STATES OF JERSEY

DRAFT SOCIAL SECURITY (AMENDMENT OF LAW No. 3) (JERSEY) REGULATIONS 201-

Lodged au Greffe on 25th September 2012
by the Minister for Social Security

STATES GREFFE

Jersey

DRAFT SOCIAL SECURITY (AMENDMENT OF LAW No. 3) (JERSEY) REGULATIONS 201-

REPORT

Revision to calculation of States Grant in respect of supplementation

Introduction

In July 2011, the States Assembly approved P.110/2011 – Social Security (Amendment of Law No. 1) (Jersey) Regulations 2011. This made a number of changes to the Social Security Law, including a new method of calculating the value of the States Grant in respect of supplementation.

The calculation was introduced to ensure that at the time of a business plan debate in September, when expenditure approvals are agreed, the value of the States Grant for the following financial year would be known with certainty.

Since that calculation was proposed and adopted by the States Assembly, the Public Finances (Amendment No. 3) (Jersey) Law 2011 has come into force, including a new financial planning cycle based on a Medium Term Financial Plan (MTFP). This planning cycle is set out in Article 7 of the Public Finances (Jersey) Law 2005. Each Plan starts at the beginning of the second full year after an ordinary election, and ends at the end of the first full year following the next ordinary election. The first Plan covers the 3 year period 2013 – 2015.

Whereas the current calculation for the States Grant removes the uncertainty in the first year of a Medium Term Financial Plan cycle, it does nothing to address the possible variation in the value of the Grant in the second and subsequent years where the total States expenditures limits will be fixed.

This further amendment aligns that calculation with the timing of the Medium Term Financial Plan to ensure that the value of the States Grant is known for each year of a Medium Term Financial Plan, at the time that the Plan is debated by the States Assembly.

The proposed calculation is the basis for the budgets for the States Grant, as part of the Social Security Department cash limit, within the 2013 – 2015 MTFP. Further calculations will be required in line with each new MTFP period.

Background

Contributors who have earnings above the lower earnings limit of £796 per month, but below the standard earnings limit of £3,778 during a month normally receive a full contribution record for that month, although the value of contribution made is below that required for a full contribution record. The process of making up the shortfall in contribution is known as supplementation, and it ensures that lower earners are able to receive full pension and benefit rights.

Until 2011 the exact value of supplementation of lower earners' contributions was calculated to determine the value of the annual payment made by the States to the Social Security Fund (the States Grant), to meet the cost of the supplementation process. This cost could vary considerably depending on the state of the economy, wage levels and the distribution of wages within the local labour market. In 2011, the method of calculating the States Grant was amended to set a fixed cost that was known in advance of the year itself, removing this uncertainty in the setting of States expenditure.

Following the move to a calculated amount in individual years, the value of the Grant may be above or below the actual cost of supplementation in that year. However, in the long term, these differences cancel out and there is minimal impact on the Fund itself.

The introduction of contributions above the standard earnings limit in 2012 now provides additional income into the Social Security Fund, which will be used to meet part of the cost of supplementation and so reduce the cost to be met by the States Grant.

Medium Term Financial Plan

The States has recently moved from a one-year financial plan to a 3 year financial planning cycle – the Medium Term Financial Plan (MTFP). The MTFP process requires that the States agree cash limits for each department across a 3 year period, rather than a one year period, and this has led to a review of the calculation of the States Grant.

Proposal

This proposal is based upon the same calculation currently used for one year, but extends it to allow the calculation to remain in place during the whole length of an MTFP. This ensures that changes in the economy or the workforce during the duration of the MTFP will not affect the cost of the States Grant to the taxpayer. As with the current system, in some periods the calculation will act to provide a higher value of Grant to the Fund, and in other periods it will provide a lower value. As the Social Security Fund is designed to operate over many decades, these temporary fluctuations have only a small impact on the long-term value of the Fund.

The revised calculation will set the same value for the States Grant in the first year of each MTFP as the current calculation. In the second and subsequent years, the value of the States Grant will be adjusted from the previous year using the change in the earnings index in the base year, which is set as the year 2 years before the beginning of the MTFP period.

The base year is set as 2 years before the start of the MTFP to ensure that each of the variables used in the calculation is available at the time at which the MTFP is lodged. In particular, the earnings index is only calculated once a year, based on data collected in respect of June with the results published towards the end of August. Full details of the calculation are provided in the **Appendix** to this Report.

Under the current electoral cycle, the MTFP will last for 3 years. Elections will next be held in 2014, and the second MTFP will start in 2016. The value of the States Grant for the MTFP starting in 2016 will be based on the actual values of supplementation, contributions above the standard earnings limit and the change in the earnings index in 2014.

Financial and manpower implications

There are no manpower considerations. The proposed calculation will result in a reduction in the value of the States Grant in 2014 and 2015, compared to the previous estimated values. The impact of this is a corresponding reduction in the overall value of the Social Security Fund over the same period.

The proposed calculations providing certain values for the States Grant for 2013 – 2015 have been included in the Social Security Department cash limits for 2013 – 2015 in the Medium Term Financial Plan.

In future MTFPs, the revised calculation may result in a higher or lower value of States Grant compared to the current calculation, depending on the relationship between the earnings index in the base year and the earnings indices in other years. If the proposed calculation is used consistently over a long period, the long-term impact on the Social Security Fund will not be significant.

The current calculation is based on 3 values:

- A – the actual cost of supplementation in the base year
- B – the actual value of contributions received above the standard earnings limit in the base year
- C – the rise or fall in the earnings index in the base year.

