Title: Pension Protection Measures for the Pensions Bill **Lead department or agency:** **Department for Work and Pensions** **Other departments or agencies:** **Pension Protection Fund** **The Pensions Regulator**	Impact Assessment (IA) **IA No:** DWP-PPF/TPR **Date:** 09/11/2010 **Stage:** Final **Source of intervention:** Domestic **Type of measure:** Primary legislation **Contact for enquiries:** **Simon Capey - 020 7449 7048**

Summary: Intervention and Options

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

The Bill makes a number of mainly minor amendments to legislation that governs the operation of the Pension Protection Fund (PPF) and the Pensions Regulator (tPR). The one substantive measure is the change of basis for indexation of pension compensation. The Government is intervening to amend legislation in the light of live running of PPF and tPR since these bodies commenced operations in April 2005, and to complement wider changes to indexation of pensions.

What are the policy objectives and the intended effects?

The objectives: (1) to change certain operational requirements on the PPF with the intention of learning from live running and improving the overall operational activities; (2) to change rules on pension compensation so that people may defer the date from which their compensation starts to be paid, and so that certain rights due as a result of a pension sharing arrangement following a divorce etc are revalued before compensation is paid; (3) to bring the indexation of pension compensation into line with the Government's wider changes to the indexation of pensions; (4) to ensure the time periods for representations relating to the Pensions Regulator's anti-avoidance measures work fairly for business in cases with inherent complexity, such as large multi-national or

What policy options have been considered? Please justify preferred option (further details in Evidence Base)

For all the amendments except the one to complement the change from RPI to CPI, the other option considered was to leave the legislation as now.
PPF measures: the preferred option was chosen as live running of the PPF since April 2005 has shown that the amendments would improve operational effectiveness and enhance the pension compensation paid.
Indexation of pension compensation: the other option was to continue to index pension compensation in line with RPI. The preferred option was chosen as to index pension compensation in line with RPI would, once the Government's other changes have been implemented, be inconsistent with the indexation of pensions.
Time periods relating to anti-avoidance measures: it was considered whether to extend the current

When will the policy be reviewed to establish its impact and the extent to which the policy objectives have been achieved?	**It will be reviewed on an ongoing basis as part of the DWP's oversite of the PPF's and tPR's operations.**
Are there arrangements in place that will allow a systematic collection of monitoring information for future policy review?	**No**

SELECT SIGNATORY Sign-off For final proposal stage 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.

Steve Webb

Signed by the responsible Minister:.. Date: 10 November 2010 .....

Summary: Analysis and Evidence Policy Option 1

Description:

Changes relating to the Pension Protection Fund and the Pensions Regulator resulting from live running, and a change to the basis for indexation of pension compensation.

Price Base Year 2010	PV Base Year 2010	Time Period Years 60	Net Benefit (Present Value (PV)) (£m)		
			Low: Optional	**High:** Optional	**Best Estimate: £4m**

COSTS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	**Optional**		**Optional**	Optional
High	**Optional**	60	**Optional**	Optional
Best Estimate	**£500m**		**£0**	£500m

Description and scale of key monetised costs by 'main affected groups'

CPI indexation change - PPF estimate a 4.8% reduction (NPV £500m) in current liabilities resulting from the change, based on an estimate of 0.5% for the RPI-CPI gap. The reduction in PPF liabilities represents a transfer of £500m NPV from current members of the PPF to employers sponsoring defined benefit pension schemes who fund the PPF through a compulsory levy. No financial costs resulting from the other pension protection measures.

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

None

BENEFITS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	**Optional**		**Optional**	Optional
High	**Optional**	60	**Optional**	Optional
Best Estimate	**£500m**		**£0.5m**	£504m

Description and scale of key monetised benefits by 'main affected groups'

CPI indexation - the reduction in PPF liabilities represents a transfer of £500m NPV from current members of the PPF to employer sponsors; this will be factored into the PPF's considerations on the rate of the Pension Protection Levy. Changes to PPF measures deliver relatively minor savings (less than £500,000 p.a) in administrative costs to schemes in an assessment period and the PPF. Changes relating to tPR will not affect the majority of businesses, but delivers non-quantifiable

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

None

Key assumptions/sensitivities/risks **Discount rate** 3.5%

For the operational improvement measures, the changes to pension compensation and amendments and to the time periods relating to the anti-avoidance measures are based on live running of the PPF and tPR.

