qualifying schemes guidance will set out a 'synthetic buy-out' basis (i.e. a method for approximating the cost of buying out benefits with insurers) which should be applied by the valuation actuary in order to value relevant liabilities.

Waiving elements of the FAS valuation

7.20 The Government recognises that there will be occasions in which full valuations would not be necessary or appropriate. One example is where a scheme's funding position is such that all remaining assets would be allocated to pensioner members, none of whom would stand to receive payments above standard 90% of FAS levels were asset shares and notional pension to be calculated. To allow for flexibility, the Regulations provide for the FAS scheme manager to be able to limit certain valuation requirements for FAS purposes.

7.21 The Government expects the FAS scheme manager to work with trustees to actively identify such cases and ensure that valuations are appropriate to the circumstances of each scheme.

When will the valuation be undertaken?

7.22 The Regulations provide for the FAS scheme manager to determine when the valuation should be undertaken. This is so that the FAS scheme manager can ensure that the necessary preparation tasks – such as bringing member information up to date or the recovery of debts – have been satisfactorily completed before proceeding with the valuation and subsequent discharge of trustees from their liabilities in respect of the scheme.

7.23 As is the convention when winding up a pension scheme, the assets and liabilities will be valued as at a specific date towards the end of wind up. The Regulations provide that the valuation calculation date will be the last day of the month in which the FAS scheme manager instructs the trustees or managers of the scheme to undertake the valuation.

Approval and finalisation of the valuation

7.24 The Regulations require that the FAS scheme manager must approve the valuation provided by the valuation actuary. This allows the FAS scheme manager to ensure that the valuation has been undertaken appropriately and that the information needed to calculate notional pensions and the subsequent FAS assistance is accurate and complete. The Regulations provide for a revised valuation to be undertaken if required.

7.25 The approval process includes a right of review for trustees should they disagree with the valuation.

7.26 The Regulations set out that the FAS scheme manager cannot proceed with the transfer of assets until the valuation is binding. The Regulations provide that a valuation is not binding until:

- it has been approved by the FAS scheme manager; and
- the period within which the approval of that valuation may be reviewed by trustees or pension scheme managers has expired; and
- any review and appeal activity is completed, following which the approved valuation remains valid.

The Transfer of assets, rights and liabilities

7.27 Once the valuation is binding, the Regulations provide that the decision as to when to proceed with the actual transfer of the assets – and when to take on responsibility for making associated payments to qualifying members will rest with the FAS scheme manager. This mirrors the approach already set out under the Pensions Act 2004 in relation to schemes eligible for the PPF. In the majority of cases the Government anticipate that transfers will happen immediately after the valuation becomes binding.

7.28 The Regulations provide for the transfer of assets to be achieved by a formal transfer notice issued electronically by the FAS scheme manager to the trustees or managers of the scheme. This too is similar to the approach used by the PPF.

7.29 The Regulations provide that on receipt of the transfer notice:

- the property and rights ('assets') held by or vested in the trustees or managers as trustees or managers of the scheme are transferred to the Secretary of State;
- certain rights and liabilities will transfer to the Secretary of State, whilst others will be discharged or remain with trustees; and
- the trustees will be discharged of remaining defined benefit pension obligations (all other defined benefit pension obligations having already been discharged).

7.30 Regulations provide for the assets to be transferred to the Secretary of State, rather than the FAS scheme manager, to ensure clear government ownership of the assets. To allow the FAS scheme manager to manage the property and rights transferred, the Regulations provide the FAS scheme manager with the same rights and powers over those assets as the Government has as the new owner of the assets.

7.31 The Government recognises that there may be outstanding legal proceedings or applications, for example to the Pensions Ombudsman, in schemes transferring assets to government. The Regulations provide flexibility for the FAS scheme manager to proceed with the transfer process if appropriate and for such legal proceedings to continue after the transfer. In such circumstances, the Regulations provide for legal cases or applications that are pending immediately before the transfer, by or against any of the trustees or managers of the qualifying scheme in their capacity as trustees or managers, to be continued by or against the Secretary of State. Under this provision, if an application by a member to the Pensions Ombudsman challenging a pension award was pending immediately before the transfer, the application would be continued against the Secretary of State.

7.32 The provisions linked to the transfer notice are intended to allow trustees to wind up the scheme by providing a discharge in respect of defined benefit pension obligations, whilst ensuring that the Secretary of State does not take on inappropriate liabilities. For example, the Regulations provide that the trustees or managers of the scheme should not be discharged of any liabilities for which they would be personally liable.

7.33 Provisions are also made to facilitate the transfer of assets by allowing for the modification of certain contracts (for example, where an insurance contract is held by a scheme); and by allowing for appropriate arrangements to be made in respect of any foreign property rights and liabilities.

Issues around money purchase assets and liabilities

7.34 The FAS only provides assistance in respect of defined benefit pensions. Money purchase liabilities and assets will need to be identified and discharged separately by the trustees of FAS qualifying schemes. However, the Government is aware of a small number of schemes where the scheme rules prevent separate discharge of defined benefit and money purchase liabilities. The Regulations allow the trustees or managers of a pension scheme to disregard the rules of the scheme in such circumstances to facilitate discharge of money purchase liabilities.

7.35 The Government anticipates that there may be occasions where trustees might be unable to discharge money purchase liabilities, for example, it is sometimes difficult for trustees to find an insurer willing to provide annuities where small amounts of assets are involved.

