# EXPLANATORY MEMORANDUM TO THE

# INDUSTRIAL TRAINING LEVY (ENGINEERING CONSTRUCTION BOARD) ORDER 2005

## 2005 No. 2089

**1.** This explanatory memorandum has been prepared by The Department for Education and Skills and is laid before Parliament by Command of Her Majesty.

This memorandum contains information for the Joint Committee on Statutory Instruments and the House of Lords Merits Committee

## 2. Description

This instrument grants power to the Engineering Construction Industry Training Board (ECITB) to impose a levy on employers in the Engineering Construction Industry and sets the rates of and exemptions from that levy.

## 3. Matters of special interest to the Committees

None

## 4. Legislative Background

The above Order is to be made in exercise of the powers conferred by section 11(1) of the Industrial Training Act 1982 (ITA). The Order is subject to affirmative resolution.

## 5. Extent

This instrument applies to Great Britain.

## 6. European Convention on Human Rights

The Parliamentary Under Secretary of State for Skills and Vocational Education has made the following statement regarding Human Rights:

In my view the provisions of the Industrial Training Levy (Engineering Construction Board) Order 2005 are compatible with the Convention rights

## 7. Policy background

### The purpose of Industrial Training Boards

Industrial Training Boards (ITBs) are set up under the ITA to ensure that the quantity and quality of training are adequate to meet the needs of the industries for which they are established.

There are currently 2 ITBs covering the construction and the engineering construction sectors and both are Non-Departmental Public Bodies. They provide a wide range of services and training initiatives, including setting occupational standards and developing vocational qualifications, delivering Modern Apprenticeships and paying direct grants to employers who carry out training to approved standards.

Employers in these sectors have consistently supported statutory underpinning for their training arrangements. They argue that the nature of their industries mean that individual employers are unable or unwilling to accept the responsibility of training their own employees. They believe that a national pool of labour, collectively funded by all employers, is the only way the industries' skill needs can be met.

### Levy Arrangements

The ITA contains provision for a levy on employers to finance an ITB's activities and to share the cost of training more evenly between companies in the industry. It is for the ITB to make proposals for the rate of levy for the industry it covers and for the Secretary of State to make an order giving effect to the proposals.

This Order gives effect to proposals submitted by the Engineering Construction ITB (ECITB) for a levy to be collected in 2006.

Every employer whose main activity is included in the definition of the engineering construction industry as set out in S.I. 1991/1305 is assessed to levy. Employers are legally required to pay the levy unless they are exempted by the ECITB.

### Exclusions

The ITA requires small firms to be excluded from the levy but does not set a minimum size threshold. In the Instrument Head Offices whose combined payroll and net expenditure on sub-contract labour is £1 million or less and sites whose combined payroll and net expenditure on sub-contract labour is £275,000 or less are exempt. The exemption is calculated by reference to an employer's payroll figure rather than the number of employees. This is because the numbers employed in any year by an employer in this industry, which largely operates on a short-term contract basis with significant usage of labour–only subcontractors, fluctuate and are therefore difficult to calculate or audit, should that be needed.

There is no exemption for other classes of employer.

### Costs to the public and/or the Exchequer

Levy rates are determined by the employer members of an ITB and are fixed in light of the Board's general policy and plans. They must cover the cost of the Board's plans for the year in question.

The ECITB rates for 2005 are 0.18% of the total of an employer's payroll and net expenditure on sub-contract labour for Head Offices and 1.5% of the total of payroll and net expenditure on sub-contract labour for engineering construction sites. There is no ceiling to the amount of levy paid by an employer. The proposals are expected to raise £10 million in the financial year-ended 31 December 2006.

For each Board the proposals involve a levy greater than 0.2% of an employer's payroll with no provision for exemption. Section 11 of the ITA says that in this case the Secretary of State may not make the Order unless he is satisfied that the proposals are necessary to encourage adequate training in the industry and that one of three conditions is satisfied.