Impact on admin burden (AB) (£m):	Impact on policy cost savings In

New AB: Nil	**AB savings:** 0.5m	**Net:** -0.5m	**Policy cost savings:** Nil	Yes

Enforcement, Implementation and Wider Impacts

What is the geographic coverage of the policy/option?			Great Britain			
From what date will the policy be implemented?			01/04/2012			
Which organisation(s) will enforce the policy?			N/A			
What is the annual change in enforcement cost (£m)?			N/A			
Does enforcement comply with Hampton principles?			Yes			
Does implementation go beyond minimum EU requirements?			N/A			
What is the CO_2 equivalent change in greenhouse gas emissions? (Million tonnes CO_2 equivalent)			Traded:		Non-traded:	
Does the proposal have an impact on competition?			No			
What proportion (%) of Total PV costs/benefits is directly attributable to primary legislation, if applicable?			Costs:		Benefits:	
Annual cost (£m) per organisation (excl. Transition) (Constant Price)	Micro	< 20	Small	Medium	Large	
Are any of these organisations exempt?	Yes/No	Yes/No	Yes/No	Yes/No	Yes/No	

Specific Impact Tests: Checklist

Set out in the table below where information on any SITs undertaken as part of the analysis of the policy options can be found in the evidence base. For guidance on how to complete each test, double-click on the link for the guidance provided by the relevant department.

Please note this checklist is not intended to list each and every statutory consideration that departments should take into account when deciding which policy option to follow. It is the responsibility of departments to make sure that their duties are complied with.

Does your policy option/proposal have an impact on…?	Impact	Page ref within IA
Statutory equality duties[1] Statutory Equality Duties Impact Test guidance	No	
Economic impacts		
Competition Competition Assessment Impact Test guidance	No	
Small firms Small Firms Impact Test guidance	No	
Environmental impacts		
Greenhouse gas assessment	No	
Wider environmental issues	No	
Social impacts		
Health and well-being Health and Well-being Impact Test guidance	No	
Human rights Human Rights Impact Test guidance	No	
Justice system Justice Impact Test guidance	No	
Rural proofing Rural Proofing Impact Test guidance	No	
Sustainable development	No	

1 Race, disability and gender Impact assessments are statutory requirements for relevant policies. Equality statutory requirements will be expanded 2011, once the Equality Bill comes into force. Statutory equality duties part of the Equality Bill apply to GB only. The Toolkit provides advice on statutory equality duties for public authorities with a remit in Northern Ireland.

Sustainable Development Impact Test guidance		

Evidence Base (for summary sheets) – Notes

Use this space to set out the relevant references, evidence, analysis and detailed narrative from which you have generated your policy options or proposal. Please fill in References **section.**

References

Include the links to relevant legislation and publications, such as public impact assessment of earlier stages (e.g. Consultation, Final, Enactment).

No.	Legislation or publication
1	The Pensions Act 2004
2	The Pensions Act 2008
3	The Pensions Schemes Act 1993
4	

+ Add another row

Evidence Base

Ensure that the information in this section provides clear evidence of the information provided in the summary pages of this form (recommended maximum of 30 pages). Complete the Annual profile of monetised costs and benefits **(transition and recurring) below over the life of the preferred policy (use the spreadsheet attached if the period is longer than 10 years).**

The spreadsheet also contains an emission changes table that you will need to fill in if your measure has an impact on greenhouse gas emissions.

Annual profile of monetised costs and benefits* - (£m) constant prices

	Y_0	Y_1	Y_2	Y_3	Y_4	Y_5	Y_6	Y_7	Y_8	Y_9
Transition costs	500*	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Annual recurring cost										
Total annual costs	500*	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Transition benefits	500*	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Annual recurring	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Total annual benefits	500.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5

*** For non-monetised benefits please see summary pages and main evidence base section**

NB: * The table relates to changes in pension liabilities as a result of the policy, the timing of the actual cash flows will differ from those shown here.

Evidence Base (for summary sheets)

1. BACKGROUND: PENSION PROTECTION FUND AND PENSIONS REGULATOR

Pension Protection Measures for Pensions Bill

The Bill makes a number of changes to legislation that governs the operation of the Pension Protection Fund (PPF) created under Part 2 of the Pensions Act 2004 and the Pensions Regulator created under Part 1 of that Act.

The Pension Protection Fund

The PPF provides pension compensation to people who were members of eligible pension schemes where the amount of pension is usually based on a person's salary at, or around, the date of retirement. Such schemes are usually referred to as "defined benefit schemes" or "final salary schemes". Pension compensation is paid where the employer that sponsors an eligible defined benefit scheme has experienced a qualifying insolvency event and where there are insufficient assets in the scheme to pay pensions at the same level as the pension compensation. The PPF is managed by the Board of the Pension Protection Fund (the PPF Board), which is a statutory corporation.