7.36 In order to ensure that this would not prevent a scheme from completing wind up, the Regulations provide the potential for money purchase assets to transfer to government. However, the FAS scheme manager would only consider such transfers where no other discharge options are available to a scheme and there is no intention for FAS assistance to be paid in respect of money purchase pensions. Should any such money purchase assets transfer as a last resort, the Regulations place an obligation on the FAS scheme manager to seek to discharge any such liabilities through an appropriate provider (whether an insurer or other pension arrangement).

Residual Assets held by schemes

7.37 The Regulations provide for the transfer of any residual assets left in schemes to which the transfer provisions do not apply i.e. those where trustees have discharged members' liabilities. Such residual assets may, for example, exist in schemes where assets have been over-allocated to expenses. To protect member interests this provision can only be used where the FAS scheme manager is satisfied that it would not be cost effective or beneficial to members for trustees to distribute these residual assets. This may arise, for example, in circumstances where members are receiving a pension less than FAS levels and distributing residual assets would still result in FAS top-up payments having to be made.

Assistance payments

7.38 Under these provisions the FAS will become responsible for paying individuals who, under the current system, would not come into the FAS because their schemes could provide them with a pension in excess of the FAS maximum. Changes to the assistance rules have therefore been made to ensure these individuals receive the full value of their share of scheme assets.

Notional pensions

7.39 An asset share will be calculated in respect of each beneficiary. This asset share will be turned into a 'notional pension', which represents the pension which could have been bought for the beneficiary had the scheme wound up by the purchase of annuities. This notional pension will be compared to the amount of assistance the individual would be entitled to under the normal rules, that is, the standard FAS rules. They will be paid whichever is the higher amount. For example, in some cases the underlying normal assistance could, at some point in the future, exceed the notional pension. Therefore, when the notional pension is put into payment an annual comparison will be made with normal assistance. If the normal assistance becomes higher than the notional pension, the individual will be transferred from payments based on that notional pension to payments made under normal FAS rules.

Pensioners

7.40 Pensioners include anyone in receipt of a pension from their scheme when these Regulations come into force and anyone who has indicated to the scheme, before this date, that they want their pension to be put into payment. Their notional pension will reflect the scheme rules on revaluation and survivor benefits (such as widows' pension). Annual increases (indexation) will be provided at the level of the Retail Prices Index, capped at 2.5 per cent.

7.41 Where the asset share is insufficient to cover all of these aspects, the asset share will first be put to covering the pension in payment. If, once this has been covered, assets remain, these shall be put to providing the indexation described above on as much of the payment as possible. This should ensure that anyone receiving a pension from their scheme when the Regulations come into force is unlikely to see the amount of their payment go down unless their scheme has been paying them more than their asset share could have provided at the end of wind up. If the asset share is more than sufficient to cover both the pension in payment and indexation at 2.5 per cent it will be put to increasing the headline rate of indexed pension.

Non pensioners

7.42 The notional pension of anyone not receiving a scheme pension when these Regulations come into force will reflect the normal FAS assistance structure.

Survivors/surviving dependants

7.43 The Regulations follow a similar process for calculating payments to survivors or surviving dependants. The date for determining whether a survivor should have a scheme-shaped or FAS-shaped notional pension calculated in respect of them will be the date of the member's death. This will ensure payments of FAS assistance are not dependant on how long the pension scheme has taken to start making payments to any survivor or surviving dependants.

Commutation of assistance

7.44 These Regulations allow certain qualifying members to commute part of their FAS assistance into a lump sum at the point their assistance is first put into payment. Those eligible are members entitled to FAS assistance as the result of a scheme pension based on their own contributions and who, at the point the scheme assets transfer to government, have yet to start receiving a pension from their scheme.

7.45 The amount that can be commuted will be calculated broadly in line with tax rules on pension commencement lump sums. Where the member's share of scheme assets is less than this amount, the maximum lump sum which can be taken will be the amount of the member's asset share (reflecting the maximum amount which a member could have taken as a lump sum if an annuity had been purchased with that asset share).

7.46 HM Revenue & Customs is planning to bring forward regulations which will, subject to Parliamentary approval, provide tax exemption for this assistance lump sum.

7.47 Where the individual chooses to commute part of their entitlement, their ongoing FAS assistance will be reduced. This will have an effect on any survivor payments made in the event of that individual's death.

Members entitled to FAS assistance on the grounds of ill health

7.48 Qualifying members in ill health can be paid assistance before their normal retirement age. Those who have a reduced life expectancy can be paid unreduced FAS assistance, whilst reduced assistance can be paid without evidence of reduced life expectancy.

7.49 For consistency and in order to allow appropriate comparisons to be made, the Regulations provide that all notional pensions to members who qualify for FAS payments on the grounds of ill health will be payable from the earlier of the date that they started to receive their scheme pension (but no earlier than the start of wind up) and the date they started to receive assistance.

7.50 The Regulations do not apply an early payment reduction factor to the notional pensions of those receiving a scheme pension before the Regulations come into force under any ill health payment scenario.

7.51 Where a member was not receiving a scheme pension at the valuation calculation date a reduction factor will be applied to the notional pension where one is required for an appropriate comparison to be made with any normal FAS entitlement on the grounds of ill health. This means that where a member is entitled to unreduced FAS assistance on the grounds of reduced life expectancy, no reduction will be made to the notional pension. Where a member is entitled to reduced assistance, a comparable reduction will be made to the notional pension.

Death benefit guarantees

7.52 The Regulations also provide for the payment of any outstanding death benefit guarantee where a member has a scheme-shaped notional pension which is higher than normal assistance. Death benefit guarantee periods operate where a member of a pension scheme dies within a specified period, usually five years but in some cases ten years, of their pension being put into payment. The guarantee is in place in order to ensure that members get at least a minimum return for the contributions they have made into the schemes.

