

**EXPLANATORY MEMORANDUM TO**  
**THE FINANCIAL ASSISTANCE SCHEME (MISCELLANEOUS**  
**AMENDMENTS) REGULATIONS 2007**

**2007 No.3581**

1. This explanatory memorandum has been prepared by the Department for Work and Pensions and is laid before Parliament by Command of Her Majesty.
2. **Description**
  - 2.1 These Regulations extend eligibility to assistance from the Government's Financial Assistance Scheme (FAS). They remove the tapered assistance levels that currently apply so that 80 per cent core assistance (subject to the cap) is available to all eligible qualifying members at age 65, regardless of how far away they were from their scheme pension age on 14<sup>th</sup> May 2004. The Regulations also increase the cap on maximum assistance from £12,000 to £26,000; and remove the de minimis rule that excludes those whose FAS payment would be £10 or less a week. Complementary changes are also made to the treatment of survivors.
  - 2.2 These Regulations also change the Financial Assistance Scheme pension scheme qualifying rules to cover members of schemes that began winding up between 1 January 1997 and 5 April 2005 where a compromise agreement is in place and where enforcing the debt against the employer would have forced the employer into insolvency. They also allow certain Small Self Administered Schemes to be considered qualifying schemes.
  - 2.3 In addition they introduce a number of amendments linked to the insolvency cut-off date, the calculation of payments, the provision of information and introduce new powers linked to reclaiming overpayments of assistance.
3. **Matters of special interest to the Joint Committee on Statutory Instruments**
  - 3.1 None
4. **Legislative background**
  - 4.1 These Regulations implement the extension of the Financial Assistance Scheme as announced in the Budget in March 2007. They also include various amendments to the scheme that have arisen following consultation with stakeholders or have come to light during operational running of the scheme over the last year. The changes made to initial payments in part

bring the regulations into line with that part of section.18 of the Pensions Act 2007 that relates to initial payments.

## **5. Territorial Extent and Application**

5.1 This instrument applies to all of the United Kingdom.

## **6. European Convention on Human Rights**

The Minister for Pensions Reform, Mike O'Brien, has made the following statement regarding Human Rights:

In my view the provisions of The Financial Assistance Scheme (Miscellaneous Amendments) Regulations 2007 are compatible with the Convention rights.

## **7. Policy Background**

- 7.1 The Financial Assistance Scheme (FAS) was originally designed to focus help on those who had suffered significant losses and were closest to retirement as it was felt that these members were least likely to be able to make up any shortfall in their retirement income.
- 7.2 In its original form the FAS provided assistance to members of qualifying defined benefit occupational pension schemes which started to wind up, under-funded, between 1st January 1997 and 5th April 2005, where the relevant employer was subject to a qualifying insolvency event.
- 7.3 Under this earliest version of the FAS, only those qualifying members who were within three years of their normal scheme retirement age (as of 14th May 2004) could receive top-ups to around 80 per cent of their expected core pension.
- 7.4 Some surviving spouses and civil partners of qualifying scheme members who died after their scheme started to wind-up were also eligible for a payment from the FAS, as were some of those who were in receipt of a survivor's pension before wind-up started.
- 7.5 A payment cap of £12,000 per year applied which meant that qualifying members would receive assistance that would top up their scheme pension to 80% of their expected core pension, or to £12,000 per year, whichever was the lower figure.
- 7.6 Payments were also subject to a de minimis of £520 a year. This meant that payments would not be made unless they were calculated to be over £10 per week (before revaluation of the payment was applied).

- 7.7 An operational unit based in York opened for business on 1st September 2005 to administer the FAS.
- 7.8 The Government originally committed £400 million in cash terms of taxpayers' money over 20 years to this version of the scheme which was expected to help an estimated 15,000 people.