The Pensions Regulator

The Pensions Regulator is the UK regulator of work-based pension schemes. It was established under the Pensions Act 2004 as an executive non-departmental public body and is accountable to the Secretary of State for Work and Pensions. The Regulator's main statutory objectives under the 2004 Act are to:

- protect the benefits of members of work-based pensions schemes
- reduce the risk of situations arising which may lead to compensation being payable from the Pension Protection Fund (PPF)
- promote, and improve understanding of, good administration of work-based pension schemes

An additional objective, established under the Pensions Act 2008, is:

- to maximise employer compliance with the employer duties (including the requirement to automatically enrol eligible employees into a qualifying pension provision with a minimum contribution) and with certain employment safeguards

2. THE SPECIFIC LEGISLATIVE PROPOSALS

PPF Technical Measures: Amendments of Part 2 of and Schedule 7 to the Pensions Act 2004 [and Schedule 8 to the Pensions Act 2008]

The Bill amends legislation around the PPF in the light of live running since April 2005.

The intention behind the changes is to:

- reduce unnecessary bureaucracy – four of the amendments remove requirements:
    - on when certain valuations must be carried out;
    - on the evidence a scheme must provide if it applies for reconsideration when it has not transferred into the PPF;
    - to make regulations on the form and content of certain determination notices made by the PPF Board; and
    - the minimum length of an assessment period;
- reduce the time and resources used on an activity by removing the requirement to take three statutory instruments through the affirmative procedures in Parliament;
- clarify how certain pension benefits flow through to pension compensation; and
- enhance the rules on pension compensation by allowing people defer the date from which their pension compensation starts to be paid and including revaluation in the calculation of pension compensation for certain pension credit members.

Savings

The I.A. shows that savings of about £500,000 per year will be achieved from the changes. This figure has been arrived at following feedback from the Pension Protection Fund. This figure is primarily made up of estimated savings of £15-20k per s143 test (the test that establishes whether a scheme’s funding level means it is drawn into the PPF) for very poorly funded schemes/overfunded schemes. In addition, shortening the minimum assessment period would reduce the period over which fees are incurred, and the deferral measures would bring some savings.

Whilst there is no specific end-date for these savings which can be applied, it is not reasonable to suggest they will apply over extended time-frames. For example, savings on administration made due to changes in the 1980s are unlikely to influence the level of administrative expenditure today. So whilst it could be argued that the savings should be calculated over a different time period as the current choice is somewhat arbitrary, we believe 10 years is a reasonable period to examine and quantify the cost savings over.

On this basis the Net Present Value (NPV) of the £500,000 saving for 10 years is £4m (rounded to nearest million).

A. Scheme valuations completed before transfer into the PPF

Background

Section 143 of the Pensions Act 2004 requires a valuation of a scheme's assets and protected liabilities to be carried out before the PPF Board may determine whether or not a scheme should transfer into the PPF. A scheme's protected liabilities are basically the cost of providing benefits equivalent to pension compensation, any non-pension liabilities of the scheme and the estimated cost of winding up the scheme.

Why consider change?

The PPF Board has asked that the requirement to undertake a valuation in all cases is removed, as experience has shown that in a high proportion of cases it is clear from existing information – for example other valuations provided to the PPF in order for it to calculate a scheme's pension protection levy - whether or not a scheme would transfer into the PPF.

Options considered

Other than to leave the legislation as now, no other options were considered.

Chosen option

The Bill removes the requirement in section 143 of the Pensions Act 2004 for a valuation of a pension scheme's assets and protected liabilities to be carried out before the PPF Board may determine whether or not a scheme should transfer into the PPF.

The amendments provide the PPF Board with the power to determine in some cases that a valuation is not required because it can use other information it has (for example, a valuation undertaken for the purposes of calculating a scheme's pension protection levy) in order to determine whether or not the scheme would transfer into the PPF. The amendments also add a requirement to Schedule 9 to the Pensions Act 2004 so that the new determinations made by the PPF Board are reviewable matters (decisions that the PPF Board is required to review if requested to do so by an interested party such as the trustees of a scheme).

Ministers chose this option because it would reduce unnecessary bureaucracy for the PPF Board.

Impacts

The change in legislation is not intended to change the outcome of an assessment period for schemes or members. The change is intended to reduce unnecessary bureaucracy and provide the PPF Board with the ability to provide for a faster flow of schemes through an assessment period. Which in turn would provide increased certainty and comfort for members (i.e. because the decision on whether to transfer a scheme into the PPF could be made earlier) and reduce costs. Whilst in assessment, schemes incur investment, advisory, administration and actuarial fees. Once schemes transfer to the PPF, many of these activities will entirely cease whilst others (e.g. administration and investment) can be carried out at a reduced rate, as they benefit from economies of scale.