Reconciliation of interim pension payments and FAS initial payments

7.53 When a member of a FAS qualifying pension scheme becomes entitled to a payment from that scheme before the scheme has completed winding up, the trustee is usually unable to calculate exactly how much to pay until wind up completes and so makes an *interim* pension payment on account of entitlement. The FAS can also make *initial* payments on account of assistance entitlement.

7.54 When the pension scheme completes wind up and the member's final entitlement from the pension scheme and the final assistance payment can be calculated, there is a need to reconcile past payments to ensure the individual receives the correct amount of assistance over their lifetime. Where the amount of scheme interim pension and initial FAS payments received by the member is higher than their final FAS assistance, the FAS scheme manager can recover the excess payment by reducing the member's ongoing assistance payment; the recovery is spread over their lifetime. If the amount of scheme interim pension and initial FAS payments received by the member is lower than their final FAS assistance, the FAS scheme manager can make a lump sum payment to the member.

7.55 The Financial Assistance Scheme Regulations 2005 (as amended) currently only provide for interim pensions paid by the scheme during the period for which an individual would be entitled to assistance – from the later of 14 May 2004 or a member's normal retirement age – to be taken into account by the FAS scheme manager so any interim pensions paid during any period of wind up prior to 14 May 2004 remain the responsibility of the trustees.

7.56 As the new Regulations provide for FAS qualifying pension schemes' remaining assets to be taken into government, it removes the ability for trustees to reconcile interim pensions paid during any period of wind up before 14 May 2004. Therefore, the Regulations extend the existing reconciliation provisions to enable the FAS scheme manager to take into account any interim pension paid from the start of scheme wind up, which may involve periods prior to 14 May 2004. This ensures that members receive the correct entitlement from both their scheme and from the FAS over their lifetime.

7.57 The new Regulations also provide the same reconciliation powers for members who will be paid at the level of their notional pension when their scheme transfers assets to government. Such members will be those whose share of scheme assets is higher than FAS levels and will include those who have no entitlement to FAS (for instance survivors outside the FAS survivor definitions or those who have retired before reaching their FAS entitlement date) The Regulations enable the FAS scheme manager to compare interim pension payments with their notional pension and to make arrears payments where the interim pension received was less than their notional pension or to reduce future notional pension payments where interim pensions were paid in excess of the amount of the notional pension. They also provide for the FAS scheme manager to take into account interim and notional pension payments made prior to FAS entitlement when comparing the notional pension and normal assistance entitlement of a member who started to receive their scheme pension before becoming entitled to assistance.

Delegation

7.58 The Regulations provide for the operation of certain functions to be delegated by the scheme manager to a third party. The newly delegated functions are the:

- calculation of notional pensions and related activity;
- calculation of payments under new schedules to the regulations;
- exercising of the rights, powers and obligations of the Secretary of State in relation to the property, rights and liabilities transferred;
- handling of arrangements in respect of foreign assets; and
- handling of any transferred money purchase assets.

Information requirements

7.59 The Regulations introduce a requirement for trustees and managers to provide information relating to the scheme's assets and debts, including details of significant debts, to assist with the planning for the transfer of the remaining assets. This information is required within 28 days of the later of the coming into force of the Regulations, the date the scheme manager notifies a scheme that it has determined that the scheme is a FAS qualifying pension scheme or the date the pension scheme becomes aware of the amount of any asset or debt. The FAS scheme manager has the flexibility to extend the 28 day timescale if considered appropriate to do so. Guidance will be provided to trustees and managers by the FAS scheme manager in relation to these requirements, including on when a debt would be considered 'significant'.

7.60 The Financial Assistance Scheme (Provision of Information and Administration of Payments) Regulations 2005 currently requires potential beneficiaries of FAS qualifying schemes to provide information required by the FAS scheme manager within two months of its request and enable the FAS scheme manager to extend this timescale where it considers appropriate. In light of operational experience, these Regulations reduce to two months, the six month period in which to provide information, whilst retaining the flexibility for the FAS scheme manager to extend the deadline as it considers appropriate.

7.61 Information from Her Majesty's Revenue and Customs' National Insurance Pay As You Earn System (NPS) has been accessed in the past by the DWP's FAS Operational Unit where the information has been necessary to the calculation and payment of assistance. As the FAS is now administered by the Board of the PPF, the existing DWP access rights do not apply. The Regulations therefore modify section 202 of the Pensions Act 2004 (a data sharing provision with the PPF which covers tax information) to enable the sharing of data held on the NPS in respect of the administration of the FAS.

7.62 To ensure that the FAS scheme manager does not over-burden scheme trustees or managers with providing information that is already held or unnecessary, the Regulations give the FAS scheme manager discretion to waive some, or all, of the information requirements. In addition, the Regulations remove the requirement to provide trustee details in annual payment and ill health payment determination notices where the trustee has been discharged of their liability to prevent queries being raised by the member with their discharged trustee.

7.63 The Regulations also provide that the FAS scheme manager must give those for whom liabilities transfer to the FAS, notice that the trustee has been discharged within 28 days of the transfer notice having been given.

Reviews and appeals

7.64 The Regulations provide a number of new rights of review and appeal in recognition of the directions that may be given by the FAS scheme manager during the preparation for asset transfer, the new categories of member being created and extended benefits provided in the Regulations. The timescales in which to request a review mirror timescales for existing reviews, however, the timescale in which to request a review of the valuation approval is limited to 21 days. This shorter timescale recognises the close working relationship that will exist between the pension scheme trustee and the caseworker undertaking the FAS work.