The current calculation sets the value of the States Grant as:

$(A-B) \times (1+C)^2$ and the base year is the year that is 2 years before the year of the States Grant.

The new calculation will be exactly the same as the existing calculation for the first year of a Medium Term Financial Plan:

States Grant = $(A-B) \times (1+C)^2$ with A, B and C referring to the year 2 years before the Medium Term Financial Plan started.

The base year is set as 2 years before the start of the MTFP to ensure that each of the variables used in the calculation is available at the time at which the MTFP is lodged. In particular, the earnings index is only calculated once a year, based on data collected in respect of June with the results published towards the end of August.

In the second and subsequent years of a Medium Term Financial Plan, rather than resetting A, B and C, the value of the States Grant will be calculated based on the States Grant in the previous year of the MTFP, increased by the factor (1+C).

The factor (1+C) represents the growth in the economy from year to year, as measured by the earnings index. The change in this index is also used to adjust the various earnings levels that are used to determine the level of contributions payable.

In the first year of an MTFP, the factor $(1+C)^2$ is used to represent the increase in contributions from the base year, 2 years ago, to the current year. The change in the earnings index for the base year is then used again in each year of the MTFP to adjust the States Grant.

The Finance Law refers to the length of the MTFP in terms of the interval between elections, and the proposed formula allows for this, as the values are reset in the first year of a new MTFP and then the same updating factor is applied to the value of the States Grant in each subsequent year of the MTFP. This formula would work with an MTFP lasting for 3 or 4 years, for example.

In terms of the actual MTFP now under consideration, the following values will be used:

In 2013, the value of the States Grant will be based on:

- A – £66,072,114, the actual cost of supplementation in 2011 (the year 2 years before 2013, which is the first year of the MTFP)
- B – £6,900,000 (as the new contribution rate was only introduced in 2012, the existing legislation provides for a fixed value for B for 2013, and the revised formula will need to refer to the same fixed value for this MTFP)
- C – 2.5% – the rise in the earnings index in 2011.

Giving a value of £62,167,702 for 2013.

In 2014, the value of the States Grant will be:

£62,167,702 x (1+2.5%) = £63,721,895.

In 2015, the value of the States Grant will be:

£63,721,895 x (1+2.5%) = £65,314,942.

Explanatory Note

This Law amends the Social Security (Jersey) Law 1974 so as to revise the way in which the annual contribution by the States to supplementation is calculated. The revised calculation has effect from 2013, being the first year to which the first medium term financial plan relates.

The changes affect the way in which the States contribution to supplementation is calculated for the second and any subsequent year to which a medium term financial plan relates. For the future, the calculations for the second and subsequent years will be based upon the amount calculated as due for the first year to which the medium term financial plan relates, increased (or decreased) in accordance with the percentage rise (or fall) in the Jersey Index of Earnings for the year that is 2 years before the first year of the medium term financial plan.

Jersey

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Made *[date to be inserted]*

Coming into force *[date to be inserted]*

THE STATES, in pursuance of Article 50 of the Social Security (Jersey) Law 1974[1], have made the following Regulations –

1 Article 9A of the Social Security (Jersey) Law 1974 substituted

For Article 9A of the Social Security (Jersey) Law 1974[2] there shall be substituted the following Article –

“9A Contributions by States to supplementation

(1) The amount required by Article 4(3) to be paid into the Social Security Fund shall be determined annually, for 2013 and ensuing years, in accordance with this Article.

(2) Where the year is the first year of a medium term financial plan, the amount to be paid for the year shall be the product of the following formula –

$(A - B) \times (1 + C)^2$

Where –

(a) A is the total amount required, for the base year, for the purpose of supplementing contributions in accordance with Article 9, reported in the accounts prepared in accordance with Article 30(4);

(b) B is –

(i) for the purpose of determining the amount payable in 2013, £6,900,000;

(iii) for the purpose of determining the amount payable for any subsequent first year of a medium term financial plan, the aggregate of the following amounts –

(A) the Class 1 secondary contributions paid for the base year in accordance with paragraph 3(2)(c) of Schedule 1A,

(B) the full rate Class 2 contributions paid for the base year in accordance with paragraph 3(c) of Schedule 1B, and

(C) the reduced rate Class 2 contributions paid for the base year in accordance with paragraph 4(c) of Schedule 1B,

as those amounts are reported in the accounts prepared in accordance with Article 30(4); and

(c) C is the percentage rise or fall in the Jersey Index of Earnings in the base year.

(3) If B is equal to or greater than A, no money is required to be paid for the year.

(4) Where the year is the second or any subsequent year of a medium term financial plan, the amount to be paid shall be the product of the following formula –

D x (1 + C)

Where –

(a) D is the amount paid under this Article for the preceding year; and

(b) C is the percentage rise or fall in the Jersey Index of Earnings in the base year.

(5) The amount to be paid under this Article for a year may be paid in a lump sum or in instalments, and at such time or times, as the Minister determines.

(6) In this Article –

'base year' means the year 2 years before the first year of a medium term financial plan;

'first year of a medium term financial plan' means the first financial year to which a medium term financial plan relates, and references to the second or any subsequent year of a medium term financial plan shall be construed accordingly;

'medium term financial plan' means a plan prepared in accordance with Article 7(1) of the Public Finances (Jersey) Law 2005[3] and approved by the States.".

2 Citation and commencement

These Regulations may be cited as the Social Security (Amendment of Law No. 3) (Jersey) Regulations 201- and shall come into force on 1st January 2013.

[1] *chapter 26.900*
[2] *chapter 26.900*
[3] *chapter 24.900*