The change contributes to some relatively minor savings – PPF estimate less than £500,000 a year in total from all the PPF technical measures – in administration costs for both schemes in an assessment period and the PPF.

B. Reconsideration of schemes that have not transferred into the PPF

Background

If a scheme does not transfer into the PPF the scheme's trustees or managers may apply for reconsideration if they think that since the point at which a scheme's assets and protected liabilities are valued (the start of the assessment period) the scheme has become further underfunded. Under section 151 of the Pensions Act 2004 the application must include a "protected benefits quotation".

Why consider change?

The PPF Board has advised that many schemes especially small ones find it impossible to obtain a quote. The PPF Board has asked for the requirement for a "protected benefits quotation" to be removed.

Options considered

Other than to leave the legislation as now, no other options were considered.

Chosen option

The Bill removes the requirement in section 151 of the Pensions Act 2004 that an application for reconsideration must include a "protected benefits quotation". The trustees or managers of a scheme that has not transferred into the PPF may apply for reconsideration by the PPF Board if they think that their scheme has become further underfunded.

The amendments provide the PPF Board with a power to determine whether or not a scheme should transfer into the PPF, after an application for reconsideration, using any information the PPF Board has available and any additional information it may request.

Ministers chose this option because it would reduce unnecessary bureaucracy for the PPF Board.

Impacts

The change is intended to reduce unnecessary bureaucracy as the inability to get a protected benefits quotation at all and/or in the prescribed format hinders the assessment and reconsideration process for schemes and therefore creates uncertainty, costs and administrative issues for the PPF Board, schemes and their members. The change in legislation is intended to remove those uncertainties, costs and administrative issues.

The change contributes to some relatively minor savings – PPF estimate less than £500,000 a year in total from all the PPF technical measures – in administration costs for both schemes in an assessment period and the PPF.

C. The content of certain determination notices made by the PPF

Background

Section 152 of the Pensions Act 2004 deals with reconsideration of schemes; it includes a requirement for regulations to be made to prescribe the form and content of notices to be provided by the PPF Board. To date regulations have not been made under the power.

Why consider change?

Regulations have not been made under section 152. The lack of Regulations has not, however, prevented the PPF Board from making the small number of determinations it has needed to.

Options considered

Other than to leave the legislation as now, no other options were considered.

Chosen option

The Bill removes the requirement in section 152 of the Pensions Act 2004 that notices about reconsideration issued by the PPF Board must be in a prescribed form and contain such information as may be prescribed. The amendments enable the PPF Board to issue a notice which is in a form and contains such information as may be decided by the PPF Board.

Ministers chose this option because it would reduce unnecessary bureaucracy for the PPF Board.

Impacts

The change is intended to reduce unnecessary bureaucracy. The change in legislation has no impact other than to remove an unnecessary regulation-making power.

D. The minimum length of a PPF assessment period

Background

Subsection 172(1) of the Pensions Act 2004 stipulates that an assessment period for the PPF must last for a minimum of 12 months. When a sponsoring employer experiences a qualifying insolvency an eligible scheme will go through an assessment period before the PPF Board decides whether or not the scheme will transfer into the PPF. We understand that the intention behind subsection 172(1) was to ensure that any applications for fraud compensation payments under Chapter 4 of Part 2 of the Pensions Act 2004 would have been made before a scheme transferred into the PPF.

Why consider change?

The PPF Board has asked for the period to be removed so that smaller less complicated cases could transfer into the PPF more quickly. There are few instances of fraud and to hold up the transfer of all schemes appears to be unreasonable. If a fraud were to be discovered after a scheme has transferred into the PPF the PPF Board has the power to transfer funds from the Fraud Compensation Fund into the PPF

Options considered

Other than to leave the legislation as now, no other options were considered.

Chosen option

The Bill removes the requirement in section 172 of the Pensions Act 2004 that an assessment period for the PPF must last for a minimum of 12 months.

Ministers chose this option because it would reduce unnecessary bureaucracy for the PPF Board.

Impacts

The change is intended to reduce unnecessary bureaucracy and as with the change to section 143 of the Pensions Act 2004, this change is intended to provide the PPF Board with the ability to provide for a faster flow of schemes through an assessment period.

The change contributes to some relatively minor savings – PPF estimate less than £500,000 a year in total from all the PPF technical measures – in administration costs for both schemes in an assessment period and the PPF.