7.65 The Financial Assistance Scheme (Internal Review) Regulations 2005 detail the determinations on which a review can be requested and the timescales in which the review request can be made. In light of operational experience, the new Regulations reduce to one month the timescale in which a review request can be made in respect of a scheme notification and scheme qualification determination. The FAS scheme manager retains the right to extend this timescale where it considers appropriate. In addition, the Regulations remove completely the timescale in which a review can be requested in respect of an annual payment and ill health payment determination.

Amendments to the Financial Assistance Scheme Regulations 2005

7.66 The Regulations also make some minor amendments to existing provisions in the Financial Assistance Scheme Regulations 2005 to ensure that payments can be made in line with the policy intention. For instance, they ensure that members and their survivors have the correct amount of revaluation applied to the accrued pension up to the point at which they become entitled to assistance. They also change the formulae for calculating payments to survivors and surviving dependants when payments are re-determined following a change in their number to ensure that these beneficiaries receive the correct amount of indexation in their future payments.

7.67 In addition, the Internal Review Regulations are amended so that annual payment and ill health payment determination notices issued by the scheme manager will not include trustees' details where the scheme in question has transferred its assets. The Regulations also remove the provision allowing the FAS scheme manager to publish determinations on its website in respect groups of members who have not qualified for FAS assistance. These group decisions will no longer be relevant following the extension of the definition of qualifying member which removes the possibility of a qualifying scheme that has not completed wind up having a group of members who would not be qualifying members.

- ***Consolidation***

7.68 This set of Regulations amends the Financial Assistance Scheme Regulations 2005 (S.I 2005/1986). They also amend the Financial Assistance Scheme (Provision of Information and Administration of Payments) Regulations 2005 (S.I. 2005/2189, as amended), the Financial Assistance Scheme (Internal Review) Regulations 2005 (S.I. 2005/1994, as amended) and the Financial Assistance Scheme (Appeals) Regulations (S.I. 2005/3273, as amended).

7.69 The Financial Assistance Scheme Regulations 2005 have now been amended several times and the Department recognises that they will require consolidation. The Department considered whether those Regulations could be consolidated as part of this set of amendments. However, it was considered that, given the extent and complexity of the amendments being made and, as there are likely to be amendments made to these Regulations later in the light of operational experience, it would be more appropriate and convenient to consolidate the Regulations at a later stage when the operation of the scheme is more settled. The Department proposes to undertake consolidation of the Regulations at the next convenient opportunity.

7.70 In the meantime, consolidated versions of all the Regulations amended by these Regulations will be available in the Law Relating to Social Security (Blue Volumes). These can be found at http://www.dwp.gov.uk/publications/specialist-guides/law-volumes/the-law-relating-to-social-security/. These are updated quarterly and are available on the internet at no cost to the public.

8. Consultation outcome

8.1 Public consultation has been undertaken on the Regulations involving key stakeholders such as pension lawyers, consultants, trustees, administrators, actuaries, insurers, trade unions and the Pensions Action Group. The consultation ran from 12 August to 6 October 2009. A period of eight weeks was considered appropriate for this element of the package of measures being introduced, as these Regulations have formed part of a series of affirmative Regulations implementing the December 2007 extension on which much consultation had already taken place. In addition to the formal consultation, regular informal consultation has taken place with key stakeholders affected by the FAS policy throughout the period of policy development. During the consultation period meetings were held with the Trustee Advisory Panel, the Pensions Action Group and individuals who will be directly affected by the changes, to talk through the policy proposals and invite comment.

8.2 A total of 42 responses to the consultation were received, of which 21 were from organisations involved in pensions. The remaining responses were from representative groups and individuals. Four responses received were outside the scope of the consultation.

8.3 The Department has made a number of changes to the Regulations based on the consultation responses, the most notable of which are set out in the following paragraphs.

Treatment of defined benefit AVCs

8.4 The Regulations contain provision to allow certain assets held in respect of defined benefit additional voluntary contributions to be disregarded. This provision is required because the Government intends that trustees should have the opportunity to discharge such benefits before the transfer of scheme assets. The Government is allowing scheme trustees to discharge such benefits at their discretion in response to concerns raised during consultation that members of schemes transferring assets could lose out in comparison to those whose schemes were buying annuities where they had made voluntary contributions.

Treatment of partial discharge cases

8.5 During the wind up process, pension schemes sometimes arrange for liabilities to be partially discharged by the purchase of annuities, or by buying back certain State Scheme entitlements otherwise foregone as part of the contracting-out process.

8.6 In other cases transfer payments might be made to members on the understanding that further assets might be allocated to those members at the end of wind up. In consultation on the draft Regulations, the Government proposed that trustees continue the discharge of liabilities in ‘partial cases’ before assets transferred to government.

8.7 Responses to the consultation identified potential barriers to completing the discharge of certain liabilities. After balancing the benefits to be gained from taking in such assets against increased operational complexity, the Government has revised its approach. The Regulations now provide for residual assets that would have been allocated to members who have received partial transfers or who have been reinstated into the State Scheme to be transferred to government and for relevant payments to be calculated in respect of those assets.

8.8 In general, the Government maintains the position that trustees should continue the discharge of liabilities for members for whom annuities have already been secured. However, it recognises that there are some circumstances where further annuity purchase would not be of material benefit to members or government (where any additional payments would merely serve to reduce the top-up payments that FAS would otherwise pay). The Regulations and envisaged operational processes provide flexibility for relevant assets to be taken into government in such cases.

Survivor Payments

8.9 In response to consultation the Regulations also now use the date of the member’s death for determining whether a survivor or surviving dependant is to be regarded as receiving a scheme pension when these Regulations come into force thus ensuring a clear point for the calculation of survivor’s FAS assistance and minimising any potential impact of a scheme’s ability to make payments to the survivor or surviving dependent.

