Department for Work & Pensions

Review of the Fraud Compensation Levy ceiling 2021

Government response

March 2022

Introduction

1. This consultation ran from 1 November to 10 December 2021. The consultation document can be viewed at:

   Review of the Fraud Compensation Levy ceiling (publishing.service.gov.uk)

2. The consultation sought views on a proposal for change to the Fraud Compensation Levy (FCL) ceiling from the levy year 2022/23.

3. Annex A lists the 11 respondents to the consultation, and the Government is grateful to them for providing their comments and advice on the proposals.

4. This document notes why it is considered necessary to increase the FCL ceiling and explains the purpose of the proposal that the Government brought forward. It provides a summary of the responses received to the consultation and the Government's responses to the comments made and advises that, following consideration of these comments, the Government decided to proceed with the proposal as set out in the consultation document.

5. Accordingly, regulations (The Occupational and Personal Pension Schemes (Fraud Compensation Levy) (Amendment) Regulations 2022 (S.I. 2022 No. 259), a copy of which is at Annex B, have been made and laid in both Houses of Parliament. A commentary on the regulations is at paragraphs 15-18 below.

Background

6. The Pension Protection Fund (PPF) was established by the Pensions Act 2004 ("the Act") in order to protect members of eligible defined benefit occupational pension schemes (and the defined benefit element of hybrid schemes) by paying compensation where an employer has a qualifying insolvency event and there are insufficient assets in the scheme to pay benefits at PPF compensation levels.

7. The PPF's responsibilities under the Act include the operation of the Fraud Compensation Fund (FCF). The FCF provides compensation to eligible occupational pension schemes where there has been scheme asset reduction, attributable to an offence involving dishonesty, and where the employer has become insolvent or is unlikely to continue as a going concern.

8. The FCL recovers from eligible occupational pension schemes the costs of compensation paid from the FCF. In November 2020, the High Court, in The Board of the PPF v Dalriada Trustees Ltd[1], clarified that pension liberation

[1] [2020] EWHC 2960 (Ch) Case No: PE-2019-000016

schemes[2], if they satisfied specified criteria, were eligible to make a claim on the FCF.

9. The consultation document explained that there are insufficient assets within the FCF to meet claims arising from that judgment in the short term. The Compensation (London Capital & Finance and Fraud Compensation Fund) Act 2021 received Royal Assent on 20 October 2021. This Act, in so far as it affects the FCF, provides the Secretary of State with a power to make a loan to the Board of the PPF. The PPF, acting in its capacity as manager of the FCF, will use the loan, along with any assets in the FCF, to meet these potential claims. The loan is expected to cover 126 schemes and total approximately £250m over the period to 2025.

10. Amendments to the Occupational Pension Schemes (Fraud Compensation Levy) Regulations 2006[3], as amended, are required to raise the FCL ceiling.

11. Regulation 3(3)(b) of the FCL regulations specifies the maximum charge (currently £0.75 per member) that may be imposed on eligible pension schemes. In the consultation document, the Government explained its proposal to increase this ceiling, so that the FCL rate for such schemes can be set by the PPF at an appropriate level.

12. Regulation 3A of the FCL regulations, inserted by the Occupational Pension Schemes (Master Trust) Regulations 2018[4], was intended to specify a lower maximum charge (currently £0.30 per member) applicable to Master Trusts. The Government explained its proposal to increase this amount, so that the FCL rate for Master Trusts can be set by the PPF at an appropriate level.

13. The proposed amendments detailed above will allow the PPF to set the FCL at levels that will enable it to repay the loan the Government intends to provide by 2030/31. The repayment schedule specified by the Government incorporates this requirement.

14. As advised in the consultation document, the FCL levy ceiling under the proposal above would provide for levy rates to be set by the PPF not exceeding £0.65 per member for Master Trusts and £1.80 per member for other eligible occupational schemes.

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[2] Pension liberation scheme fraud involves members being persuaded to transfer their pension savings from legitimate schemes to fraudulent schemes with promises of high investment returns or access to a loan from their pension scheme before age 55 without incurring a tax charge.

[3] S.I. 2006 No. 558

[4] S.I. 2018 No. 1030

The FCL amendment regulations 2022

Regulations 1 & 2 – Citation and commencement

15. Regulation 1 is a general regulation which gives the title of the regulations and specifies the date on which the regulations are proposed to come into force. They are proposed to come into force on 1 April 2022.
16. Regulation 2 specifies that the regulations will extend to England and Wales and Scotland.