*The first extension to the FAS – the current scheme*

- 7.9 In May 2006, the Government announced a £1.9bn extension to the scheme - bringing the total funding to £2.3bn in cash terms over 60 years. This extension to the scheme was estimated to help around 40,000 people over its life time.
- 7.10 Under this extension, which came into force on 16th December 2006, qualifying members who were within seven years of their normal scheme retirement age (as of 14th May 2004) would receive top-ups to around 80 per cent of their expected core pension. For people seven to 11 years from scheme retirement age the figure would be 65 per cent, and for people between 11 and 15 years from retirement it would be 50 per cent.
- 7.11 The cap and de minimis rules were retained and applied to all beneficiaries in the same way and at the same level as previously described.

*The latest proposed extension*

- 7.12 In his Budget Statement on 21st March 2007, the Chancellor of the Exchequer announced that public funding for the Financial Assistance Scheme would be significantly increased. The key changes:
- all qualifying members of qualifying pension schemes will have their pensions topped up to a level broadly equivalent to 80% of the core pension rights accrued in their scheme (subject to the cap);
  - the cap will be increased from £12,000 to £26,000 a year;
  - the minimum payment rule (de minimis) will be removed.
- 7.13 As a result it is expected that all of the estimated 125,000 people who have lost their pensions as a result of their employer undergoing a qualifying insolvency event will now receive at least 80% of their core expected pension (subject to the raised cap).
- 7.14 This extension will mean that the Government's total long-term cash expenditure on the scheme will increase from £2.3 billion to £8 billion (or £1.9 billion Net Present Value).

- 7.15 In addition, the Government announced on 18th April this year that it will further extend FAS to cover members of schemes that began winding up between 1st January 1997 and 5th April 2005, where a compromise agreement is in place and enforcing the debt against the employer would have forced the employer into insolvency. It is estimated that this will mean that FAS will help around 13,500 members.
- 7.16 Following an approach from an affected scheme, the Government is also amending its definition of excluded schemes so that certain Small Self Administered Schemes may become eligible to seek assistance for their members from the FAS.
- 7.17 The Government is also amending the provision which currently prescribes a cut-off date by which an employer insolvency event must occur in order for a scheme to qualify for the FAS.

*Further potential changes to the FAS*

- 7.18 The Government has commissioned a FAS Review of Pension Scheme Assets, led by Andrew Young of the Government Actuary's Department, to assess whether better use can be made of funds in winding-up schemes and to assess other sources of non-public funding. The Government has pledged to match the additional value generated with the aim of moving towards 90% assistance levels.
- 7.19 The review team has also been asked to determine whether there are other pension schemes where, although the sponsoring employer has not undergone an insolvency event, it would not be reasonable to expect the employer to have a continuing responsibility for supporting an under funded scheme.
- 7.20 Any further changes to the FAS arising from the final recommendations of the review will be brought forward via legislation next year.

*A more detailed overview of the current scheme*

*Scheme Qualification*

- 7.21 A pension scheme must progress through two stages to qualify for the FAS, notification and qualification.
- 7.22 Notification is simply the provision of some basic information, including the name of the scheme and the name of any employer in relation to the scheme.

7.23 The scheme then has to meet the necessary qualifying conditions to be eligible as a qualifying scheme. For example, it must have completed notification as above; not be a money purchase scheme and have started winding up between 1 January 1997 and 5 April 2005. Also, the relevant employer must have experienced a qualifying insolvency event or, where no insolvency event referred to elsewhere in the regulations has occurred to the employer, the Secretary of State must be satisfied that:

- the employer is unlikely to continue as a going concern;
- the value of the employer's assets are less than the amount of its liabilities, taking into account its contingent and prospective liabilities; and
- the employer is unable to pay its debts as they fall due or have fallen due.