8.10 A more detailed analysis of the consultation outcome has been published and is on the DWP website: http://www.dwp.gov.uk/lifeevent/penret/penreform/fas/. The document details the reactions to the individual proposals and the Government's response.

9. Guidance

9.1 The Government will provide actuarial guidance detailing the method and assumptions that should be used by the 'valuation actuary' when undertaking the valuation. This guidance will also set out the buy-out basis that will be used by actuaries to determine relevant liabilities – that is, those that fall to be valued on a buy-out basis – and used by the FAS scheme manager to determine notional pensions. The Government anticipates that final guidance will be published to coincide with the date the Regulations come into force in order to help ensure effective implementation.

9.2 A communication strategy is being developed by the FAS scheme manager to explain the asset transfer process to trustees. The strategy will also include details of the FAS payment process to the new category of member created by these Regulations will be implemented when the Regulations come into force.

10. Impact

10.1 The main impact on business is the lost opportunity to annuity providers resulting from the transfer of scheme assets to government. This will result in those assets not being used by pension schemes to purchase annuities to the value of between £120m to £160m. While this figure appears large, it is small compared to the overall size of the annuities market. In 2008 just over 454,000 annuities were sold with a median fund value of around £15,000 each. This suggests a conservative estimate of the overall value of the annuities market is about £6.5 to £7 billion per year. There is no impact on charities or voluntary bodies.

10.2 There were no comments received to the consultation on the lost business opportunities to annuity providers, resulting from the transfer of scheme assets to government rather than being used by trustees to purchase annuities.

10.3 The FAS scheme manager already pays FAS assistance up to a level of 90 per cent of expected pension which is funded by the tax payer. The extra costs of paying asset share related payments will be funded by the assets taken in by government. The associated administration costs will be minor once the initial set up and design is implemented.

10.4 A full impact assessment is attached to this memorandum.

11. Regulating small business

11.1 The legislation applies to small business.

11.2 In order for assistance to be paid to qualifying members of qualifying schemes, trustees of the affected pension schemes need to supply information on the pension scheme and its members. The requirements are the same for all schemes regardless of size. To minimise the impact of the requirements on firms employing up to 20 people, these Regulations introduce the discretion for the FAS scheme manager to waive some or all of the information requirements where considered appropriate to do so.

11.3 The discretion to assist small business was introduced following discussions with representatives of trustees through the Trustee Advisory Panel. It should be noted that over 75% of FAS qualifying schemes are managed by large businesses.

12. Monitoring & review

12.1 Legislation requires that the FAS scheme manager (the Board of the Pension Protection Fund) must provide the Secretary of State for Work and Pensions with annual reports and accounts at the end of each financial year on the operation of the FAS including the number of persons who have received payments under the Financial Assistance Scheme Regulations 2005 (as amended) and the total amount of those payments. The first report by the Board must be provided as soon as practicable after 31st March 2010 and annually thereafter. This report will be laid before Parliament when received by the Secretary of State.

12.2 Where any part of that Report raises concerns over the operation of the FAS, the Department for Work and Pensions will take the appropriate action, which could include raising its concerns with the Board.

12.3 The Government wants FAS qualifying members and their survivors to get the correct level of payment at the appropriate time. It will agree with the Board of the Pension Protection Fund targets to ensure this is achieved. The Board's delivery of these targets will be monitored to satisfy Ministers that the changes specified in these Regulations are being implemented appropriately, that members and their families are getting the payments the Regulations provide for; and that the relevant elements of the December 2007 announcement are being delivered.

13. Contact

Julie Guthrie at the Department for Work and Pensions - Tel: 020 7449 7414 or email: Julie.Guthrie1@dwp.gsi.gov.uk - can answer any queries regarding the instrument.

Summary: Intervention & Options

Department /Agency: **Department for Work and Pensions**	**Title:** **Impact Assessment of** The Financial Assistance Scheme (Miscellaneous Amendments) Regulations 2010	
Stage: Final		**Date: 8th December 2009**

Related Publications: The Financial Assistance Scheme (FAS) Review of Assets (the 'Young Review')

Available to view or download at:

http://www.dwp.gov.uk/consultations/

Contact for enquiries: Julie Guthrie **Telephone:** 020 7449 7414

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

The Financial Assistance Scheme (FAS) provides assistance to members of defined benefit pension schemes that commenced winding up under-funded between 1st January 1997 and 5th April 2005 (with a very limited number of exceptions where wind-up began after that date). Financial constraints have meant that assistance provided by government has been limited. In 2007 the Government commissioned the Financial Assistance Scheme Review of Assets (the 'Young Review') to consider whether an alternative treatment of the residual funds in affected pension schemes could

What are the policy objectives and the intended effects?

- The transfer of pension scheme assets to government to supplement funding provided in respect of the FAS;
- Making provision for some members of schemes who would have received more than the assistance payments FAS would otherwise provide had their scheme continued to wind-up and purchase annuities rather than transfer assets.
- Provide for other changes to FAS payments including provision for the payment of lump sums to certain members in respect of whom assets transfer.

