
Abolition of short service refunds in occupational pension schemes

Department for Work and Pensions

RPC rating: validated

An impact assessment (IA) for this measure was first produced to support the Pensions Act 2014. The RPC validated the estimated equivalent net cost to business of the measure at £29 million. However, as the measure was not implemented in the last parliament, this figure needs to be updated for accounting purposes under the business impact target in the current parliament. The Department has, therefore, revised the IA, taking the opportunity to use updated price base years and data (from HMRC and the occupational pension schemes survey) on the number of short service refunds since automatic enrolment began.

Description of proposal

Prior to implementation of the Pensions Act 2014, members of occupational pension schemes who left schemes within two years of joining them could be offered cash equivalent transfers to other schemes or refunds of their contributions – a short service refund. Members who did not actively choose a transfer could receive a short service refund by default, thereby losing an element of their pension savings and the value of their employers' contributions. Short service refunds are not possible in workplace personal pension schemes, so there was a disparity in treatment of members depending on the type of scheme employers choose for their employees. From 1 October 2015, occupational pension schemes have, therefore, not been permitted to offer short service refunds.

Impacts of proposal

The IA states that abolishing short service refunds generates three types of costs and benefits¹:

- Long term benefits to employees in retaining their employers' and the State's contributions to their pension pot and the investment growth delivered by leaving their pension pot invested rather than taking a cash refund of their contributions (£44.5 million).

¹ Figures are average annual costs and benefits over ten calendar years from 2015, expressed in 2014 prices

- Associated short term costs to employees (£16.4 million) and employers (£17.6 million) as a result of money being retained in employees' pension pots rather than transferred to employees and employers via refunds; and to the State via tax paid on employees' refunds (£3.8 million).
- Recurring administration costs (£3.2 million) in maintaining dormant pension pots, net of charges paid on them over the same period (£1.6 million); and savings from no longer having to process refunds (£1.3 million); net cost to pension schemes - £0.3 million

Following the adjustments made by the Department, the IA assesses the net present value (NPV) of the measure at £51.58 million in 2014 prices over a ten-year period beginning in 2015. The business NPV is assessed as -£149.63 million (net cost). This translates to an estimated equivalent annual net direct cost to business (EANDCB) of £17.4 million, which the RPC is able to verify. The measure is a qualifying regulatory provision that should be accounted for under the business impact target.

Quality of submission

The IA is well drafted and very clearly structured. The Department has provided a clear narrative of how the measure has been developed and, in particular, how the assessment has been adjusted to reflect the latest data and prices. The assumptions used are explained clearly, with concise summaries provided.

Small and micro business assessment (SaMBA)

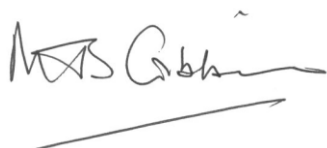
The SaMBA explains that the measure applies to all employers/schemes regardless of size. However, evidence from DWP qualitative research suggests that it is only large employers and employers with very high staff turnover that process large volumes of short service refunds. The IA states that the research states that smaller employers and those with a low staff turnover considered the vesting rules to be of little overall importance, relative other elements of a trust-based pensions scheme. Many did not consider them to be a benefit at all, and some felt that the administration involved in processing occasional short service refunds is a disadvantage: "*They don't really offer much of a benefit. There is administration involved...[which is a]... nuisance really... [with no]...benefit at all.*" (Paragraph 39) The IA concludes that abolishing short service refunds affects large employers predominantly and, for the vast majority of small and micro employers and schemes, the impact will be negligible or nil.

Departmental assessment

Classification	Qualifying regulatory provision (IN)
EANDCB	£29 million (initial estimate) £17.4 million (final estimate)
Business net present value	-£149.63 million
Net present value	£51.58 million

RPC assessment

Classification	Qualifying regulatory provision (IN)
EANDCB – RPC validated ²	£17.4 million (final estimate)
Business impact target score	£87.0 million
Small and micro business assessment	Sufficient



Michael Gibbons CBE, Chairman

² For reporting purposes, the RPC validates EANDCB figures to the nearest £100,000.