

Title: The Statutory Sick Pay Percentage Threshold (Revocations, Transitional and Saving Provisions) (Great Britain and Northern Ireland) Order 2014 IA No: DWP0035 Lead department or agency: Department for Work and Pensions Other departments or agencies: HMRC	Impact Assessment (IA)		
	Date: 21/11/2012		
	Stage: Final		
	Source of intervention: Domestic		
	Type of measure: Secondary legislation		
Contact for enquiries: Daniel Foster 020 7449 5559			
Summary: Intervention and Options			RPC Opinion: N/A

Cost of Preferred (or more likely) Option			
Total Net Present Value	Business Net Present Value	Net cost to business per year (EANCB on 2009 prices)	In scope of One-In, Measure qualifies as One-Out?
£1,076m	£115m	-£23m	No
			NA

What is the problem under consideration? Why is government intervention necessary?

The Percentage Threshold Scheme (PTS) offers partial reimbursement to employers choosing to participate in the scheme and whose expenditure on Statutory Sick Pay exceeds 13% of their Class A National Insurance Contributions. The scheme does not help employers to manage sickness absence and weakens the incentive for them to manage absences themselves. The independent Review of Sickness Absence recommended abolishing the PTS and launching a service that will help employers to manage long term absences and reduce associated costs.

What are the policy objectives and the intended effects?

- to incentivise employers to better manage sickness absence
- to provide a non-regulatory alternative (through the provision of a health and work advisory service) to support employers to more effectively manage sickness and mitigate potential increased costs of sick absence due to the removal of the PTS
- to establish a health and work advisory service which considers the occupational health of employees after four weeks of sickness absence and makes recommendations for interventions where appropriate with the aim of facilitating a more rapid return to work.

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)

We have considered:
Do nothing
Option 1: remove the PTS (a tax measure) and launch independent health and work advisory service (a spending measure) - this is non-regulatory.

Option 1 is the preferred option and generates benefits over costs for employers, government and the economy as a whole.

Will the policy be reviewed? It will not be reviewed. If applicable, set review date: Month/Year					
Does implementation go beyond minimum EU requirements?			N/A		
Are any of these organisations in scope? If Micros not exempted set out reason in Evidence Base.	Micro Yes	< 20 Yes	Small Yes	Medium Yes	Large Yes
What is the CO ₂ equivalent change in greenhouse gas emissions? (Million tonnes CO ₂ equivalent)			Traded: N/A	Non-traded: N/A	

I have read the Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) that the benefits justify the costs.

Signed by the responsible Minister: _____ Freud _____ Date: _____ 26/11/2012 _____

Summary: Analysis & Evidence

Policy Option 1

Description: Option 1: Removal of the Percentage Threshold Scheme; Launch of independent health and work advisory service

FULL ECONOMIC ASSESSMENT

Price Base Year 2012	PV Base Year 2014	Time Period Years 5	Net Benefit (Present Value (PV)) (£m)		
			Low: 333	High: 1,819	Best Estimate: 1,076

COSTS (£m)	Total Transition (Constant Price) Years		Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	10	1	90	429
High	10		183	865
Best Estimate	10		136	647

Description and scale of key monetised costs by 'main affected groups'

Exchequer would be liable for estimated £39m annual cost of running new health and work advisory service £50m annual cost of (voluntary) interventions (includes £16m tax) is attributed to employers, though state may (part) fund this. Employers would cease to receive approximately £47m per year under the PTS.

Other key non-monetised costs by 'main affected groups'

While employers have advised that the new service will work alongside and not replace existing Occupational Health / Vocational Rehabilitation services, some displacement may occur. Employers will bear wage costs for employees returning from sickness absence (assumed to be equivalent to associated output increase). Employees returning to work will forgo sickness pay [and in addition will incur pecuniary/non-pecuniary costs/benefits from being back in the workplace]. Quantified estimates of impacts of returns to work on Employers and the Exchequer were based on net changes so gross costs and benefits relating to wage payments are not quantified here.

BENEFITS (£m)	Total Transition (Constant Price) Years		Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	0	1	258	1,198
High	0		483	2,248
Best Estimate	0		370	1,723

Description and scale of key monetised benefits by 'main affected groups'

Employees' early return to work from sickness absence saves employers £123m per year in sickness pay; Exchequer recovers £141m per year in additional tax/NIC based on early return to full pay plus £16m in tax on interventions; reduced likelihood of individuals flowing onto Employment Support Allowance saves Government £43m per year [all three total £200m]. Exchequer saves further £47m per year in PTS costs.

Other key non-monetised benefits by 'main affected groups'

Employers who would have submitted claims under the PTS are no longer exposed to the administrative cost of doing so. Since no reliable estimates of this cost are available (but it is expected to be small) the benefit of its removal is not quantified. The new service may also raise awareness of Occupational Health and Vocational Rehabilitation, and make its provision part of standard working practices. Employees benefit from increased income from return to work [in addition to pecuniary/non-pecuniary costs/benefits associated with return to the workplace]. Employers benefit from increased output from reduced days lost to sickness absence (increase is assumed to be equivalent to wage cost). Increased economic output is a key wider impact of the service but the estimates quantified here focus on the direct impacts on business.