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

The 'Young Review' recommended three options for the use of pension scheme assets :

- Continue to top up pensions
- Modified annuitisation
- Managed use of scheme assets

The Review concluded that, to provide a guaranteed benefit level, the best value would come from government absorbing all residual assets in FAS qualifying schemes and taking responsibility for making associated payments. Based on assets of £1.7billion, the Review estimated this would provide additional financial value of between £340 to

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

Arrangements to steward the Board of the Pension Protection Fund (PPF), as FAS scheme manager, have been put in place. These will be extended to include monitoring the Board's effectiveness in transferring assets and assessing assistance payments. The Board, as FAS scheme manager, is required to submit accounts and reports to DWP for scrutiny. An annual report will be laid before Parliament containing details of FAS

Ministerial Sign-off For Impact Assessments:

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:

Angela Eagle Date: 8th December 2009

Summary: Analysis & Evidence

Policy Option:	Description:

COSTS

ANNUAL COSTS		Description and scale of **key monetised costs** by 'main affected groups'
One-off	**Yr**	Administrative costs of transferring assets. An estimate of the additional cost to pension scheme assets (which is effectively a cost to the public sector as government will be taking in the assets) of providing information to government necessary to transfer member data is between £1m and £3.1m. Taking in scheme assets and making the associated payments will lead to a higher administrative burden on the Board of the PPF. These additional costs
£ 28.1m	4	
Average Annual Cost (excluding one-off)		
£ 0		**Total Cost** (PV) **£ 28.1m**

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

Lost opportunity to annuity providers: Pension schemes who are transferring their assets to government will not secure members' benefits by purchasing annuities. While this is not a cost to annuity providers it does represent a lost opportunity of

BENEFITS

ANNUAL BENEFITS		Description and scale of **key monetised benefits** by 'main affected groups'
One-off	**Yr**	The Financial Assistance Scheme (FAS) Review of Assets concluded that to provide a guaranteed benefit level, the best value would come from government absorbing residual assets in FAS qualifying schemes. The additional financial value was estimated to be between £340m and £425m. This benefit will accrue
£ 340m	90	
Average Annual Benefit (excluding one-off)		
£ 0		**Total Benefit** (PV) **£ 340m**

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

None

Key Assumptions/Sensitivities/Risks

Changes in the value of investments may mean that the estimates of the additional value of bring assets into government may be under or overstated. Also the administrative

Price Base Year 2009	Time Period Years 90	**Net Benefit Range** (NPV) **£ 312 - 399m**	**NET BENEFIT** (NPV Best estimate) **£ 355m**

What is the geographic coverage of the policy/option?	UK
On what date will the policy be implemented?	Spring 2010
Which organisation(s) will enforce the policy?	DWP
What is the total annual cost of enforcement for these	**£ Negligible**
Does enforcement comply with Hampton principles?	N/A
Will implementation go beyond minimum EU requirements?	N/A

What is the value of the proposed offsetting measure per year?			**£ N/A**	
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	No	No

Impact on Admin Burdens Baseline (2005 Prices)					(Increase -	
Increase	£ N/A	Decrease	£	**Net**	£ N/A	

Key **Annual costs and** **(Net)**

Evidence Base (for summary sheets)

Background

The Financial Assistance Scheme (FAS) was created under the Pensions Act 2004 to provide assistance to members of qualifying occupational pension schemes which generally started to wind up, under-funded, between 1st January 1997 and 5th April 2005.

FAS makes payments to members of defined benefit occupational pension schemes that, because of under-funding, cannot pay members the full amount of their accrued pension rights. FAS tops up any payment from the scheme to 90% of a member's expected pension, subject to a maximum limit. Payments are made from the later of 14th May 2004 or a member's scheme normal retirement age. In certain circumstances members may access FAS assistance before their normal retirement age.

The FAS also makes payments to certain survivors of qualifying members on their death.

Extension to the Financial Assistance Scheme

The Financial Assistance Scheme Review of Assets (the 'Young Review') was commissioned by the Government in 2007 to consider whether an alternative treatment of the residual assets in affected pension schemes could supplement the committed government funding of the FAS. The Review recommended three options for the use of pension scheme assets:

- continue to top up pensions
- modified annuitisation
- managed use of scheme assets

The Review concluded that, to provide a guaranteed benefit level, the best value would come from government absorbing all residual assets in FAS qualifying schemes and taking responsibility for making all associated payments. Taking in assets would be a new process for FAS.

Following acceptance of the 'Young Review' in December 2007, the Government announced, in December 2007, a package of measures to:

- transfer the residual assets of FAS qualifying pension schemes to government; and
- extend the assistance provided by FAS.

In addition, the Government subsequently announced its intention to confer the role of the FAS scheme manager on the Board of the Pension Protection Fund (PPF) (a non-departmental public body which deals with schemes that had insolvency events from 6th April 2005 onwards and are funded to a level below PPF compensation).

These changes have been implemented in stages and these Regulations cover the final stage. They include transferring relevant FAS qualifying pension scheme assets to government and taking responsibility for making payments to certain beneficiaries, who would have received higher payments than FAS would otherwise provide, when assets transfer.

The transfer of FAS qualifying scheme assets requires the Government to implement a process that provides for the valuation of and transfer of scheme assets and liabilities. As a result additional information is required for pension scheme members who previously would not have been eligible for help from FAS in relation to survivor benefits and death benefit guarantees payable to members.

These Regulations also provide for the payment of lump sums through the commutation of assistance although this does not require any additional information requirements in respect of these payments.

Net Benefit

From the data contained in the summary on page 3 and in table 4 below, the overall net benefit range of these measures is calculated by taking the lower estimate of additional value (£340m) and subtracting the highest estimate of the additional costs (£28.1m) which gives £312m as the lower end of the range. To calculate the upper end of the range, the upper estimate of additional value (£425m) is taken, from which the lower end of the range of additional value (£26m) is subtracted, producing a figure of £399m.

The overall best estimate of the net benefit is £355m, which is the mid-point of the lower-end estimate of £312m and the upper end estimate of £399m.