The conditions are:-

(a) that organisations representing more than half the persons likely to pay the levy and organisations representing persons who together are likely to pay more than half the aggregate amount of the levy consider, after taking reasonable steps to consult their members, that the proposals are necessary to encourage adequate training in the industry.

(b) that the Order will be made less than two years after the making of a former levy Order giving effect to proposals in respect of which condition (a) was satisfied.

(c) that neither condition (a) or (b) applies, but the proposals are considered by the Secretary of State to be appropriate in the circumstances.

Formal consultation on the proposals took place in the summer of 2004 and they were supported by the industry's main employer organisations, who represent over 50% of leviable employers. Those employers are together likely to pay 87% of the total levy. Condition (a) above has therefore been satisfied.

## 8. Impact

A Regulatory Impact Assessment is attached to this memorandum

## 9. Contact

Simon Perryman at the Department for Education and Skills Tel: 0114-259-3913 or e-mail: simon.perryman@dfes.gsi.gov.uk can answer any queries regarding the instrument.

**REGULATORY IMPACT ASSESSMENT**

**THE INDUSTRIAL TRAINING LEVY (ENGINEERING CONSTRUCTION BOARD) ORDER 2005**

**Declaration:**

**I have read the Regulatory Impact Assessment and I am satisfied that the balance between cost and benefit is the right one in the circumstances.**

**Signed by the responsible Minister**

**Ivan Lewis**
**……**

**Date ……22 November 2004……**

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**Date:** 11 November 2004

**Department:** Education and Skills

**REGULATORY IMPACT ASSESSMENT**
**THE INDUSTRIAL TRAINING LEVY (ENGINEERING CONSTRUCTION BOARD) ORDER 2005**

## The Issue and Objective

1. The measure gives effect to one of the provisions of the Industrial Training Act 1982, which empowers the Secretary of State to set up industrial training boards (ITBs) to ensure that the quantity and quality of training are adequate to meet the needs of the industry for which they are established. It enables the Engineering Construction Industry Training Board (ECITB) to impose a levy on employers, other than the smallest, whose activities fall within its scope (as defined in the Industrial Training (Engineering Board) Order 1964 (amended by the Industrial Training (Engineering Construction Board) Order 1991)).

2. The context of this legislation is unusual in that it is to all intents and purposes self-imposed, and this should be taken into account in any judgement of the way in which it impacts on employers in the engineering construction industry. Against the tide of Government policy of transforming ITBs from statutory to non-statutory organisations, two industries, of which this is one have, through their representative organisations, persuaded the government to retain their statutory basis, including the power to impose a levy. This is to address particular industry characteristics which are outlined in paragraph 15. In practice this means that each year the engineering construction industry, after a process of consultation (as required by the Industrial Training Act), submits, through the ECITB, its proposals for the following year's levy arrangements. The industry has had a levy/grant arrangement for over 35 years.

3. The Industrial Training Act 1982 also empowers ITBs to make grants to those employers whose training courses are approved by the Board. An employer who provides no training will have to pay a levy but will get no grant from the Board; an employer who does approved training will pay the levy but may receive grants towards the cost of training. In this way an employer will have an incentive to see that employees receive training and in particular to see that the quality of training is of a standard approved by the Board.

4. In addition to the payment of direct grants, the ECITB funds and manages a range of training programmes, including an apprenticeship scheme; up-skilling training for new entrant and existing adult employees in craft, technician and supervisory management skills. Engineering construction is an industry with considerable movement of labour between employers and projects and a high degree of labour-only subcontracting. These programmes are designed to benefit the industry collectively by providing a pool of skilled labour from which all employers benefit. The Board also provides a free training consultancy service to the industry and develops standards of competence and associated national vocational qualifications and training specifications. It also awards qualifications, often in partnership with other organisations.