E. Statutory instruments on the PPF administration levy, the pension protection levy ceiling and the pension compensation cap

Background

Section 316 of the Pensions Act 2004 requires certain statutory instruments to go through the affirmative procedures in Parliament. The statutory instruments affected are: (a) regulations on the PPF administration levy, which is collected on behalf of the Secretary of State to recoup any money paid by the Secretary of State out of money provided by Parliament to meet the administrative expenses of the PPF Board (section 117 of the Pensions Act 2004); (b) orders to increase annually the levy ceiling that limits the amount that the PPF Board may estimate it will collect through the pension protection levy (section 178 of the Pensions Act 2004); and (c) orders to increase annually the pension compensation cap that is applied to compensation paid to people who are below their scheme's normal pension age at the start of an assessment period (paragraph 27 of Schedule 7 to the Pensions Act 2004). The levy ceiling and the pension compensation cap are increased annually in line with increases in the general level of earnings. The Secretary of State may make an order to increase the levy ceiling above the annual increase in line with increases in the general level of earnings.

Why consider change?

The PPF administration levy is similar in nature to the general levy made under the Pensions Schemes Act 1993, which goes through the negative resolution procedures. The primary legislation on the pension protection levy ceiling and the pension compensation cap sets out how both should be uprated each year and the affirmative debates in Parliament cannot change the figures in the orders.

Options considered

Other than to leave the legislation as now, no other options were considered.

Chosen option

The Bill removes the requirements in section 316 of the Pensions Act 2004 that the statutory instruments listed above must not be made unless a draft of the instrument has been laid before Parliament and approved by a resolution of each House of Parliament. The amendment does not change the requirement that an order to increase the levy ceiling above the annual increase in line with increases in the general level of earnings must not be made unless a draft of the instrument has been laid before Parliament and approved by a resolution of each House of Parliament.

Ministers chose this option because it would reduce the time and resources used on routine activities.

Impacts

The change in legislation is intended to reduce the time and resources expended by officials and Ministers to routinely uprate the PPF administration levy, the levy ceiling and the pension compensation cap.

F. Pension compensation – admissible rules

Background

Schedule 7 to the Pensions Act 2004 provides the rules on pension compensation. Paragraph 35 stipulates what "admissible rules" are considered when calculating pension compensation. Paragraph 35 stipulates that certain changes made to scheme rules or discretionary increases in the three-year period before the start of an assessment period are disregarded.

Why consider change?

The PPF Board has alerted us to a concern that if an employer has powers to augment scheme benefits those changes would not be captured. This provides the potential for abuse – i.e. someone could augment scheme benefits for individuals or groups of people shortly before an insolvency event with the result that pension compensation would be paid at a higher rate. In addition, paragraph 35 is ambiguous because it does not make it clear that it applies to changes made to scheme rules or discretionary increases or a combination of the two.

Options considered

Other than to leave the legislation as now, no other options were considered.

Chosen option

The Bill amend paragraph 35 of Schedule 7 to the Pensions Act 2004 to clarify that the “admissible rules” that are considered when calculating pension compensation do not include rule changes, discretionary increases, augmentations or any combination of the three made in the three-year period before the start of an assessment period.

Ministers chose this option to clarify how certain pension benefits flow through to pension compensation.

Impacts

The change in legislation is intended to clarify how certain pension benefits flow through to pension compensation and to lessen the potential for abuse by the augmentation of scheme benefits for individuals or groups of people shortly before an insolvency event with the result that pension compensation would be paid at a higher rate. Any increase in pension compensation has the potential to flow through to an increase in the pension protection levy paid by schemes.

G. Pension compensation - deferral past normal pension age

Background

Schedule 8 to the Pensions Act 2008 amends Schedule 7 to the Pensions Act 2004 to allow pension compensation to be deferred past normal pension age (NPA). The amendments in the Pensions Act 2008 were made following a request from the PPF Board. The intention behind the proposal was that people who have different tranches of pension compensation due at different NPA’s would be able to defer payment so that all tranches could come into payment at the same time. That would reduce an administrative burden – the PPF currently has to administer each trance of pension compensation separately.

Why consider change?

The provisions in the Pensions Act 2008 do not work as intended. For example – the way and the in which revaluation is applied (revaluation is the process by which the annual value of compensation is increased in line with the increases in prices to the date when a person not in receipt of compensation reaches NPA). The amendments in Schedule 8 to the Pensions Act 2008 have not been commenced.

Options considered

Other than to leave the legislation as now, no other options were considered.

Chosen option

The Bill amends the rules on pension compensation in Schedule 7 to the Pensions Act 2004 so that people may defer payment of their pension compensation past their normal pension age (NPA) – and, if they do so: (a) the pension compensation cap would apply at the time the person first becomes entitled to pension compensation (their NPA); (b) revaluation only applies until a member’s NPA; and an actuarial increase is paid to take account of lost indexation (the process by which pension compensation in payment is increased each year in line with prices) and the fact that the compensation has not been paid for a period of time. Where there is entitlement to a survivor’s benefit, survivors would receive half of any pension compensation that has been deferred including any actuarial increase.