Impact of the regulatory changes

Impact on business: The transfer of scheme assets to government could be viewed as resulting in a lost opportunity to annuity providers. This is because pension schemes that have members eligible for FAS assistance and are transferring their assets to government will no longer look to secure pension payments for their members by purchasing annuities.

Impact on pension scheme assets: These Regulations will result in a cost to pension schemes' assets of trustees providing additional information so that the policy of transferring assets from pension schemes to government can take place and extended FAS assistance payments be calculated. The cost of providing this information in the vast majority of cases will be met from scheme assets and therefore will not present a cost to business as they will effectively fall on FAS when topping up a pension scheme member's pension. The Regulations enable the FAS scheme manager to waive some, or all of the information requirements where considered appropriate.

The first part of this evidence base considers lost opportunity costs to annuity providers and the second focuses on the cost to pension scheme assets of trustees providing information to the FAS scheme manager to calculate and pay assistance.

Part 1: Lost opportunity to annuity providers:

Background – why the Government are taking into the Financial Assistance Scheme, the assets of qualifying pension schemes

The 'Young Review' concluded that, to provide a guaranteed benefit level, the best value would come from government absorbing all residual assets in FAS qualifying schemes and taking responsibility for making all associated payments.

Based on estimated assets of £1.7billion, the Review estimated this would generate an additional financial value of funds available to FAS of between £340m and £425m than if the government continued to top-up annuity payments.

Part of the additional value to government of taking in assets from FAS qualifying schemes is generated through the FAS in the public sector being a monopoly that does not operate in contestable markets. Insurers do compete and they need to earn margins to reward shareholders for taking market share risks.

The ‘Young Review’ estimated that the margin needed by insurers in order for them to offer annuities to members of FAS qualifying schemes was between £120m and £160m in total. This margin included the profits and prudence for the insurer. This means that an upper estimate of the lost opportunity to annuity providers of the Government taking in pension scheme assets rather than pension scheme trustees purchasing annuities might be between £120m and £160m which will be a saving to government. While this figure appears large, it is small when compared to the overall size of the annuities market; in 2008 just over 454,000 annuities were sold with a median fund value of around £15,000 each. This suggests a conservative estimate of the overall value of the annuities market is about £6.5 to £7 billion per year.

There have been no adverse comments from insurers, who specialise in providing annuities for winding-up defined benefit schemes, about government taking in assets rather than allowing pension schemes to purchase annuities for their members.

<u>Part 2: Costs of providing information necessary for transferring pension scheme assets to government</u>

A survey outlining the additional information that would be required as a result of these draft Regulations was sent to a number of trustees who were asked to provide estimated costs for providing the information as outlined.

Their responses have been used to estimate the additional costs. All the costs in this impact assessment have been taken from this survey unless otherwise stated.

The costs related to:

- Transferring assets to government (Cost 1-2)
- Providing information on the new category of pensioner members in FAS (Costs 3-5)
- The cost of purchasing annuities (Cost 6)

Costs 1 to 2: Transferring assets to government

Two notional costs have been identified with transferring pension scheme assets to government and the responses from trustees suggested that these costs are scheme-specific and vary greatly.

Cost 1: The additional cost of a scheme having to sell assets that it may otherwise have been able to transfer to an annuity provider. Whilst in some cases this may be an additional cost for a scheme, discussions with trustees have indicated that in most cases liquidating assets prior to transfer is the easiest and most cost-effective method.

Cost 2: The cost of implementing the valuation calculations and providing information to support validation processes (over and above those that would be incurred were conventional winding-up processes to be followed in relation to these schemes). For instance, although a valuation of assets and liabilities would need to be undertaken in a conventional wind-up ‘in-house’ approaches might be taken to reconciling past payments made to members against the share of assets allocated to the member. Additionally, standard processes will be required to meet FAS requirements that could incur additional processing costs.

Table 1

	Lower estimate (per scheme)	**Higher estimate** (per scheme)
Cost 1: Cashing assets	Negligible or small administrative costs - £0	Up to £5000 for a scheme with complex assets
Cost 2 : Valuation of scheme assets and liabilities and providing information for validation	£2,000 to £3,000 for a replacement valuation of assets and liabilities at the time of transfer	Between £10,000 and £25,000 depending on the size of the scheme

There are approximately 450 schemes that could transfer assets into government. This means that the costs of cashing the assets are between £0 and £2.25m (450 * £5000) and the costs of valuing the scheme assets are between £1.1m ((£2,000+£3,000)/2 * 450) and £7.9m ((£10,000+£25,000)/2 * 450).

Costs 3 to 5: The additional cost of providing information in respect of the new category of pensioner members

As a result of taking in FAS qualifying scheme residual assets, the FAS will make payments to pensioners who are currently receiving their pension from their pension scheme (above standard FAS levels). The operation of relevant statutory priority orders that dictate the order in which scheme assets are allocated mean many of these pensioners would stand to receive pensions higher than the assistance payments that FAS would otherwise provide.

In order to make payments to this category of member, the FAS scheme manager will need some of the same type of information that it is currently collected from pension schemes for scheme members who receive FAS payments. However, the FAS scheme manager will also require additional information from the trustee in relation to the level and proportion of survivor benefits and death benefit guarantees available to the member under the pension scheme rules.

Trustees would expect to provide information to an insurer for the purpose of purchasing an annuity so only the additional cost of providing the information to the FAS scheme manager compared with providing information to an insurer for an annuity purchase has been assessed. A number of trustees said that much of this data would be necessary in order to wind-up the scheme and purchase annuities, so the additional costs would not be significant and were difficult to cost individually. This would mean that there was no additional cost of the pensioner members being paid through the FAS operational unit.