5. It is for the Board to make proposals for the particular levy arrangements and rates for the industry. Levy proposals are submitted annually by the ECITB and are subject to Ministerial and Parliamentary approval. This RIA concerns the levy arrangements for 2006.

6. The measure is designed to:

- share the cost of training between firms

- secure an adequate supply of properly trained workers at all levels in the industry

- meet the administrative expenses of the Board

**Risk Assessment**

**(i) The problem and harm**

7. The statutory Industrial Training Boards (ITBs) which had been set up by the Industrial Training Act 1964 were progressively wound-up between 1981 and 1992 and replaced by new employer-led organisations without a statutory framework.

8. However, employers in the engineering construction industry have consistently put forward a strong case for the continuation of statutory training arrangements for their sector.

9. Ministers have acknowledged that to insist on non-statutory arrangements is unrealistic and have agreed to retain a statutory ITB subject to regular review. The ITB is governed by the Industrial Training Act 1982, which includes the power to raise a levy. The levy is imposed by an order which gives effect to proposals which are submitted annually by the Board and require the approval of both Houses. The smallest employers are exempted from the levy.

**(ii) The risk**

10. The industry argues that without collectively funded training, paid for by a statutory levy on all employers and administered by the ITB, there is a serious risk that insufficient training will be carried out to meet the industry's skill needs.

11. This could result in skill shortages, wage inflation and a less competitive engineering construction industry.

**Options**

12. There are two options:

Option 1 - reject the proposals. This would mean that the Board would have no levy income for the financial year ended December 2006 and the only money available for operating purposes would be its reserves, which would soon be exhausted.

Option 2 - approve the proposals and enable the Board to raise the income it requires to continue to provide incentives by way of grants for employers who train. Also to deliver the training services required by the industry.

**Issues of Equity and Fairness**

13. The context of this legislation is unusual in that it is to all extents and purposes self-imposed by the employers in the engineering construction industry.

14. It runs contrary to the current position of non-statutory training arrangements in most industry sectors but is nevertheless employer-led and employer-funded in accordance with employers' wishes.

**Identify the Benefits**

15. The options have the following benefits:

Option 1 - employers would not have to pay the training levy but, according to the industry, the particular employment patterns in the sector i.e. the itinerant nature of the workforce and extensive use of labour-only subcontractors, mean that employers individually might not be prepared or might be unable to undertake adequate (either qualitative or quantitative) training.

Option 2 - with its operating income secured the Board would be able to continue to organise, manage and fund the range of training services that have been developed in on the industry's behalf. The cost would be shared between firms.

**Quantifying and Valuing the Benefits**

16. The monetary benefit for each option is:

Option 1 - zero

Option 2 - £12.4m (estimated expenditure on grants & training programmes) plus the benefits of the Board's other services e.g. training consultancy, research & development of training standards, qualifications and materials. Also the availability of a skilled pool of labour from which all employers benefit

17. The costs of the options are:

Option 1 – cannot be quantified or costed

Option 2 - £9.5 - £10m raised in levy from the industry

18. £12.4m is expected to be returned to the industry in the form of grants and training programmes. The nature of these is set out in paragraph 4.

**Business Sectors Affected**

19. Employers in the engineering construction industry as defined in the Industrial Training (Engineering Board) Order 1964 (amended by the Industrial Training (Engineering Construction Board) Order 1991).

20. Estimated no of companies in sector - 400 (estimated total employees - 66,000 of which 9,500 are employed under labour-only agreements). Employers are not required to register with the ECITB; rather it is for the ECITB to identify those that fall within its scope. Around 202 (59%) site establishments and 264 (77%) Off Site establishments are expected to fall below the exclusion threshold and thus will not be liable to pay the respective levy.

**Compliance Costs for a "Typical" Business**

21. The compliance cost for business is:

- the cost of training not previously carried out but which has been encouraged by the imposition of the levy (see note below).

