EXPLANATORY MEMORANDUM TO

THE PENSION PROTECTION FUND (PRESCRIBED PAYMENTS AND INVESTMENT COSTS - AMENDMENT) REGULATIONS 2011

2011 No. 671

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

2. Purpose of the instrument

These Regulations make provision for the Board of the Pension Protection Fund ("the Board") to make payments from the Pension Protection Fund ("the PPF") to meet certain expenditure which is currently met by the Board's administration budget. The expenditure to be charged to the PPF includes those costs resulting from the Board's investment and recoveries functions, and expenditure related to the transfer of UK property, rights and liabilities to the Board.

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

None

4. Legislative Context

4.1 The Pensions Act 2004 ("the Act") established the PPF which commenced operations from 6 April 2005. The PPF was set up to provide compensation to members of eligible defined benefit occupational pension schemes, where the employer has a qualifying insolvency event, there is no possibility of a scheme rescue and there are insufficient assets in the scheme to pay benefits at PPF compensation levels. An insolvency event is typically when an employer does not have sufficient funds to pay its debts, buy goods, etc.

4.2 The Act also established the Board, which is a corporate body, in order to hold and manage the PPF, and created two distinct strands of income:

- The **administration levy,** which was established to pay for the running costs of the Board (the running costs are met by Grant-in-Aid from the Department and recouped from schemes through the administration levy).

- The **pension protection levy** which along with funds from schemes that transfer into the PPF and investment income, was established to contribute to the cost of paying pension compensation to members.

4.3 Section 173 of the Act lists the things that can be charged to the PPF rather than the Board's administration budget (funded by the administration levy). These Regulations add further things to that list.

5. Territorial Extent and Application

This instrument applies to the United Kingdom.

6. European Convention on Human Rights

As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

7. Policy background

What is being done and why

7.1 These Regulations provide for the following four sets of costs, which are currently met from the Board's administration budget, to be paid out of the PPF:

(i) Costs incurred by the Board in relation to the prudent investment of the PPF and in relation to the prudent investment by schemes which are being assessed to see whether they can enter the PPF. This includes, for example, costs arising from the management, modelling and monitoring of the PPF's financial risks relating to its investments and appointment of its investment fund managers; and expenditure that relates to the preparation and management of the PPF's assets (which are described in its Statement of Investment Principles). It also includes costs arising from the transfer of assets to the Board from schemes for which the Board is required to take responsibility.

(ii) Expenditure which is incurred for the purpose of exercising the Board's rights as a creditor to recover debts or its functions under the Act that relate to those rights. This includes, for example, costs of obtaining advice from legal advisers, insolvency practitioners and others where the Board is involved in negotiating or enforcing its rights in recovering debts both in UK and overseas jurisdictions.

(iii) Expenditure incurred in relation to the transfer of UK property, rights and liabilities to the Board. The Act already enables certain costs connected with the transfer of foreign property, rights and liabilities to be borne by the PPF, these Regulations provide similar treatment for UK property.

(iv) Expenditure that is incidental or conducive to the Board's functions but only insofar as it relates to those costs that may be met from the PPF (under section 173 of the Act and these Regulations).

7.2 The Government consider it appropriate to make these changes for the

following policy reasons –

- If the PPF was a pension scheme the activities that give rise to these costs would be charged to the scheme rather than the sponsoring employer. Charging these costs to the PPF is equivalent to charging them to a scheme.

- Some of these costs are generated by PPF eligible pension schemes that are more likely to enter the PPF – paying these costs from the administration levy puts an undue burden on well-run schemes that are unlikely to enter the PPF. Raising funds to cover these costs through the pension protection levy would mean that schemes that are more likely to enter the PPF pay a proportionate share of these compensation administration costs. This is fairer to eligible pension schemes.

- In the long-term the Board will move more towards a large scale fund management and finance operation – in this context it is considered appropriate for the PPF to bear the costs arising from the investment management function (including the cost of managing and monitoring the PPF's financial risks and its fund managers).

- Including these costs in the administration levy potentially gives an inaccurate view of the costs of running these functions of the Board – making this change will allow closer scrutiny of the Board's overhead costs which remain in the administration levy.

7.3 The change in the funding source from the administration levy to the PPF will mean that the Board's administration budget will be lower from 1 April 2011. This will be taken into account when administration levy rates are calculated for future years.

Consolidation

7.4 Regulation 3 revokes the Pension Protection Fund (Payments to meet Investment Costs) Regulations 2005 ("the 2005 Regulations"). The new regulation 3 covers everything that is provided for by the 2005 Regulations. Therefore there is no need to retain the 2005 Regulations, and revoking them simplifies the PPF legislation by reducing the number of Statutory Instruments.