Regulation 3 – Amendment of the 2006 Regulations

17. This regulation amends regulation 3(3)(b) of the Occupational and Personal Pension Schemes (Fraud Compensation Levy) Regulations 2006 in order to increase the FCL ceiling to £1.80 per member for occupational pension schemes other than Master Trusts. It further provides, in regulation 3(3)(b), that the FCL ceiling per member for Master Trust schemes which are authorised under the Pensions Act 2017 shall be increased to £0.65.

Regulation 4 – Amendment of the 2018 Regulations

18. This regulation amends the Occupational and Personal Pension Schemes (Master Trusts) Regulations 2018 in order to remove regulation 23(2)(c). Regulation 23(2)(c) is no longer required because Regulation 3(3)(b), as noted above, specifies the FCL ceiling applicable to Master Trusts.

Summary of the consultation responses received

19. The Government sought comments on the proposal set out in the consultation document and asked 3 questions:

- **Question 1** - do you support the proposal? Please indicate why you support, or do not support, the proposal.
- **Question 2 -** what is the impact to your scheme/business of raising the FCL under the proposal?
- **Question 3 -** how will your scheme respond to an increase in the FCL? (For example: would it be absorbed by the scheme, passed on to members or to employers?)

20. **11 responses** to the consultation were received. The most common themes that emerged in the responses to Question 1 were as follows:

- **10** respondents expressed support for the provision of compensation for pension schemes affected by fraudulent activity;

- **9** respondents did not express support for the funding proposal set out in the consultation document (increase the FCL ceiling to £0.65 per member for Master Trusts and £1.80 per member for other occupational pension schemes);

- **9** respondents suggested that the structure of the FCF and/or the FCL should be reviewed. Some suggested that such a review could also encompass the provision of compensation from other sources, such as the Financial Services Compensation Scheme (FSCS);

- **7** respondents suggested that the increase in the FCL ceiling should be delayed pending a review. Most favoured a delay of one year;

- **7** respondents queried the efforts that are made to secure restitution for schemes affected by fraud prior to the payment of compensation from the FCF.

A more detailed summary of the responses is provided below.

21. 10 respondents expressed support for the provision of compensation for pension schemes affected by fraudulent activity. In this context, some underlined the importance of such compensation in maintaining full confidence in the UK pensions system, and observed that failing to provide compensation following losses due to fraud could severely erode confidence and trust in that system, in the Government and in regulators. The fact that the Dalriada judgment provided clarity on the eligibility of pension liberation schemes in respect of the FCF was viewed positively by some respondents and there was also some support for an appropriate increase in the FCL in order to help deliver better retirement outcomes. There was recognition on the part of some respondents that the pensions industry should meet the costs of protecting the sector, rather than spreading the costs to all taxpayers.

22. Though there was broad support for fraud compensation, 9 respondents did not support the Government's funding proposal as outlined above. Some respondents expressed the view that the pensions liberation claims brought into the scope of the FCF by the Dalriada judgment were not envisaged when the FCF was created and that "the goalposts have been moved". In the light of this factor in particular, 9 respondents argued that there should be a structural review of the FCF and/or the FCL, and gave examples of the issues they felt such a review could usefully address. The suggestions included provision for the FCL to take account of scheme assets and of the risk of a scheme becoming a charge on the FCF, charging for active members only and applying a banding approach based on scheme membership. Some respondents believed that such a review should encompass all the routes by which schemes and members can access compensation. 7 respondents believed that the proposed increase in the FCL ceiling should be suspended

pending the outcome of such a review. Most believed a delay of one year would be sufficient for this purpose.

23. The Government acknowledges the strength of feeling amongst respondents on the subject of a review. However, it is not persuaded that an urgent review is required. Its immediate priorities are to ensure the FCF is properly funded through the Government loan so that all legitimate claims can be met as promptly as possible, and to put in place robust arrangements for the recovery of that loan. Taxpayers in general, not all of whom benefit from the provision of occupational pensions, are entitled to expect the Government and the PPF to ensure that repayment of the loan begins without delay using existing FCL recovery machinery, and to recover the loan in full within a reasonable period. That is why the Government proposes an increase in the FCL ceiling from 2022/23, with full repayment of the loan anticipated by 2030/31. However, the Government will consider the possibility of a review over the medium term, alongside ongoing monitoring of the FCL ceiling.