- the cost of completion of the annual levy assessment return

- the amount of the individual levy assessment

- the cost of processing the levy bill

- the cost of completion of grant claims

*Less*

- the benefits of training grants and programmes and other Board services

Note: The purpose of the Industrial Training Act 1982 is to encourage adequate training in any given industry. The imposition of a levy/grant mechanism means additional training costs are incurred in the short term. The cost of training is made up of training fees paid and productivity loss of the trainees attending the course. This cost is difficult to calculate exactly but is estimated to be more than offset by the future productivity and capability gains of the employees.

22. All firms are required to complete an assessment return in order that their levy liability can be calculated. It is estimated that this is a small direct cost amounting to no more an hour for a small firm up to 8 hours for the largest, at £50 per hour. Firms eligible to claim grants are required to complete claim forms and it is estimated that this cost amounts to 0.5% per £1000 claimed.

23. Compliance costs vary from company to company, dependent on its payroll and use of labour-only workers. For the purpose of the costing examples that follow, we have assumed that it takes an hour on average at £50 p/h to complete the forms.

24. The costing examples on the following two pages include costs and benefits of training services provided and grants awarded. Due to the proposed changes in operations at the ECITB including the re-introduction of the off-site levy it is not appropriate to rely entirely on historical data in the following examples. The historical data has been used to give best estimates for future outcomes.

**Example 1**: A large engineering construction contractor. The company has over 2,000 site employees and over 600 head office staff. The levy payment was 1.15% of total payroll.

The company gets most value from the learners it has on site placements and the work that they do. The company gets over £300,000 in grants for training employees.

| | £ | £ |
|---|---|---|
| Completion of assessment returns | 400 | |
| Processing of levy bill | 50 | |
| Levy Payment | 663,122 | |
| Cost of claiming grants | 1,518 | |
| | | |
| **Less** | | |
| Grants | | 303,606 |
| NASEC- Learner Productivity | | 577,200 |
| NASEC- 7 learners recruited | | 280,000 |
| Free Training | | 38,676 |
| | | |
| Net Cost/ (Benefit) | | (534,392) |

**Example 2**: A contractor in the steel erection industry. Have just over 180 employees on-site. The levy payment was 1.5% of total payroll.

The company in this example pays a levy of over £40,000 in return it claims nothing in grants. The company gets real value from the NASEC learners.

| | £ | £ |
|---|---|---|
| Completion of assessment returns | 150 | |
| Processing of levy bill | 50 | |
| Levy Payment | 41,924 | |
| Cost of claiming grants | 0 | |
| | | |
| **Less** | | |
| Grants | | 0 |
| NASEC- Learner Productivity | | 137,400 |
| NASEC- 7 learners recruited | | 120,000 |
| Free Training | | 51,663 |
| | | |
| Net Cost/ (Benefit) | | (266,939) |

**Example 3**: A process contractor. The company has a total of 295 employees working on-site or in the head office. The levy payment was 0.89% of total payroll.

| | £ | £ |
|---|---|---|
| Completion of assessment returns | 250 | |
| Processing of levy bill | 50 | |
| Levy Payment | 50,073 | |
| Cost of claiming grants | 39 | |
| | | |
| **Less** | | |
| Grants | | 7,700 |
| NASEC- Learner Productivity | | |
| NASEC- 7 learners recruited | | |
| Free Training | | |
| | | |
| Net Cost/ (Benefit) | | 42,752 |

**Example 4**: A contractor involved in pipework, steelwork and tanks. This company has around 70 employees and did not use any ECITB services. The levy payment was 0.32% of total payroll.

| | £ | £ |
|---|---|---|
| Completion of assessment returns | 50 | |
| Processing of levy bill | 50 | |
| Levy Payment | 4,672 | |
| Cost of claiming grants | 0 | |
| | | |
| **Less** | | |
| Grants | | 0 |
| NASEC- Learner Productivity | | 0 |
| NASEC- 7 learners recruited | | 0 |
| Free Training | | 0 |
| | | |
| Net Cost/ (Benefit) | | 4,772 |