#### *Member qualification*

7.24 Currently, a scheme member may be considered for a FAS payment if he belongs (or belonged) to a qualifying pension scheme, and if he was within fifteen years of his pension scheme's normal retirement age (NRA) or older on 14 May 2004 (when the FAS was announced). Those members within 7 years of their NRA on 14th May 2004 ('Group 1 members') benefit from FAS topping up their pensions to 80% of their 'expected pension' (subject to the cap and de minimis mentioned previously). Those between 7 and 11 years from their NRA ('Group 2 members') are considered for a top-up to 65% of their 'expected pension', and 50% for those between 11 and 15 years ('Group 3 members') (again subject to a de minimis and a cap)

7.25 Surviving spouses and civil partners of qualifying scheme members who died after their scheme started to wind-up may also be eligible for a payment but at a lower rate. Some of those who were in receipt of a survivor's pension from the qualifying pension scheme before wind-up may also be eligible for a payment in their own right if they meet the NRA rule.

7.26 In most cases FAS payments begin from the 65th birthday. Survivors and qualifying members who are terminally ill may be paid earlier than 65.

7.27 There are two types of FAS payment: Annual Payments and Initial Payments

7.28 'Annual payments' cannot be determined until scheme liabilities in respect of a member have been discharged or the allocation of scheme assets finalised. This usually occurs at the end of the scheme wind-up process, which can take some time.

- 7.29 However, in order to provide some assistance to qualifying members who turn 65 and whose liabilities are not discharged before the end of wind-up, FAS can, at the request of trustees, make discretionary ‘initial payments’ in anticipation of their eventual receipt of annual payments. Initial payments top up any interim pension the scheme is paying members to 80 per cent of expected core pension (subject to the cap and de minimis). Initial payments can also be made to survivors of qualifying members who have died during wind-up.

### *The Changes*

- 7.30 These Regulations make a number of changes to the Financial Assistance Scheme Regulations 2005 (SI 2005/1986). These amending Regulations:
- remove the date by which an insolvency event must occur if a pension scheme is to be considered a qualifying scheme within the Financial Assistance Scheme. Under current regulations the relevant employer of a pension scheme must have undergone a qualifying insolvency event by 28th February 2007 in order for their scheme to qualify for FAS. On the 27th February 2007, the then Minister of State for Pensions Reform announced that he would extend that date to 31st August. However, following a recommendation in the interim report of the Young Review (published in July) the Government has confirmed that it will not now enforce that date.

However, the Government continues to believe that where there is a healthy solvent employer that employer has a moral obligation to meet the pension promise made to their members. Therefore, whilst we will remove the cut-off date that applies to employer insolvency events by regulations, we have inserted a provision that means that the scheme manager must be of the opinion that the wind-up of the scheme and the insolvency event of the employer were linked in order for the scheme to qualify.

We expect that employer insolvency will already have occurred or will occur soon for most relevant schemes and we will assume that scheme wind-up and employer insolvency were linked in relation to employer insolvencies that occur before 1st January 2009: we have no reason to believe otherwise and this assumption will aid administrative processes.

For employer insolvency events that occur after that date evidence of a connection will need to be provided and the scheme manager will have to take the view that scheme wind-up and the insolvency event were linked in a relevant way in order for the scheme to

qualify for the FAS. For example, schemes might provide evidence from company accounts that shows the employer was in a difficult financial position before the start of scheme wind-up which continued up to the insolvency event.

- provide the scheme manager with discretion to accept certain schemes that began winding up between 1st January 1997 and 5th April 2005 as qualifying schemes where no insolvency event referred to elsewhere in the regulations has occurred to the employer, where:
  - a compromise agreement is in place; and
  - he is satisfied that had a compromise agreement not been entered into either the value of the employer's assets would have been less than the amount of its liabilities, taking into account its contingent and prospective liabilities, or
  - the employer would have been unable to pay its debts as they fell due.

In order for us to take decisions on whether or not this new provision is met scheme representatives will need to provide suitable evidence. We envisage that such evidence might include:

- statements of accounts showing the employer's assets and liabilities;
- evidence of the full debt that would have been payable by the employer had the debt not been compromised;
- evidence of the binding agreement that compromised the employer debt; and
- documented reasons for accepting the compromise agreement and any supporting documentation, for example copy of an independent auditors report about the employer's financial position

Many compromise agreements were entered into before the FAS was announced. In many cases, had trustees known at the time that by compromising the debt to keep an employer solvent they would exclude their members from FAS they might have chosen instead to force employer insolvency to ensure FAS qualification for their members.

