EXPLANATORY MEMORANDUM TO

THE PENSION PROTECTION FUND (RISK-BASED PENSION PROTECTION LEVY) REGULATIONS 2006

2006 No. 672

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

2. Description

2.1 These regulations provide for the Pension Protection Fund (PPF) to take into account additional risk factors when calculating the risk based levy.

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

3.1 There are no matters of special interest.

4. Legislative Background

4.1 Section 175 of the Pensions Act 2004 requires the Board of the PPF to charge an annual levy to eligible schemes, composed of two parts: a scheme-based levy and a risk-based levy. The scheme based levy is calculated by reference to the amount of scheme liabilities. The risk based levy is calculated by reference to scheme underfunding and the likelihood of employer insolvency.

4.2 175(3)(b) allows for the provision of extra risk factors that the Board of the Pension Protection Fund may wish to take into account, if it considers appropriate, when calculating the risk-based levy.

4.3 These regulations provide that the Board may take account of the nature of, and any risks associated with, arrangements which reduce the risk of compensation being payable from the PPF. The arrangements referred to in these regulations may include, for example, a letter of credit or guarantee from a bank that releases funds on the event of insolvency or a guarantee from a parent Company . Parental guarantees are usually provided directly to the relevant trustees and the employer is often the global parent of the company(s) participating in the UK defined benefit pension scheme.

4.4 The effect of making provision for the inclusion of nature of and any risks associated with these arrangements is to reduce the net risk posed to the PPF by eligible schemes, and therefore require a lower levy for schemes and a lower total levy burden on industry overall. These

arrangements would not otherwise be taken into account when assessing liabilities/assets.

4.5 It was decided to make specific provision to add to the risk factors in relation to any risks associated with arrangements which reduce the risk of compensation being payable from the PPF after public consultation by the PPF into the calculation of the Pension Protection Levy showed that industry was strongly in favour of this approach.

4.6 These regulations use the power under section 175(3)(b) to provide for the inclusion of risk factors in relation to risks associated with arrangements which reduce the risk of compensation being payable from the PPF as a general group in the risk-based levy calculation.

5. Extent

5.1 This instrument applies to Great Britain.

6. European Convention on Human Rights

The Minister of State for Pensions Reform, Stephen Timms, has made the following statement regarding Human Rights:

In my view the provisions of The Pension Protection Fund (Risk-based Pension Protection Levy) Regulations 2006 are compatible with the Convention rights.

7. Policy background

7.1 The Pension Protection Fund has been set up to provide a statutory form of compensation for members of defined benefit occupational pension schemes, where the employer has a qualifying insolvent event and the assets in the scheme would not provide pension at Pension Protection Fund compensation levels.

7.2 The PPF is funded through an annual levy charged to all qualifying defined benefit occupational pension schemes. In addition when the PPF assumes responsibility for a scheme it assumes all assets of the scheme.

7.3 These Regulations are made before the expiry of the period of six months beginning with the coming into force of the provisions of the Act by virtue of which the Regulations are made, the requirement for the Secretary of State to consult such persons as he considers appropriate does not apply. However, these regulations have been drafted in response to consultation undertaken by the Pension Protection Fund relating to the calculation of the Pension Protection Levies. Consultation responses strongly supported the addition of further risk factors relating to the risks associated with arrangements

which reduce the risk of compensation being payable from the PPF within the levies calculation.

7.4 As these regulations are affirmative, they will be debated in both Houses.

8. Impact

8.1 A Regulatory Impact Assessment has not been prepared for this instrument as it has no impact on business, charities or voluntary bodies.

8.2 There is no impact on the public sector.

9. Contact

Clare Judkins at the Department for Work and Pensions Tel: 0207 712 2734 or e-mail: Clare.Judkins@dwp.gsi.gov.uk can answer any queries regarding the instrument.