Ministers chose this option to enhance the rules on pension compensation.

Impacts

The change in legislation is intended to enhance the rules on pension compensation by allowing people defer the date from which their pension compensation starts to be paid. This would provide people with the flexibility to take small tranches of pension compensation, which in some circumstances can become payable at different dates, all together.

The change contributes to some relatively minor savings – PPF estimate less than £500,000 a year in total from all the PPF technical measures – in administration costs for both schemes in an assessment period and the PPF.

H. Pension compensation – revaluation of pension credit members

Background

Schedule 8 to the Pensions Act 2008 amends Schedule 7 to the Pensions Act 2004 to allow pension compensation paid to pension credit members (PCMs) to be revalued. The intention was that pension compensation would be revalued only where revaluation applied in the PCMs scheme.

Why consider change?

The provisions in Schedule 8 to the Pensions Act 2008 do not work as intended as they allow revaluation even where none was provided by a PCMs scheme. The legislation has not been commenced.

Options considered

Other than to leave the legislation as now, no other options were considered.

Chosen option

The Bill amends the rules on pension compensation in Schedule 7 to the Pensions Act 2004 to allow pension compensation paid to pension credit members to be revalued if their scheme provided for revaluation.

Ministers chose this option to enhance the rules on pension compensation.

Impacts

The change in legislation is intended to enhance the rules on pension compensation by including revaluation in the calculation of pension compensation for certain pension credit members.

Costs and benefits for all of the PPF measures

None of the amendments impose a cost on business. Amendments A, B, D and G would, however, result in some relatively minor savings – PPF estimate less than £500,000 a year - in administration costs for both schemes in an assessment period and the PPF.

Implementation

The intention is that changes A, B, D, G and H above would be implemented as soon as possible after the Bill is enacted and any secondary legislation is brought into force. Changes C and E do not require implementation.

Pension Compensation – Indexation

Background

The Bill makes a change to the legislation that governs the indexation of pension compensation paid by the Pension Protection Fund (PPF).

Pension compensation has some of its value protected against price inflation through a legal requirement to provide annual increases - “indexation”. Currently, this indexation is linked in statute to the retail prices index (RPI).

The Government announced on 8 July 2010 that it proposed to move to a different inflation measure - the consumer prices index (CPI) – as the basis for the indexation of pension compensation made by the PPF. This decision is part of a wider decision to use CPI as the Government’s general measure of inflation for social security benefits, Financial Assistance Scheme payments, State pensions, public sector pensions, statutory minimum revaluation of private sector pensions and pension compensation, which will all switch from RPI to CPI.

Although the Government’s intention is to use the CPI for increasing pension compensation, it does not want to be tied to using CPI by the legislation. The Government wants to be able to choose the best way to measure inflation and it might be that, in the future, CPI is no longer considered to be the best way to measure inflation. For example, the way CPI is determined may change, new measures of inflation may be introduced or the economy may change.

In order to provide this flexibility and avoid a proliferation of legislation should a change be required in the future, the Bill amends legislation to allow the Secretary of State (SofS) to choose the measure of inflation he or she thinks is appropriate. However, as the amended legislation will not set out a specific inflation measure for readers, the Bill requires the SofS to publish how the general level of prices has been determined – for example by reference to the CPI.

Why make the change

The Government believes that CPI is an appropriate measure of price changes. The CPI measure:

- provides consistency with the measure used as the Bank of England’s inflationary target;
- is a better reflection of actual inflation experiences because its methodology takes account of substitution behaviour;
- is the headline and most high profile measure of inflation; and
- excludes mortgage interest payments, which are not relevant to most benefit and pension recipients (a sharp drop in mortgage interest in 2009 was the chief cause of a fall in RPI, in turn causing many pensions to be frozen)

Which options were considered?

The Government believes that it would be inappropriate to use a different measure for the PPF - which is a protection scheme - than for the legislation governing pension schemes themselves.

Stakeholder views

Initial feedback suggests the following positions of key stakeholders:

- Members of affected schemes and their representatives oppose the change to CPI as it will lead to lower payments in the future
- Trade Unions. Opposed.
- Pensions Professionals. Neutral.
- Also, the Board of the Pension Protection Fund is neutral - the change is a matter of Government policy.

<u>Impacts</u>

Individuals

The PPF estimate a 4.8% reduction (NPV £500m) in current liabilities resulting from the proposal, based on an estimate of 0.5% for the RPI-CPI gap. This includes revaluation and indexation. The Bill only covers the indexation change for pension compensation. Changes in respect of revaluation are being taken forward by Regulations.