The Government's intention is to help members of pension schemes where there is no legal obligation for the employer to contribute further to the scheme and where the trustees reached a compromise agreement in an attempt to secure maximum financial advantage for their scheme members, where the insolvency of the employer was otherwise inevitable. We believe that the regulations

as drafted strike the right balance between ensuring that trustees and employers have acted reasonably in reaching a compromise agreement whilst preventing the taxpayer from having to subsidise the failure of unscrupulous employers from meeting their pension promise.

The Young Review of pension scheme assets is looking at schemes in similar circumstances which are not covered by these or previous regulations. The recommendations of the Review are expected in 2007 and the Government will respond in due course.

- allow certain Small Self Administered Schemes (SSAS) to gain entry to the FAS. As things stand, SSAS designated as such by virtue of historic HMRC legislation, cannot qualify for the FAS. The vast majority of such schemes were established on a money purchase basis. However, we have received representations from a scheme that offered defined benefits and that is ruled out by this provision. The members of the scheme appear to be in similar circumstances to members of other schemes that are already being assisted by the FAS: they had an accrued right to a defined benefit that has been significantly depleted through no fault of their own as a result of their employer's insolvency. We believe the FAS should be extended to include such members. This amendment replaces the definition formerly employed by HMRC with one used elsewhere in pension's legislation (for example in relation to qualification for the Pensions Protection Fund).
- extend eligibility for help from the Financial Assistance Scheme to all members of qualifying pension schemes irrespective of how close they were to their pension scheme's normal retirement age (NRA) on 14th May 2004. Further amendments are made to remove the tapers that currently apply to qualifying members so all members of qualifying pension schemes will have their pensions topped up to a level broadly equivalent to 80% of the core pension rights accrued in their scheme (subject to the cap). These changes will apply to annual and initial payments and were announced in the Budget in March this year. A similar change to initial payments was brought forward via the Pension Act 2007 which received Royal Assent in July. This amendment brings the FAS regulations into line with the change to initial payments implemented by the Act. Payments of annual and initial payments will continue to start at a member's 65<sup>th</sup> birthday unless the member qualifies for early access on the grounds of terminal illness.
- increase the cap on assistance from £12,000 to £26,000 and completely remove the de minimis below which level no payments



of assistance are made. The Government recognises that it is not appropriate in the longer term for the FAS cap to remain static. On 21st May 2007 the then Minister for Pensions Reform told the House of Commons that “we intend to ensure that the cap retains its value, even where assessments are made for members who will not be eligible for payment until many years in the future.”

However, we believe that the treatment of the cap is best considered in the wider context of any changes to the FAS that may arise from the Young Review of pension scheme assets that is expected to report later in November. Our priority in these regulations is to introduce the changes to the FAS announced in the Budget 2007 that will increase assistance available to members now. As relatively few members are affected by the cap and as any significant effect of non-indexation will not bite for some time, we consider that it makes sense to defer any associated changes to the cap to the New Year where they can be considered and consulted upon alongside any other necessary changes to the way in which assistance is calculated.

- provide the FAS scheme manager with the power to re-determine the amount of an initial payment if the amount paid by way of initial payment is incorrect. Initial payments are designed to top-up interim pensions paid by schemes but different amounts of interim pension might be paid by schemes across different periods. If we were to determine FAS initial payments on the amount of interim pension in payment at a particular point in time and backdate those payments to an earlier date, and if different interim pensions had been paid during that earlier period, then this could result in either an excessive payment or an underpayment counter to our intention that eligible members receive 80% of their core expected pension during the wind-up of their scheme.
- clarify that all of those people who start to receive a survivor's or a dependent's pension from a qualifying scheme before that scheme starts to wind-up stand to receive FAS assistance based on the unreduced survivor's or dependent's pension they would have received had their scheme been able to meet their pension in full (rather than by reference to the deceased member's 'expected pension'). As FAS regulations stand only those people in receipt of such pensions at the crystallisation date fall to be treated in this way; this amendment corrects that oversight.
- clarify that initial payments fall to be revalued where there is a month or more between certification date and the date on which an initial payment is first payable to a beneficiary in the same way as

revaluation is applied to annual payments. The amendment corrects an oversight in the original regulations.