24. 7 respondents raised the issue of restitution for schemes affected by fraud prior to the payment of compensation from the FCF. Some respondents underlined the potential relevance of compensation payable from the FSCS and its relationship to the FCF, arguing that the latter should be treated as the scheme of last resort. Others sought assurances that restitution is sought with appropriate energy before payment becomes possible and that the Government should, whenever it deems it appropriate, direct the PPF to achieve that outcome. It was also suggested that restitution could be sought from HMRC, on the basis that, it was alleged, the gateway allowing new pension schemes to register as such was insufficiently robust.

25. The relevant legislation provides for the payment of compensation only when all reasonable prospects for recovery have been exhausted[5]. The PPF works closely with trustees so their responsibilities in this area can be properly fulfilled. The PPF also liaises with the FSCS where it appears that regulated advice could be a factor and both bodies work together to ensure that their liaison arrangements are in good order and that any scope for improvement is identified. The relevant legislation does not specify that one compensation route should take priority over the other. This issue has not appeared a significant one to date but the position will be kept under review.

26. The PPF has been an independent statutory body since its inception. As Parliament intended the PPF to operate with a large measure of independence, it would not be appropriate, or indeed possible, for Ministers or departmental officials to interfere in the operation of the FCF.

27. It was suggested by some respondents that restitution should be sought from HMRC. HMRC does not authorise pension transfers and makes this clear to consumers and the industry, in guidance and through stakeholders. Pension schemes are responsible for carrying out due diligence on transfers to other

[5] Namely that further recoveries of value are unlikely to be obtained without disproportionate costs or within a reasonable timescale. This is an important consideration, not least because all recovery is ultimately funded by the occupational schemes that pay the FCL.

pension schemes and ensuring they comply with all legislative and regulatory requirements. In particular, HMRC guidance encourages consumers to seek professional advice before transferring their pension.

28. The PPF has advised the Government that it has received representations that FSCS compensation could be relevant where individuals were acting within a regulated environment, even if they were not themselves subject to regulation. The significance of this issue is as yet unclear, but the PPF will look to ensure that it has identified all occasions where FSCS compensation could be payable.

29. Some respondents called for greater clarity about the FCF and where detailed information about it can be obtained. A standalone website and Twitter account for the FCF exists at:

    www.fraudcompensationfund.co.uk
    (@FraudCompFund)

30. A factsheet for independent trustees has also been produced by the Pensions Ombudsman (TPO) about what they are expected to do where there are reasonable grounds for believing that a scheme asset reduction is attributable to an offence involving dishonesty. This is available on TPO's website at the following location:

    The Pensions Ombudsman and the Fraud Compensation Fund factsheet.pdf (pensions-ombudsman.org.uk)

31. As respondents will note, the factsheet also covers TPO's powers in this area. Furthermore, TPO has created a new 'Pensions Dishonesty Unit' to undertake investigations with the aim of directing trustees to repay monies wrongly obtained. Currently it is not clear how much money affected pension schemes would be able to recover from the fraudulent trustees if found liable and directed to repay by a TPO determination. The Pensions Dishonesty Unit is currently being piloted and this will allow evaluation of the initial cost and investment against monies recovered.

32. 5 respondents observed that it is unfair for Master Trusts to be required to contribute to the FCF when, these respondents argued, it is hard to see how this scheme type could benefit from the existence of fraud compensation. As the consultation document indicated, all occupational pension schemes, however well-governed, derive benefit from the existence of robust fraud compensation arrangements, which increase the level of consumer confidence in pension saving. These arrangements, underpinned by the FCL, also incentivise schemes to take thorough precautions against fraud and dishonesty, both within the scheme and when transferring members to other schemes.

33. 4 respondents acknowledged the importance and the usefulness of the lower FCL ceiling applicable to Master Trusts. However, 5 respondents took the view that the burden the proposals would create for Master Trusts would be too

great. It is axiomatic that reducing the burden for one group of levy payers will lead to a greater burden for others. The proposed FCL ceiling for Master Trusts is a little over a third that of other occupational schemes, and the Government believes that this would be an appropriate response to the particular circumstances of such schemes. In this context, the Government is mindful of the position of DB pension schemes, where nearly half are in deficit[6].