Key assumptions/sensitivities/risks

Discount rate (%) 3.5

2014/15 is the final year of the PTS; the new service starts in 2014/15. The removal of the PTS doesn't precipitate (illegal) discrimination by employers against employees with poor sickness absence records and that out-of-year claims are similar in proportion to in-year claims as in 2010/11 (the only year for which this information is available). Employers pay for all interventions recommended by the new service, including resulting employee tax liability, which is incurred at the basic rate [employees are basic rate taxpayers].

BUSINESS ASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £m:			In scope of OIOO?	Measure qualifies as
Costs: 89	Benefits: 112	Net: 23	No	NA

Evidence Base (for summary sheets)

Policy Rationale

What is the current policy?

1. The Percentage Threshold Scheme (PTS) allows employers to recover some of the Statutory Sick Pay (SSP) paid in a month. SSP is the minimum rate at which employers are obliged by law to pay employees who are unable to work because of sickness. It is payable for spells of sickness lasting between 4 days and 28 weeks, though employers can continue to pay beyond this period (and/or above the statutory minimum rate) if they wish. The 2012/13 rate of SSP is £85.85 per week for qualifying employees for up to 28 weeks.
2. Employers usually meet the full cost of Statutory Sick Pay, but can recover via the PTS that part of the cost that exceeds 13% of the employer's class A National Insurance Contribution (NIC) liability in a month. Micro employers (with fewer than 10 employees) receive 70% of the recovery. HMRC figures from 2009/10 suggest that the average amount claimed under the scheme is £500 per year, per claimant (employer).

What is the change in policy?

3. The independent Review of Sickness Absence¹ identified that the PTS offers poor value for money: while reimbursing some of the costs of sickness absence it does not support employers to effectively manage absences and weakens the incentive for them to manage absences themselves. The review recommended that Government abolish the PTS and introduce a new service to provide an independent assessment of individuals' fitness for work after they had been absent from work for health reasons for four weeks. The response to the review takes this further, proposing a service that manages both health assessments and appropriate interventions, co-ordinating these with the employer, the individual and their GP. In addition, the service will also provide general occupational health advice. The service will offer accessible advice on how to prevent employees from leaving the workplace due to illness and how to overcome barriers preventing employees from returning to the workplace.
4. For employees who enter long term sickness absence, the service will provide a State-funded assessment by occupational health professionals and provide advice to employers on how to facilitate a return to work. For employees with more complex needs, the service will continue to offer case management and ongoing support to enable their return to work.
5. Regulations currently provide employers with the right to satisfy themselves of an employee's entitlement to Statutory Sick Pay and the right to withhold payment if an employee declines a request to seek (further) medical advice. Employees can also challenge employer decisions to withhold statutory sick pay through HMRC's dispute process. As such, participation in the service will be voluntary for employees, but employers may choose to make payment of part or all of sickness payments conditional on an employee's engagement with the service and its recommendations. We don't anticipate changes to volumes of disputes raised with HMRC as a result of the introduction of the new service.

Options considered:

Do nothing: the Exchequer will continue to reimburse costs of statutory sick pay above 13% of employer NIC liabilities for employers making successful applications to the PTS.

Option 1: Abolish the PTS and launch independent health and work advisory service. This option is a non-regulatory alternative to support employers to manage sickness absence more effectively.

Costs and benefits of Option 1

6. Costs and benefits are presented in 2012 price terms as averages over the first 5 years of the service. The service will be built in the final year of the PTS' operation, and be fully operational in the first year of the PTS' abolition.

¹ Black, C. and Frost, D. (2011) *Health at work – an independent review of sickness absence*. DWP. Available at: www.dwp.gov.uk/docs/health-at-work.pdf

7. The abolition of the PTS removes a transfer of around £50m per year from the Exchequer to businesses;² the new health and work advisory service will generate a net value of around £70m per year for employers (£120m in benefits minus £50m in intervention costs) and around £160m per year for the state, and will increase economic output by around £670m per year.
8. In developing and analysing the impact of this service, the review response drew on the two seminal scientific reports in this field³ and the further insights of Dr Nick Kendall,⁴ Professor Kim Burton⁵ and of Professor Stephen Boorman.⁶ They agreed the projection that the service would reduce the net cost of sickness absence associated with its customers by 20%-60%, which is consistent with interventions of this nature. The response to the review made the conservative assumption that the service reduces sickness absence duration for its customers by just 20%-40%.
9. Based on 560,000 service users per year (half the number of employees who reach 4 weeks of sickness absence per year) the service is expected to cost the state around £40m per year and to recommend a further £30m in interventions [the full cost of interventions is attributed to employers in this IA, though the State may (part) fund these; as the cost is attributed to employers, it attracts a further £20m cost in tax, which is a transfer from employers to the state]. Early returns to work are expected to save employers £120m in sick pay if they pay at the statutory minimum, and significantly more if they pay above the minimum.
10. Earlier returns to normal pay should also generate £140m in tax and National Insurance contributions (these will be smaller if sick pay is closer to normal pay than the statutory minimum) and should also reduce the likelihood of employees flowing into unemployment and onto sickness benefits, saving a further £40m in Employment Support Allowance (and subsequently Universal Credit) costs. The state also receives £20m in tax on interventions.
11. The attached technical annexe from the draft review response discusses in more detail the analysis underpinning the projected costs and benefits of the new service, though it describes these to the nearest £10m (not the nearest £1m, as in the template sections of this IA) and gives steady state values (not the average annual values given throughout this IA).

