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## **Funded to Fail?**

The Pension Protection Fund has been established to provide an insurance for pension schemes in deficit where sponsoring employers become insolvent. But in a submission to the PPF Frank Field MP questions whether the method chosen by the Government to finance the levy will have the paradoxical effect of increasing the schemes having to draw upon the Funds, thereby bringing the Fund itself into question.

The consultations on the new scheme ends today.

The proposal for a British Pension Protection Fund was first made by Frank Field in a Private Member's Bill in 2002. The Government blocked the bill only to introduce its own measure. The Government's proposals follow the original bill in all but two respects – both crucial to the long-term wellbeing of pensioners.

- The Government chose, prior to establishing the Pension Protection Fund, to present taxpayers with a £400m bill to cover part of the pensions already lost by people who were members of wound-up schemes that were under funded or where the sponsoring employer went insolvent. A Financial Assistance Scheme was enacted but the Government has so far refused to place a levy on the huge unclaimed assets of banks and building societies to finance an adequate lifeboat operation – as was suggested in the original bill –

even though it has admitted that the £400m taxpayers' contributions will prove inadequate.

- As the proposed Pension Protection Fund levy is being placed on scheme funds the Government has had to invent a highly complicated formula to take account of a pension fund's deficit, as well as the possible long-term solvency prospects of the sponsoring firm. This move contradicts the Government's avowed intention of simplifying pension administration law and administration.

In the original bill Frank Field proposed a levy on pensioners and employees of company schemes as these are the groups who have most interest in ensuring that their pensions are paid.

The submission proposes a reversion to the original proposal with

- £12 a year levy on current occupational pensioners
- £50 a year levy on active members.

The full submission is attached.

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*Sara Protheroe*

Thank you for inviting comments on the PPF levy. The consultation is a model of how best to develop policy and this submission welcomes the opportunity to propose a total rethink of the basis on which the new PPF levy is to be made.

At the end of 2002 I introduced the **Pensions (Winding-up) Bill**. While the Government blocked the passage of the Bill, it carried out its main proposals in all but two respects in its own **Pensions Act 2004**. Unfortunately these two areas are fundamental and concern the funding of the Financial Assistance Scheme as well as the Pension Protection Fund.

Instead of placing a levy on the unclaimed assets of banks and building societies, the Government has placed a burden of £400 million on taxpayers to finance the Financial Assistance Scheme. Even the Government admits that this sum is inadequate to finance the scheme over the longer term. The promise has been that the long term financing of the FAS will form part of the next public expenditure review. The delay by a year of this review gives the Government the opportunity of looking again at placing a levy on unclaimed assets.

There are two other issues upon which I would like to comment. The first is the changing of the eligibility rules of the PPF and second is the basis of the funding of the scheme.

Initially ministers were adamant that only schemes where the levy had been paid could be eligible for payments from the PPF. By ruling Turner & Newall eligible without any payments the Government has set a precedent that puts at risk the financial viability of the whole scheme. The smallest reported shortfall on this pension fund is put at £125 million.



With the rules being so arbitrarily changed it is not surprising that the yearly sum necessary for the successful running of the PPF has already risen from £300 to £600 million.

Confidence is crucial in any insurance scheme – those who are paying premiums need to know the rules governing the calculation of premiums and conditions on which the scheme will make payments. The Government may have thought it a smart move to change the rules so early on in the scheme's life, but the long-term consequences of playing fast and loose with the rules undermines the sense of certainty and security which the PPF was to bring to an area of policy sadly lacking in each of these two attributes.

The Government is further putting the scheme at risk in two additional respects. It is placing the insurance levy on the schemes themselves when it should be levied directly on employees. It is they, not employers, who have the greatest interest in seeing an insurance scheme operating in case their employer ceases trading when their pension fund is in deficit. By placing the levy on schemes the Government is forced into a mine field of devising how to calibrate the levy according to the deficit in a scheme as well as the employer's own longer term viability.

The result of taxing the wrong group is a levy which takes into account the risk of under funding, the risk of insolvency as well as the different structures of the schemes. Here is the basis of not only an enormously complicated formula but an amount of untold additional work for pensions schemes themselves. How can the Government keep a straight face? It introduces a massively complicated levy system and yet assures the industry that its overriding objective is to move towards a simpler legal and administrative structure for pension schemes?

The Government should go back to the drawing board and pick up on how the original **Pensions (Winding-up) Bill** proposed to fund the insurance scheme. In the debate surrounding the Bill I made plain that the levy should be on employees and that the scheme should be kept dead simple.

There are three groups of scheme members – those drawing pensions, those with deferred benefits, and active members who are still working for their employer even where the pension scheme has been closed to new accruals. As most schemes do not know the whereabouts of



scheme has been closed to new accruals. As most schemes do not know the whereabouts of many of their deferred pensioners this group will have to be initially excluded from the levy. Often the deferred benefits are small and some owners of such entitlements are likely to be active members of another scheme and would therefore pay the levy anyway.

I believe the levy should be placed on members of both public and private sector schemes. It is inconceivable that any public scheme will be allowed to go bankrupt. All taxpayers stand behind public sector pension guarantees and already pay by increased council tax and other taxation to meet their deficits. It is only fair that, in return for this guarantee, members of public sector schemes should help finance a similar guarantee to their colleagues in private company schemes.

As pensioners have an equal interest in their scheme's survival I suggest that a pound a month be levied on each of the 9.8 million occupation scheme members currently drawing a pension. Pensions are paid monthly and the schemes should be given the power to deduct one pound a month of each pension which will thereby raise £120 million a year in insurance payments.

Of the active 9 million members of occupational schemes I suggest that they pay a levy of £50 a year, or a little less than a pound a week, giving an additional total of £500 million towards financing the PPF.

These particular sums should be open for discussion. The levy, for example, could be fine-tuned to exempt pensions below a certain threshold. Likewise the poorest members of schemes could be exempt by raising the levy to £75 a year for all contributors earning over, say, £50,000 a year. The aim of this submission is not to cast in stone any particular sum but to establish the financial approach upon which the PPF levy should be funded.

It is now too late for this reform to come into force before the start of the PPF. But the Government could make its intention known that the employer levy will last a single year only and that the switch to an employee-based levy will come into play one year after the opening of the PPF. A years delay will also give time to work out how best to levy deferred members.



The Government has one last chance to change the funding of the PPF. What is crucial is to establish a means of funding which all scheme members can easily understand, which places the levy on those individuals that have the greatest interest in a guarantee, which puts a minimum administrative cost on schemes, and which finances the PPF in a way which does not endanger the long term financial viability of those companies providing occupational pensions.

A handwritten signature in black ink, appearing to read 'Nick Hargrave'.