34. 4 respondents suggested that a banding system, such as that operating in the case of the General Levy[7] (GL) on pensions schemes, could be introduced as a means of lessening the burden of the FCL on larger schemes. However, the considerations that underlie the GL banding system do not apply to the FCL. The GL system is designed to recognise that supervisory costs do not rise in a linear and consistent way as scheme size increases. By contrast, the FCL is essentially a collective system designed to meet a burden created external to Government.

35. 3 respondents suggested that it is unfair for schemes that did not exist at the time when the pensions liberation fraud was perpetrated to share the burden of higher levy charges following the Dalriada judgment. It will always be possible for some occupational schemes to come into existence after matters eligible for compensation have come to light, particularly given the length of time that can elapse before the dishonesty issues are uncovered and investigated. Exempting such schemes from the FCL would add complexity to what is intended to be a levy system that is simple to understand and operate. It would also mean that a smaller number of occupational schemes would need to shoulder the cost burden of compensation relating to historic matters. Finally, it would mean that the robustness of the FCF, from which all schemes derive benefit, would be diminished by limiting its coverage. For these reasons, the Government does not plan to treat the date of a scheme's establishment as a factor in determining liability under the FCL.

36. 3 respondents argued that the levy calculation should exempt members with small pension pots. 3 other respondents sought an exemption for pots below £100, in recognition of the fact that it is the Government's intention to legislate to provide a minimum level, initially set at £100, before a flat fee element of a charging structure can be applied to such pots[8].

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[6] The PPF 7800 Index (November 2021). Available at: https://www.ppf.co.uk/sites/default/files/2021-12/PPF7800-30-November-2021-December-update.pdf

[7] The General Levy on pensions schemes recovers the core regulatory costs of The Pensions Regulator, the costs of the Pensions Ombudsman and the pensions-related costs of the Money and Pensions Service. The levy rate per member reduces as scheme size, by number of members, increases. There are seven levy rate bands, covering the smallest schemes to those with 500,000 members or more.

[8] Permitted Charges within Defined Contribution Pension Schemes – Government response (publishing.service.gov.uk)

37. Scheme members should be able to realise the best possible outcomes from their workplace pension savings. Consolidation of deferred small pots in the automatic market is a key part of this, but it will take time to develop and implement effective and durable solutions.

38. Following the industry working group meeting in 2020, chaired by DWP, the Government welcomes the pensions industry's progress, led by the PLSA and the ABI, in tackling the administrative challenges in this area and working towards pragmatic solutions. The group's report, published on 30 September 2021[9], shows the progress that is being made, including the member exchange feasibility study ahead of a potential pilot. Alongside this, the Government, with industry, is helping consumers with both keeping track of their various pensions, including small pots, and retirement planning through Pensions Dashboards and Simple Annual Benefit Statements – which may support member-led consolidation.

39. It should be noted that not all small pots necessarily remain small, in particular if they are active and through consolidation. It follows that a general exemption for small pots within the FCL would risk excluding occupational pensions that may benefit from protection and, in doing so, could diminish consumer confidence. The Government is committed to the protection of all pensions savers.

40. Furthermore, exempting small pots from the FCL might act as a disincentive for schemes to consolidate pension pots where this would otherwise be possible. The Government is keen to see progress by the pensions industry and providers continue in this area, working with regulators and the Government. For these reasons, the Government is not attracted to an exemption for small pots at this time.

41. 3 respondents raised issues about the future of the FCL, namely:

    i. the risk the proposal could lead to overfunding of the FCF;
    ii. whether the FCL ceiling will be reduced once the loan has been repaid;
    iii. whether a commitment can be given in respect of such a reduction; and
    iv. future consultation arrangements in respect of the FCL.

42. On i. above, once there are no longer any outstanding claims following the Dalriada judgment and the Government loan has been repaid, the PPF will avoid any overfunding of the FCF by charging the FCL at levels consistent with projected FCF liabilities, adjusting those levels over time as necessary.

[9]Small Pots Cross-Industry Co-Ordination Group: Update Report, September 2021: https://www.plsa.co.uk/Policy-and-Research/Document-library/Small-pots-cross-industry-co-ordination-group-update-report

43. On ii. above, it should be unnecessary to reset the FCL ceiling at a lower level as the possibility of overfunding will be addressed in the manner described above.