Table2

	Estimate for the administrative review on burdens to trustees of providing information[4] (per member)	
Cost 3: Cost of providing information to FAS per member	£25.50	
	Lower estimate	**Higher estimate**
Cost 4: Survivor benefit.	£ negligible	£60
Cost 5: Death Benefit Guarantees.	Already included	Already included

There are approximately 23,000 pensioner members currently being paid by their pension scheme who will be paid by the FAS operational unit in the future. The cost of providing information on pensioner members, including for survivor and death benefits, is estimated to be between £586,500 (£25.50 * 23,000) and £2.0m ((£25.50 + £60) * 23,000).

Cost 6: Purchasing annuities

To appreciate the additional costs to business of providing information to calculate and pay extended FAS assistance, it is necessary to understand what pension scheme trustees would have spent in providing information in order to purchase an annuity for their members.

Consultation suggested that the cost of purchasing annuities varies widely due to the:

- complexities of each scheme;
- approach taken by the insurer;
- costs of obtaining advice if needed from a consulting firm; and
- cost of legal advice.

The following table summarises details of costs as provided by trustees.

Table3

	Lower estimate (per scheme)	**Higher estimate** (per scheme)
Cost 6: The administrative cost of purchasing annuities.	£1,500	£20,000 – although costs could be as high as £60,000 for a complex scheme.

There are approximately 450 schemes that are transferring assets into government.
The total cost of purchasing annuities will therefore be between £675,000 (£1,500 * 450) and £9m (£20,000 * 450). The highest estimate cost of £60,000 relates only to a very small number of schemes and therefore the figure of £20,000 has been used as a representative average for the higher estimate, given also that many schemes will cost considerably less.

[4] This figure is based on standard assumptions that have been used within the FAS programme since 2007. The cost has been inflated using the All Items RPI – not seasonally adjusted (CHAW).

The additional cost of providing information to government / Total additional costs

The following table summarises the total costs in relation to transferring assets into government.

Table 4

	Lower estimate	Higher estimate
Cost 1: Cashing assets	£0	£2,250,000
Cost 2 : Valuation of scheme assets	£1,125,000	£7,875,000
Cost 3: Cost of providing member information to FAS	£587,000	£587,000
Cost 4: Survivor benefit.	£0	£1,380,000
Cost 5: Death Benefit Guarantees.	£0	£0
Sub total	£1,712,000	£12,092,000
Less Cost 6 The administrative cost of purchasing annuities	£675,000	£ 9,000,000
Total	£1,037,000	£3,092,000

Therefore the additional cost to trustees of providing the information necessary to transfer the pension scheme assets into government is estimated to be between £1m and £3m. This is the difference between the cost of providing information to FAS and the cost of purchasing an annuity which pension schemes currently have to do to ensure the members benefits once the scheme has wound-up.

A FAS Trustee Advisory Panel which comprises of trustees, administrators and annuity providers from the pensions industry has been engaged with DWP officials at all stages of the implementation of the December 2007 announcement and have discussed with them the financial implications of providing additional information requirements resulting from these changes.

In all cases of information collection, the FAS scheme manager will ensure that any requests for information are limited to only that which is necessary and relevant to the calculation and payment of FAS assistance and the management of the FAS.

These Regulations include a provision for the FAS scheme manager to waive some or all of the information requirements where it considers that the information is not necessary or relevant to its FAS work. The Regulations also provide for the FAS scheme manager to restrict valuation requirements in certain exceptional circumstances where it would not be cost-effective for full valuation requirements to be followed - this may arise where a scheme’s funding position is such that all residual assets will be allocated to pensioner members and none of those pensioner members would stand to receive payments that would otherwise be above FAS levels.

Costs that a trustee incurs in providing information are likely to be recovered by the trustee from the pension scheme assets prior to their transfer to government. In using scheme assets to cover the cost of providing information members’ asset shares may be reduced, however in many cases this will be offset for the member by an increase in FAS assistance (to a maximum of 90% level, subject to the FAS cap). As the cost of providing information will reduce individual asset shares it is possible that a small number of people with asset shares in excess of 90% (and hence do not receive a top up from the FAS) will see a small reduction in the value of their payments due to the cost of information provision reducing their asset share. Whilst detailed information on members which may be in this position is not held, it is believed that the number of members affected to be small, and the loss to affected members also to be small.

Administrative Costs

The FAS scheme manager already pays assistance up to a level of 90%, therefore the extra costs of paying asset-backed payments will be minor once the initial set up and design is implemented. Hence running costs, and start up costs will be minor given that this is already an ongoing process.

Competition Assessment

The Government's absorption of FAS qualifying scheme assets does not affect competition in the insurance sector as it removes business from the entire annuity sector and not from any particular area of this sector.

Government itself is not part of the annuity business sector and would not be purchasing annuities on behalf of FAS qualifying pension schemes.

Small Firms Impact Test

The Government recognise that the additional information requirements may place a cost on small businesses and the definition of small businesses may apply to some of the trustees that manage pension schemes. The basic information requirements, per scheme, are the same regardless of the size of scheme. It should be noted however, that over 75% of FAS schemes are managed by large businesses.

Legal Aid

There will be no impact on legal aid.

Sustainable Development, Carbon Assessment, Other Environment.

It is not expected that these regulations will have any impact in these areas.

Health Impact Assessment

The options have been considered against the screening questions for health impact assessments and a full health assessment is considered to be unnecessary.

Human Rights

These regulations are compatible with the Human Rights Act 1998.

Rural Proofing

These regulations have no specific impact on rural communities.

Equality Impact Assessment

An Equality Impact Assessment has been published which relates to FAS in its entirety.

Specific Impact Tests: Checklist

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