- extend the powers of the scheme manager to re-determine rates of annuity. Under current regulations rates of annuity can effectively be re-determined if trustees secure annuities with annual increases greater than those provided for in scheme rules. This power was intended to help prevent trustees taking advantage of the publicly funded FAS by purchasing enhanced annual increases which would lower the starting rate of an annuity and therefore increase the FAS top-up.

We understand that scheme rules often allow trustees significant discretion over the increases they could secure and we have recently been asked by trustees how we would treat annuities secured with a lower initial annuity rate but enhanced increases. As this action could increase Government liabilities and decrease the additional benefits that might be realised as a result of the Young Review we have made a change to the FAS regulations so that the scheme manager has the power to re-determine annuity rates where he considers that annual increases that have been secured are unreasonable. Given the potential for moral hazard, and given that annuity quotes are often time-bound (such that rates offered by insurers may be guaranteed only for a limited period) we have not consulted on this change to regulations on grounds of urgency.

- corrects a typographical error linked to the description of handling commutation in initial payment cases

7.31 The Regulations amend the FAS (Provision of Information and Administration of Payments) Regulations 2006 to:

- permit the scheme manager to prescribe the manner in which information should be provided to enable a decision on scheme and member eligibility.
- provide for a new power to recover overpaid assistance from individuals who are not beneficiaries as defined within the main FAS regulations.
- expand the powers of the scheme manager to suspend payments of FAS to non-beneficiaries of pension schemes.

#### *Consultation*

7.32 As the Regulations were made more than six months after the coming into force of the provisions of the Pensions Act 2004 under which the majority are made, the Secretary of State was required to consult such persons as he considered appropriate before making them.

- 7.33 The consultation period started on 29th August and closed on 9th October 2007. The length of the consultation struck a reasonable balance between time for respondents to contribute, and bringing in the rules to allow payments to be issued. Where proposals have been stimulated by previous consultation, Cabinet Office guidance provides that a shorter consultation period may be appropriate. Taking account of all these factors, Ministers decided that a consultation period of 6 weeks was appropriate.
- 7.34 60 responses were received on the draft regulations with most of those who did respond criticising the broad scope of the scheme - such as the level of assistance or payment from 65 rather than normal retirement age - rather than the detail of the proposals. A response to the consultation was published on the FAS website - <http://www.dwp.gov.uk/fas> - at the time these regulations were laid.
- 7.35 As described under the penultimate bullet point in paragraph 7.30 above we are making a change to regulations in order help prevent trustees buying annuities with enhanced annual increases and thus increasing government liabilities. We have not consulted on this change for reasons of urgency.

#### *Guidance*

- 7.36 Details of the proposed changes have been published on the FAS website. We have also been liaising with trustees and scheme managers to assist them in understanding the impact of the changes. We will also be updating our public facing leaflets and guidance.

#### *Consolidation*

- 7.21 Consolidated versions of the FAS regulations will be available in the Law Relating to Social Security (Blue Volumes). These can be found at <http://www.dwp.gov.uk/advisers/docs/lawvols/bluevol/index.asp>. These are updated quarterly and are available on the internet at no cost to the public.

## **8. Impact**

- 8.1 An impact assessment has not been published for this instrument as it has only a negligible impact on business, charities and voluntary bodies.
- 8.2 The impact on the public sector is nil.

## **9. Contact**

Any enquiries about the contents of this memorandum should be addressed to: Mr C Jennings, Department of Work and Pensions, FAS Team  
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