44. On iii. above, a commitment to reduce the ceiling once the loan has been repaid is unnecessary in the light of the information provided above.

45. On iv. above, primary legislation mandates a consultation exercise before any change in the FCL ceiling can be made.

46. 2 respondents suggested that the notice period given for the proposal is unreasonably short. The notice period is consistent with that given for other proposals for changes to DWP's pensions levies. Furthermore, the passage of The Compensation (London Capital & Finance and Fraud Compensation Fund) Act 2021 underlined the Government's commitment to fully compensate those schemes brought into the scope of the FCF by the Dalriada judgment. Given that it gave no indications to the contrary, it was reasonable to assume that the Government planned to use existing FCL recovery machinery to cover the resultant costs.

47. 2 respondents argued that a full impact assessment should have accompanied the proposal. An impact assessment is not required when changes to an existing statutory levy regime are being proposed. However, the Government sees the value in producing a summary of impacts where a significant proposal is made and has done so in this instance. Further information about better regulation is available at the following location:

    [Better regulation framework - GOV.UK (www.gov.uk)]

48. 1 respondent suggested that the proposed increase in the FCL ceiling should be made more gradual. This would carry a risk that the FCF would have insufficient funds to meet its liabilities as they fall due. The proposed FCL ceiling is consistent with the liabilities that have been projected.

49. In summary, the Government notes the broad support for the provision of fraud compensation that has been expressed, but recognises that there are strong views about the implementation date of the amendment to the FCL ceiling and the associated suggestion that a full review of the FCF should be mounted. Although the Government believes the increase in the FCL ceiling is pressing and has decided not to delay implementation, nor undertake an immediate review of the FCF/FCL, it will, as discussed in paragraph 23 above, monitor the position going forward. It may then decide that a full review is warranted. On restitution, the Government believes that the arrangements discussed in paragraphs 24-28 above are generally robust and that the information given may provide respondents with sufficient reassurance.

Impact

50. Questions 2 and 3 in the consultation document addressed the impact of an increase in the FCL ceiling and how schemes would respond to it.

51. There were 11 responses to these questions. A summary is as follows:

- 7 respondents indicated that costs would rise significantly. Although the increase in costs was not expected to have a destabilising effect, it could limit the scope to make improvements in scheme design and to enhance customer service. Some respondents added that the proposal needed to be set against other regulatory demands on the sector that were being imposed;
- 9 respondents said that increased levy costs would be absorbed by providers or employers, at least initially. However, 8 of these respondents said that the costs would ultimately be met by scheme members.

52. The Department has undertaken a detailed analysis of the responses noted above. It has also drawn upon a range of external and internal data held by the Department. It concludes that whilst the levy places a direct cost to business, it will provide an equal benefit to schemes and members affected by fraud. More widely, pension providers can also benefit from increased consumer confidence in the market created by the existence of the FCF. Indirectly, while many respondents indicated they would pass the additional cost to members, not all additional costs will be passed on owing to competitive pressures, and the scale of the increase will not be detrimental to retirement outcomes.

53. A more detailed summary of impacts is at Annex C.

Government response

54. Having considered the responses received, the Government decided to proceed with its proposal as set out in the consultation document without amendment.

Conclusion

55. The Government would like to thank all the respondents who have offered their views and advice in response to this consultation exercise. The regulations (The Occupational Pension Schemes (Fraud Compensation Levy) (Amendment) Regulations 2022 (S.I. 2022 No. 259)) which amend the 2006 Regulations to reflect the Government response above have been made and laid before both Houses of Parliament.

    These regulations are available on the UK Legislation website:

The Occupational Pension Schemes (Fraud Compensation Levy) (Amendment) Regulations 2022

This document is available on the Gov.UK website:

Review of the Fraud Compensation Levy ceiling - GOV.UK (www.gov.uk)

Annex A: list of those who responded to this consultation

ABI

B&CE

Creative Group

Nest Corporation

NOW: Pensions

SAUL (Superannuation Arrangements of the University of London)

Smart Pension

The Phoenix Group

PLSA

USS (Universities Superannuation Scheme Ltd)

XPS Pensions Group

Annex B: draft amendment regulations

The Occupational Pension Schemes (Fraud Compensation Levy)(Amendment) Regulations 2022.