**Total Compliance Costs**

25. The Engineering Construction Industry costs and benefits as a whole is shown below. The example takes into account the changed structure of the organisation where resources are primarily focussed on NASEC and NSDS training schemes, together with Supervisory training. It takes into account the restoration of levy for Off-Site and the anticipated training benefits for that sector. The anticipated activities in 2006 will result in the following:

| | £ | £ |
|---|---|---|
| Completion of assessment returns | 58,000 | |
| Processing of levy bill (200 @ £50) | 10,000 | |
| Levy Payment | 10,000,000 | |
| Cost of claiming grants | 20,000 | |
| **Less** | | |
| Grants | | 4,000,000 |
| NASEC- Learner Productivity | | 2,500,000 |
| NASEC- learners recruited | | 6,000,000 |
| Certification and Quality Assurance | | 650,000 |
| Career Attraction | | 150,000 |
| Free Training | | 750,000 |
| Tax Relief | | 2,700,000 |
| Net Cost/ (Benefit) | | (6,622,000) |

N.B. The calculation above does not include estimated external income for 2006 (£2.5m). Also not included in the calculation is the benefit of companies being able to recruit from a skilled labour pool.

## Consultation with Small Business: "The Litmus Test"

26. In consultation with the industry (see Paras 2 and 31) provision has been made for the exemption of small firms from payment of the levy as follows:

- Site establishments whose combined payroll / net labour-only payments are £275,000 or less are not liable to pay the levy.

- Off Site establishments whose combined payroll / net labour-only payments are £1 million or less are not liable to pay the levy.

27. Around 48% of site establishments and 78% of Off Site establishments are expected to fall below the exclusion threshold and thus will not be liable to pay the respective levy.

**Other Costs**

28. No other costs have been identified. Neither option has a cost for the Department or the Government.

**Results of Consultation**

29. The estimates are based wherever possible on statistical information published by the ECITB. Where this was not available assumptions have been obtained from the Board.

30. The ECITB and its statutory levy system has been retained at the express wish of employers in the sector and their representative organisations. The levy provisions contained within this Order were proposed by the Board and have the support of the industry as required by the Industrial Training Act 1982. Evidence of that support has been obtained from the representative employer organisations and the ECITB Customer Satisfaction Survey 2002. All companies that do not declare a membership to an employer body have been consulted directly on the proposals.

**Summary and Recommendations**

31. On the basis of expected costs and benefits, option 2 is the preferred option.

32. The conclusion is also sensitive to the belief that employers are best-placed to decide which training arrangements best suit their needs. As required by the governing legislation for Industrial Training Boards, they have been consulted on and support the levy proposals in question.

**Enforcement, Sanctions, Monitoring and Review**

33. As a Non-Departmental Public Body the ECITB is subject to a periodic review (at least every five years) of its performance and the continuing need for its existence. The next review is scheduled to take place in early 2008.

34. An ITB's levy proposals are normally submitted to Ministers on an annual basis. This Order gives effect solely to the Board's proposals for a levy in 2006.

**Appendix A**

**How does Government satisfy itself that ECITB represents good value for money?**

- Quinquennial Review – the most recent was completed 2003 and augmented by an independent strategic review by the ECITB.
- ECITB regional committees are made up of industry and trade union representatives and other stakeholders.
- Customer Satisfaction Survey – see below.
- The ECITB sets and awards qualifications approved by the QCA and SQA.
- Government Assessors attend ECITB Board meetings.

**The ECITB can demonstrate the value added in the following areas:**

1) Image and recruitment

The ECITB runs a modern apprenticeship scheme with completion rates of around 65%. This delivers highly skilled new entrants to the industry each year.

It has been calculated that for private contractors it would cost up to £60 - 80,000 to put a learner through the 3-4 year Modern Apprenticeship. The ECITB can do it for around half this cost due to the benefits of economies of scale and the payment of an allowance rather than wages.