The £500m figure relates to all changed future cash-flows. Due to the features of PPF compensation such as recognising divorce, dependents and inheritance rules the changes to future cash-flows will last for many years in the future – potentially in excess of 100 years. However, the vast majority of the changed cash-flows will occur over the next 60 years. As such, whilst the £500m is calculated across all cash-flows, the impact is shown as applying over 60 years, as saying the changes lasted over 100 years would be misleading given only a very small number of individuals would be affected over such a time period..

Pension Schemes

The reduction in PPF liabilities represents a transfer of £500m NPV from current members of the PPF to employers sponsoring Defined Benefit Pension Schemes who fund the PPF through a compulsory levy. Once again, the transition period during which the vast majority of the cash flows are changed is expected to be approximately 60 years.

The PPF's Annual Report and accounts published in October 2010 note that the capital impact of the change would, at the best estimate, reduce its future liabilities by approximately £500m. These accounts were audited by the National Audit Office. As mentioned previously, this figure is based on an assumption of a 0.5% difference between CPI and RPI.

Business

For regulatory purposes it is helpful to convert the overall NPV of £504m to an annual equivalent and so it is useful to note that a figure of £44m for the next 20 years would have the same net present value as the benefit to scheme sponsors from these reforms. Twenty years is chosen as this is the duration over which the PPF has an ambition to become self-sustaining. Therefore the saving to firms from this reform has the same monetised value as annual savings of £44m over a period of 20 years. We consider £44m to be the value of the annual equivalent saving to business and is therefore appropriate to be scored as an "OUT". It should be noted however that this figure does not relate to the cash flows of firms or the pensions of PPF members and is provided purely and solely for One-in, One-out purposes.

The PPF

Implementation costs are not expected to be significant.

<u>Implementation</u>

It is hoped that the changes made by the Bill will take effect on 1 January 2012.

Amendments to time periods relating to the Pensions Regulator's anti-avoidance powers in the Pensions Act 2004

<u>Background</u>

The Bill amends legislation around tPR in the light of live running since April 2005. The policy intention behind the changes is to ensure that the time periods relating to the Regulator's anti-avoidance powers operate fairly for business particularly in cases with inherent complexity, such as large multi-national and multi-employer groups.

The Pensions Act 2004 gave the Regulator powers to address the risk of "moral hazard" or avoidance activity. This is the deliberate manipulation of the affairs of an employer responsible for sponsoring a defined benefit scheme in an attempt to walk away from their pension obligations or to off-load them onto the PPF. The Regulator has two main anti-avoidance powers:

- A contribution notice (CN) permits the Regulator to require a cash payment to the pension scheme up to the value of the section 75 debt under the Pensions Act 1995 (the section 75 debt established the sponsor employer's debt to the scheme). There are certain grounds for the use of this power, this includes where an act or failure one of the main purposes of which is to avoid the employer's section 75 debt to the scheme (actual or contingent). In order to impose liability on any person to pay the sum specified in a contribution notice, the Regulator must be of the opinion that it is reasonable to impose such liability on that person.
- A financial support direction (FSD) allows the Regulator to direct that that arrangements are put in place by the employer or a connected or associated person to ensure that financial support is put in place for the pension liabilities of the sponsoring employer. Financial support may include parental guarantees, joint and several liability or such other arrangements as are proposed by the recipient of the FSD ("the target") and are approved by the Regulator. In order for an FSD to be issued, the sponsoring employer company must be either a "service company", or be "insufficiently resourced", as defined by section 44 of the Act. In the event of non compliance with an FSD, the Regulator is empowered by section 47 to issue a contribution notice to any person where it is of the opinion that it is reasonable to impose liability on that person to pay the sum specified in the notice having regard to a number of specified factors.

Why consider change?

The Regulator has found that in practice it can take many months from the time it begins to investigate a case to the time it has sufficient evidence to issue a CN or an FSD warning notice, and then there could be further months before the Determinations Panel could issue the decision (the determination notice). In complex cases, very often involving multi-national companies, the time required by the legislation for the whole process means that there can be a compressed timeframe within the FSD 2-year period (6 years for CNs) for the affected company to prepare its response to a warning notice of intended proceedings. The intervention is needed to ensure an adequate and appropriate time period for companies to make representations.

Stakeholder views

The current arrangement has led to criticism from directly affected parties, usually business and advisers, who have complained of having too little time for representations and if the proposed change is not introduced, there could be a significant risk that some directly affected parties could be placed at a disadvantage in having only a short time in which to make representations.

Which options were considered?

While it would be possible to again extend the prescribed period within Regulations, it would not entirely address the root cause of the problem, that is, ensuring there is a longer period of time, where appropriate, for recipients of a notice to prepare meaningful representations for the Determination Panel's hearing.