Annex C: summary of impacts – increase in FCL ceiling from April 2022

As the Department is proposing a change to the levy ceiling, this section sets out the estimated impacts of raising the rates compared to keeping them at their current level. The current and proposed ceilings are outlined in Table 1.

Table 1: Current and proposed rates for the Fraud Compensation Levy per pot[10]

Scheme Type	Levy Ceiling 2021/22	Levy Ceiling 2022/23
Master Trusts	£0.30	£0.65
All Other Eligible Occupational Schemes	£0.75	£1.80

Modelling Methodology

The model compares the proposed rates with the "Do Nothing" scenario (i.e., rates stay at 2021/22 level) to understand the impacts. It should be emphasised that any modelling is subject to related uncertainties, heavily dependent on underlying assumptions, and the development of the pension and labour markets.

Revenue Forecasts

Membership forecasts are multiplied by the relevant levy rate (Table 1) to generate revenue projections over the next nine years[11].

Membership Forecasts

Total membership is estimated by forecasting the growth in each scheme type. Departmental forecasts are based on the following key assumptions (Table 2):

[10] 2021 Fraud Compensation Levy
[11] It is assumed the Fraud Compensation Fund levy ceiling does not increase beyond 2022/23.

Table 2: Membership Forecasting Assumptions

Type of Pension	**Scheme Size**	**Annual Membership Growth**
Occupational Defined Benefit and Hybrid (excluding Hybrid Master Trusts)	All Members	Number of members remains at current levels.
Occupational Defined Contribution and Hybrid (including Master Trusts)	2 - 499,999 Members	Growth rates are set at the 3-year geometric average[12].
	500,000+ Members	Growth rates are set at the 2-year geometric average[13].

We have used a different assumption for larger DC schemes because a three-year average captures the end of Automatic Enrolment rollout which predominately affects larger DC schemes. For example, at the end of 2012 there were just under 1.2 million members of occupational DC schemes with more than 5,000 members. This grew to just under 21 million by the end of 2020[14].

Do Nothing - Counterfactual – Levy frozen at 2021/22 rates

Even with no change to the levy ceiling we would still expect a change in revenue driven by the increase in total membership. Table 3 estimates revenue generated through the FCF in a “Do Nothing” scenario. Analysis on the impacts of the proposed change is compared to this counterfactual.

[12] Scheme return data from 2019, 2020 and 2021. Data may be lagged due to the timing of TPR’s data collection. Growth rates are flat lined from 2028 onwards. The geometric average for a series of numbers is calculated by taking the product of these numbers and raising it to the inverse of the length of the series.
[13] Scheme return data from 2020 and 2021. Data may be lagged due to the timing of TPR’s data collection. Growth rates are flat lined from 2028 onwards
[14] TPR (2021). *DC trust scheme return data 2020-21.* Available at: https://www.thepensionsregulator.gov.uk/en/document-library/research-and-analysis/dc-trust-scheme-return-data-2020-2021. TPR does not define band widths larger than 5,000. This analysis is for indicative purposes only to illustrate growth in larger schemes after automatic enrolment.

Table 3: Revenue projections in "Do Nothing" and "Proposed Change" scenarios. [15]

Scenario[16]	**2022/23**	**2023/24**	**2024/25**	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30**	**2030/31**
Do nothing (£m)	16.3	17.5	18.9	20.5	22.5	24.7	27.4	27.4	27.4
Proposed Change (£m)	37.5	40.1	43.2	46.8	51.0	56.0	61.8	61.8	61.8
Impact (£m)[17]	21.2	22.7	24.3	26.3	28.6	31.3	34.4	34.4	34.4

Without a change in the levy, Table 3 shows that projected revenue would have been expected to rise from £16.3m in 2022/23 to £27.4m in 2030/31, a direct result of increased membership. Under the proposed change, revenue is projected to increase from £37.5m in 2022/23 to £61.8m in 2030/31. The introduction of the proposed change would have an additional impact of £257.5m over the nine-year period.

Impact of the proposed levy rates

Question 2 in the consultation document addressed the impact of increases in the levy on providers. The following section summarises these responses and examines the impact on members.

There were 11 respondents who gave 15 responses to question 2[18]:

- 5 respondents indicated increased levy costs would be absorbed by providers with 2 respondents making direct reference to resources being diverted away from other work.