7.5 Informal consolidation of these Regulations will be included in due course in the Department's "the law relating to Social Security" (the Blue Volumes) which are available at no cost to the public on the internet at: http://www.dwp.gov.uk/publications/specialist-guides/law-volumes/the-law-relating-to-social-security/

8. Consultation outcome

8.1 The Department consulted on these Regulations from 13 December 2010 – 4 February 2011. The Government Code of Practice on Consultation

recommends a minimum 12-week consultation period for public consultations, unless there are good reasons for a limited consultation period. In this case, the issue was of a specialist nature that was likely to be of interest to a limited number of the Department's and the Board's pensions stakeholders, and the length of the consultation struck a reasonable balance between time for respondents to contribute and the desirability of bringing these Regulations into force for the 2011/12 financial year. Taking account of these factors the Minister for Pensions decided that a limited consultation period was appropriate. The consultation document and the Government's response to the consultation is available on the Department's internet site at - http://www.dwp.gov.uk/consultations/2010/ppf-regs-2011-consultation.shtml

8.2 A list of those consulted is at Annex A to this memorandum. The draft Regulations were also available on the Department's internet site. The Department received five responses to the consultation: two respondents provided comments, and three respondents had no comments to make.

8.3 Of those who commented, one respondent commented on the transparency of the sums which are now to be paid from the PPF. The Government and the Board acknowledge this concern. The Board has therefore given a commitment that the costs paid out of the PPF will be disclosed in its Annual Report and Accounts for 2011/12 and onwards. Parliament will have oversight of the published PPF Annual Report and Accounts, and the PPF chief executive will remain accountable to the Department's Permanent Secretary and to the Secretary of State for the PPF expenditure. The Board has also confirmed that following any changes it will consider and where appropriate revise its reporting procedures to ensure transparency for stakeholders.

8.4 One respondent felt that the Regulations might overlook one or more relevant provisions. This respondent also suggested that a more description-based structure would mitigate this risk and avoid unintended consequences. The Government carefully considered this response and felt, on balance, that including the statutory references was most appropriate. However the Board's investment and recovery functions are of necessity wide-ranging, and it is possible that other related activities might arise that should be covered. In response to this concern Regulations have been modified to provide that where the Board incurs expenditure in relation to the exercise of any of its statutory functions under the Act connected with its investment or recovery activities, those costs are to be paid out of the PPF. The Regulations have also been modified to include some costs on investments made by schemes and recoveries of debts owed to schemes as such costs can have a bearing on the Board's investment and recoveries costs relating to the PPF.

9. Guidance

No guidance is being issued on these Regulations since they are largely based on existing legislation. The Department will have copies of the Regulations and be in a position to explain them to members of the public.

10. Impact

10.1 The changes in these Regulations will have no impact on the overall costs to business and civil society organisations

10.2 The impact on the public sector is negligible.

10.3 A full impact assessment has not been prepared for this instrument

11. Regulating small businesses

The changes in these Regulations will have no impact on the overall costs to small business.

12. Monitoring & review

As with all PPF legislation the Department will keep this under review in light of the Board's operational experience. The effectiveness of these changes will also be monitored through contacts with the pensions industry and member representative organisations.

13 Contact

Any queries regarding these instruments are to be directed to Rob O'Carroll at the Department for Work and Pensions Tel: 020 7449 7426 or e-mail: Rob.O'Carroll@dwp.gsi.gov.uk

Annex A: List of organisations consulted

Age Concern /Help the Aged
Actuarial Profession
Association of British Insurers
Association of Chartered Certified Accountants
Association of Consulting Actuaries
Association of Corporate Trustees
Association of District Judges
Association of Independent Financial Advisers
Association of Pension Lawyers
Board for Actuarial Standards
British Chambers of Commerce
Better Regulation Executive
Carers UK
Confederation of British Industry
Consumers' Association
Department for Business, Innovation & Skills
Department for Social Development (Northern Ireland)
Engineering Employers' Federation
Equality and Human Rights Commission (EHRC)
Eversheds
Faculty & Institute of Actuaries
Family Justice Council - Money and Property sub committee
Family Proceedings Rule Committee
Federation of Small Businesses
Financial Ombudsman Service
Financial Services Authority
Government Actuary's Department
HM Revenue & Customs
HM Treasury
Hammonds LLP
Her Majesty's Courts Service (HMCS)
Hewitt Associates
Independent Pensions Research Group
Industry Wide Pension Schemes Group
Institute of Chartered Accountants in England and Wales (ICAEW)
Institute of Chartered Accountants in Scotland
Institute of Directors
Institute of Payroll and Pensions Management
Investment and Life Assurance Group
Investment Management Association
Joint Working Group
Law Society
Law Society of Scotland
Ministry of Justice
National Association of Pension Funds

National Consumers Council
National Pensioners Convention
Northern Ireland Office
Office of Fair Trading
Pensions Management Institute
Pensions Ombudsman
Pensions Policy Institute
Scottish Parliament
Scotland Office
Society of Pension Consultants
The Pension Protection Fund
The Pensions Advisory Service
The Pensions Regulator
Towers Watson
Trades Union Congress
Welsh Assembly
Wales Office
Which?