Option chosen

It is proposed to amend the primary legislation so that the end point of the prescribed period is the issuing of the warning notice instead of a determination notice. This should provide for a sufficiently long period between the warning notice and the issuing of the determination notice to enable targets and other directly affected parties to have sufficient time to make representations in response to the warning notice, after which the Determinations Panel will have to decide whether it is justifiable to issue a determination notice.

It is also proposed that section 43 should then include a negative resolution regulation-making power to set out the maximum period between the issue of the warning notice and the issue of a determination notice by the Determinations Panel.

Impacts

The overwhelming majority of pension schemes and employers/businesses will not be affected by this proposals and the change would not therefore represent a burden on employers, business or the Regulator. Those very few employers, who are the subject of a Regulator warning notice, may well find their costs reduced as advisers and lawyers will have more time to prepare cases but it is not possible to quantify. It will not affect individuals, the pensions industry or the exchequer.

Costs and benefits

There are no financial costs resulting from this proposal, and the benefits are that the change will give companies adequate time to prepare within the fixed statutory time-scales.

Implementation

The intention is that this change can be effected in line with any “common” date specified for Pensions Bill measures.

SPECIFIC ITEMS CHECKLIST FOR ALL PENSION PROTECTION MEASURES

Equality and Fairness

Women may be impacted more by changes to indexation as they currently live longer than men, although the gap between male and female life expectancy is narrowing.

It is not believed that there will be an impact on the equality strands as a result of the proposed amendments.

Human Rights

There should not be any effects on human rights as a result of the proposed amendments

Small Firms Impact Test

The proposals will not have a negative effect on small firms. In general the effect on businesses should be neutral.

Competition Assessment

The provision of a defined benefit occupational pension scheme is currently voluntary. The impact of these changes on businesses will be very slight and there should therefore be no impact on competitiveness.

Legal Aid

There will no impact on Legal Aid.

Sustainable Development, Carbon Assessment, Other Environment

There will be any impacts on these areas. The initial tests have been looked at and do not apply.

Health Impact Assessment

No health impact issues were identified by the initial assessment.

Enforcement and Sanctions

The proposals would not involve any changes to enforcement and sanctions.

Rural Proofing

No impact on rural communities was identified by the initial rural proofing assessment.

GUIDANCE

There is discretion for departments and regulators as to how to set out the evidence base. However, it is desirable that the following points are covered:

- Problem under consideration;
- Rationale for intervention;
- Policy objective;
- Description of options considered (including do nothing);
- Costs and benefits of each option;
- Risks and assumptions;
- Administrative burden and policy savings calculations;
- Wider impacts;
- Summary and preferred option with description of implementation plan.

Inserting text for this section:

Select the notes here and either type section text, or use **Paste Without Format** toolbar button to paste in the standard EBBodyPara Style. Format text by applying EB styles from the toolbar.

Annexes

Annex 1 should be used to set out the Post Implementation Review Plan as detailed below. Further annexes may be added where the Specific Impact Tests yield information relevant to an overall understanding of policy options.

Annex 1: Post Implementation Review (PIR) Plan

A PIR should be undertaken, usually three to five years after implementation of the policy, but exceptionally a longer period may be more appropriate. A PIR should examine the extent to which the implemented regulations have achieved their objectives, assess their costs and benefits and identify whether they are having any unintended consequences. Please set out the PIR Plan as detailed below. If there is no plan to do a PIR please provide reasons below.

Basis of the review: **[The basis of the review could be statutory (forming part of the legislation), it could be to review existing policy or there could be a political commitment to review];**
Review objective: **[Is it intended as a proportionate check that regulation is operating as expected to tackle the problem of concern?; or as a wider exploration of the policy approach taken?; or as a link from policy objective to outcome?]**
Review approach and rationale: **[e.g. describe here the review approach (in-depth evaluation, scope review of monitoring data, scan of stakeholder views, etc.) and the rationale that made choosing such an approach]**
Baseline: **[The current (baseline) position against which the change introduced by the legislation can be measured]**
Success criteria: **[Criteria showing achievement of the policy objectives as set out in the final impact assessment; criteria for modifying or replacing the policy if it does not achieve its objectives]**
Monitoring information arrangements: **[Provide further details of the planned/existing arrangements in place that will allow a systematic collection systematic collection of monitoring information for future policy review]**
Reasons for not planning a PIR: **[If there is no plan to do a PIR please provide reasons here]** **A formal PIR is not planned as the Department for Work and Pensions has continuous policy and stewardship oversight of the Pension Protection Fund and the Pensions Regulator.**