- 2 respondents said the increased cost of the levy would be passed to employers, or that new employers will be quoted higher charges in the future.

[15] Revenue forecasts contained within this response are different to the consultation document published in 2021. Consultation on the review of the Fraud Compensation Levy ceiling - GOV.UK (www.gov.uk) This response uses updated modelling, more recent TPR data and refined assumptions.
[16] Rounded to the nearest decimal place.
[17] This is the aggregate impact on both business and government.
[18] Some of the respondents were pension consultants, who advised costs would be distributed differently depending on scheme type. This means that the number of responses exceeds the number of respondents.

- 8 respondents declared increased costs would be passed onto members.

Direct Costs to Business

The increase in the levy does place a direct cost on pension providers. Table 4 below breaks down the impact of the proposed change for each scheme type from 2022/23 to 2030/31.

Table 4: Additional Costs of Proposed Change by Scheme Type

Total Cost of Proposed Change[19] (£m)	2022/23	2023/24	2024/25	2025/26	2026/27	2027/28	2028/29	2029/30	2030/31	Additional Total Costs
Defined Benefit	6.8	6.8	6.8	6.8	6.8	6.8	6.8	6.8	6.8	60.8
Hybrid	4.9	4.9	4.9	4.9	4.9	4.9	4.9	4.9	4.9	44.4
Defined Contribution (excluding Master Trusts)	1.7	1.8	2.0	2.2	2.5	2.8	3.1	3.1	3.1	22.3
Master Trusts	7.9	9.2	10.7	12.4	14.4	16.8	19.6	19.6	19.6	130.0

Eligible pension schemes will be impacted by changes to the levy ceiling. We estimate total additional costs of approximately £260m after 9 years.

9 respondents stated increasing the levy will lead to higher operating costs. 2 respondents declared the increase in the levy would have minimal operational impact and the affects would be 'immaterial'[20].

The additional cost for DB schemes over the 9-year period is estimated to be approximately £60m. In 2021 only 10% DB members were active, and this figure is

[19] All figures are rounded to the nearest decimal place. Totals across scheme types may not be consistent with Table 3 due to rounding. The total over the 9-year period may not equal the sum of each year due to rounding.
[20] There was no correlation between scheme type and operating cost e.g., respondents who said the raised levy will significantly increase operating costs was a mixture of DB, Hybrid, DC and MT's. Similarly, respondents who said the increase in levy would be minimal were a mixture of DB, DC and MT's.

falling[21]. It is anticipated that the majority of DB schemes will either absorb the cost of the increased levy, or pass the cost to employers, because they are unable to pass costs on to the small portion of active members. For DB schemes, the cost of regulation lies with the sponsoring employer. We assume that any cost incurred to DB schemes will represent a cost to business.

For occupational DC schemes (excluding Master Trusts), there would be a direct cost to the pension scheme provider. The additional cost over the 9-year period is estimated to be approximately £20m. 4 out of 10 DC respondents indicated they would absorb the additional costs which represent a direct cost to business.

For Master Trusts, the additional cost over the 9-year period is estimated to be approximately £130m compared to the 'Do Nothing' approach. Some Master Trusts, such as NEST or the People's Pension, do not charge employers[22]. It is, therefore, unviable to pass the additional cost on. In these circumstances, increased levy costs must either be absorbed or funded through charges on members. 2 out of 9 Master Trusts stated they would absorb all the additional costs, with an additional Master Trust declaring costs would be partly absorbed and partly transferred to members.

Indirect Costs to Business

Increasing the fraud compensation levy places an opportunity cost on providers since resources are diverted away from other areas such as investing in research and development. 5 respondents stated increasing the levy will reduce spending on development which could stifle innovation and affect the member experience.

Benefits to Business

The FCF helps to provide confidence in the occupational pensions market. This could encourage more individuals to enroll in a workplace pension, or not opt-out if automatically enrolled. Confidence in the industry could foster greater contributions where individuals are more likely to pay into a pension scheme if they know their funds will be compensated against in the unfortunate event of dishonesty. Confidence in the market creates a positive externality which benefits all schemes regardless of scheme type.

Benefits to schemes and members

All additional revenue collected through the FCF will be passed on to schemes whose members fell victim to fraud. This is a direct transfer of approximately £260m to 126 schemes who will compensate members. As highlighted by 2 respondents, many members who fell victim to fraud were already financially vulnerable, hence the increase in the levy could improve retirement outcomes for those affected.