2) Qualifying the workforce

The ECITB runs a Safety Passport scheme to ensure that employees working on site have had the necessary safety training.

The ECITB is currently engaged in the Assuring Competence in Engineering Construction (ACE) initiative. This scheme plans to qualify the entire 20,000 engineering construction on-site work force to S/NVQ level 3 standards by the end of 2008. The project has secured support of almost £20 million from external funding over the life of the initiative.

3) Improving performance

The ECITB has recently undertaken an independent strategic review. Following this review the ECITB has re-organised to ensure more value is delivered to its customers. This includes a focused regional approach to engaging levy payers. Employer engagement in the forums is increasing, giving greater, more effective dialogue and needs analysis.

4) Customer Satisfaction 2004

- The survey in 2004 shows that overall satisfaction has improved from the survey in 2002 by an average of 14% points.

5) Financial Return to the Industry

The financial return to the industry was recently calculated to be £1.40 (£1.34 in 2002) returned to industry for each £1 paid in levy. This calculation does not include external funds raised or benefit of tax relief for in-scope customers.

**Appendix B**

## Proposals for and Exemptions from Levy

Below are two extracts from the proposed levy order setting out the details of the levy and defining specifying the two categories of employers who are exempt from the payment of levy.

**Imposition of levy**

**4.**—(1) The levy to be imposed by the Board on employers in respect of the levy period shall be assessed in accordance with the provisions of this article.

(2) The levy shall be assessed by the Board separately in respect of each leviable establishment of an employer, but in agreement with the employer one assessment may be made in respect of any number of such establishments, in which case those establishments shall be treated for the purposes of that assessment as constituting one establishment.

(3) Subject to the exemptions in article 5 the amount to be assessed by way of levy in respect of each leviable establishment shall be the aggregate of —

1.5 per cent. of (A + B – C) (disregarding any negative total) and

0.18 per cent. of (D + E – F) (disregarding any negative total), where —

| | |
|---|---|
| A | is the total emoluments of all the persons who are site employees employed by the employer in the base period at or from the establishment. |
| B | is the sum of all payments (including payments for the incidental use of tools) made by the employer during the base period under labour-only agreements for services rendered to him by site employees, |
| C | is the sum of all payments (including payments for the incidental use of tools) received by the employer during the base period under labour-only agreements for services rendered by him or on his behalf by site employees, |
| D | is the total emoluments of all the persons who are off site employees employed by the employer in the base period at or from the establishment, |
| E | is the sum of all payments (including payments for the incidental use of tools) made by the employer during the base period under labour-only agreements for services rendered to him by off site employees, |
| F | is the sum of all payments (including payments for the incidental use of tools) received by the employer during the base period under labour-only agreements for services rendered by him or on his behalf by off-site employees. |

**Exemptions from the levy**

**5.**—(1) An employer in whose case the aggregate of—

(a) the total emoluments of all the persons who are site employees employed by the employer at or from the leviable establishments of the employer in the base period; and

(b) the sum of all payments (including payments for the incidental use of tools) made by the employer during the base period under labour-only agreements for services rendered to him by site employees,

was less than £275,000, shall be exempt from that part of the levy which is 1.5 per cent. of (A+B-C) referred to in article 4(3) above.

(2) An employer in whose case the aggregate of —

(a) the total emoluments of all the persons who are off-site employees employed by the employer at or from leviable establishments of the employer in the base period; and

(b) the sum of all payments (including payments for the incidental use of tools) made by the employer during the base period under labour-only agreements for services rendered to him by off-site employees,

was less than £1,000,000, shall be exempt from that part of the levy which is 0.18 per cent. of (D+E-F) referred to in article 4(3) above.

(3) A charity within the meaning of section 506 of the Income and Corporation Taxes Act 1988(**1**) shall be exempt from the levy.

(**1**) 1988 c.1