Interaction with existing Occupational Health services at work

12. In stakeholder engagement exercises during the formulation of Government's response to the Review, employers indicated that the proposed health and work advisory service would operate in conjunction with existing Vocational Rehabilitation (VR) and Occupational Health (OH) services in the workplace, rather than replacing them. Nevertheless we anticipate the new service having greatest impact where employees don't have access to VR and OH services through their workplace.

Non-exemption of micro businesses

13. Smaller employers are the least likely to offer Occupational Health services to their employees⁷ and so are expected to benefit disproportionately from the new service. Micro employers (those with fewer than 10 employees) currently receive around 70% of money paid out under the PTS. To exempt smaller employers from the removal of the PTS would therefore not only leave the new advisory service with a significant funding gap, but would also be likely to attract criticism from other types of employer, who through the loss to non-micro employers of the PTS would effectively be paying for a service that disproportionately benefits smaller employers.

Direct costs to businesses.

² Removal of the PTS will also remove administrative costs for employers choosing to apply to the scheme, but as there is no direct evidence of the value of these and it is reasonable to presume they are small relative to the value of refunds themselves, we have not reduced the 'cost' of the scheme's removal to reflect this.

³ Waddell, G. and Burton, K. (2006) *Is work good for your health and well-being*. DWP. Available at: www.dwp.gov.uk/docs/hwwwb-is-work-good-for-you.pdf and Waddell, G., Burton, K. and Kendall, N. (2008) *Vocational rehabilitation: what works, for whom, and when?* DWP. Available at: www.dwp.gov.uk/docs/hwwwb-vocational-rehabilitation.pdf

⁴ Co-author of "Vocational rehabilitation: what works, for whom, and when?"

⁵ Co-author of "Is work good for your health and well-being" and "Vocational rehabilitation: what works, for whom, and when?"

⁶ Author of Boorman, S. (2009) *NHS Health and Wellbeing - The Boorman Review*. NHS. Available at: www.nhshealthandwellbeing.org/pdfs/NHS_Staff_H&WB_Review_Final_Report_VFinal_20-11-09.pdf

⁷ Around 10% of small employers report providing access to Occupational Health services for some or all of their employees, compared to around 50% of medium sized employers and around 80% of large employers: Table 3.1 Young, V. and Bhaumik, C. (2011) *Health and well-being at work: a survey of employers*. DWP Research Report No. 750. Available at: <http://research.dwp.gov.uk/asd/asd5/rports2011-2012/rrep750.pdf>

14. Employers currently receive around £50m per year through the PTS costs (2010/11 shows an SSP outturn of £48m (http://research.dwp.gov.uk/asd/asd4/budget_2012_060812.xls) and so this is the cost to employers of its withdrawal, though the withdrawal of the PTS and provision of a non-regulatory health and work advisory service to support employers is a spending decision which is out of scope for One-in, One-out (or One-in, Two-out).
15. For the purposes of this Impact Assessment we have assumed that the cost of interventions recommended by the service (estimated at £50m per year, including £20m in tax) will be met in full by employers, though in reality some or all of the interventions may be delivered through the NHS or otherwise funded by Government. There will be no regulatory requirement on employers to meet these costs.

Non-monetised costs and benefits

16. As we have noted in the template for this IA, employers will benefit from increased output associated with fewer working days lost to sickness absence, but will also incur a wage cost above their normal rate of sick pay. The total wage cost to the employer and the benefit to the employer of an employee's output are assumed to be equal and opposite, and are both omitted from this analysis. All the analysis of the new service is based on net changes compared with the do nothing option.
17. Increased economic output is a key wider impact of the service but the estimates quantified here focus on the direct impacts on business.
18. We have also omitted the impact on the employee of an earlier return to work because the financial case for the intervention is made on the basis of its impact on employers and the state; the impact on employees in this framework is less clear, since the financial impact must be weighed against the (non-pecuniary) 'cost' of having to work, yet the overwhelming conclusion from health and wellbeing literature is that individuals at work are generally happier and healthier than those not at work,³ and that especially after four weeks of absence, the net impact of labour market detachment will be negative and increasing as the absence continues.

Summary and conclusions

19. Overall, there is a good case to abolish the PTS as its replacement with the new service improves employers' incentives and ability to manage sickness absence, with a corresponding reduction in costs that more than offsets the loss of PTS as a revenue stream: the abolition of the PTS will cost employers approximately £50m per year, but the incoming service will save employers £70m per year, giving a net employer benefit of £20m per year.