Costs to members

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[21] The Purple Book (2021). Available at: https://www.ppf.co.uk/sites/default/files/2021-12/PPF_PurpleBook_2021.pdf

[22] The People's Pension have a one-off set up charge, but employers are not charged on a regular basis. Available at: [Why The People's Pension? | The People's Pension (thepeoplespension.co.uk)]()

Pension scheme members will not incur any direct costs from the levy changes. Members will not be required to do anything because of the levy changes and there will be no costs arising from familiarisation or implementation. However, they could experience indirect costs as outlined below.

For members of DB schemes, the additional cost of the levy could affect the affordability of contributions for sponsoring employers and thus be passed to active members through increased contribution rates. Active members of DB schemes generally pay a fixed percentage of pensionable pay as set out in the Trust Deed and Rules. Increasing active member contribution rates to cover additional levy costs would require amending the Trust Deed and Rules. Where employers operate a 'share of cost' approach, the additional levy cost is shared between employers and active members. Only 10% of DB members are actively contributing with most schemes closed to future accrual and thus most DB schemes are unable to pass the increased cost of the levy on to members[23]. The sole DB respondent confirmed that additional costs would be absorbed.

Though it is not anticipated that schemes will pass on costs to members through increased contribution rates, absorbing additional costs could reduce their ability to deliver other improvements to members such as salaries or benefits.

The number of DB schemes in deficit at the end of November 2021 was 2,403 which equates just over 46% of all DB schemes[24]. Whilst the number of schemes in deficit is gradually decreasing, placing a higher levy on DB schemes risks increasing the funding gap. If liabilities exceed assets, members may risk not receiving their pensions.

Members of DC schemes typically pay a charge towards their pension scheme. DC schemes may choose to pass on the additional levy cost to members through increased annual management charges, or by altering the combination charge which may be a charge on contributions or a flat fee. However, whether a scheme chooses to do this depends on current charges and whether they are close to or at the charge cap level.

The levy increases are relatively small. In a hypothetical situation where all costs were passed on to members through higher chargers, members of Master Trusts would pay an additional £0.35 per year, totaling £3.15 over the 9-year period. Similarly, members of all other eligible schemes e.g., DB, Hybrid and DC (excluding Master Trusts) would pay an additional £1.05 per year, totaling £9.45 over the 9-year period. The Government believes the proposed increases in the Fraud Compensation Levy will not be significant or detrimental to retirement outcomes. Putting the additional cost of the levy into perspective, the average Master Trust pot

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[23] The Purple Book (2021). Available at: https://www.ppf.co.uk/sites/default/files/2021-12/PPF_PurpleBook_2021.pdf

[24] The PPF 7800 Index (2021). Available at: https://www.ppf.co.uk/ppf-7800-index

size is £1,000[25] and the average charge per pot is 0.48%[26]. In this scenario, average annual charges equal £4.80 per year, therefore if the additional cost of £0.35 were entirely passed onto members, it would equate to a 7% increase. Increased costs may be offset by the increased confidence of having security in supporting victims of fraud.

8 respondents said they would pass additional costs of the fraud compensation levy on to members. Whilst pension providers state they will pass additional costs onto members, competitive pressures within the market suggest that not all additional costs will be passed on to members. Evidence shows strong downward pressure on charges for both qualifying schemes (used for automatic enrolment) and non-qualifying schemes, with an average charge to members of 0.48% for qualifying schemes significantly below the charge cap of 0.75%. Similarly charges for non-qualifying schemes have fallen to an average of 0.53%, with 88% of members of non-qualifying schemes now below the cap level[27]. Providers typically felt that competition would continue to maintain a downward pressure on charges.

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[25] PPI (2020). Policy options for tackling the growing number of deferred members with small pots. Available at: [2020-07-23 Policy options for tackling the growing number of deferred members with small pots | Pensions Policy Institute.]() This specifically relates to Master Trusts who may have different memberships to other parts of the DC industry.

[26] Pension Charges Survey (2020). Available at: https://www.gov.uk/government/publications/pension-charges-survey-2020-charges-in-defined-contribution-pension-schemes/pension-charges-survey-2020-charges-in-defined-contribution-pension-schemes

[27] Ibid.