

## **Paper for the DAS Regulatory Review Working Group.**

### **Payment Distribution - redistribution to the advice sector**

The current consultation on returning funds to the advice sector says the following:

From 1 January 2018 until 1 December 2018 there were 753 public sector DPPs approved. With an estimated average admin fee of £420 per year, the total funds would be in the region of £316,000 per annum.

This is a top end estimate as cases are approved at various points in the year and will not have each been paying every month for the year.

There is also the matter of missed payments where each payment cannot be guaranteed by debtors.

This would suggest that in the first year, on the basis of no increase in numbers, around £100,000 would be available to distribute.

This has been widely interpreted as implying the AiB would retain “the remaining £216,000” available in the first year to cover its costs. This is however not what was intended. This note explains why – and sets out more details as requested on the approach we will adopt.

First, the figure of £316,000 is simply a result of multiplying the 753 public sector cases approved in 2018 by £420 (the average expected fee per case). However, in the first year, some cases will begin at the start of the year, and some cases will begin at the end of the year. On the basis that cases begin equally across the year, it is reasonable to estimate that the average case in the first year will bring in only six months’ fee - £210. That would halve the total fee income to £158,130. That would also be, for example, before allowing for any revocations – which across the caseload run at an average of 9% a year, but might be expected to be higher in the first year of a case’s life. Since we do not expect AiB to be appointed as payment distributor in every DAS case from a public sector money adviser, the figure of £100,000 was only ever intended to give an order of magnitude as to the likely sums available for redistribution to the free sector.

That however does beg the question of future years. We have said that AiB will seek to retain only sufficient to cover the costs of the payment distribution function itself. This paper sets out an approach to doing so, and invites the Group to endorse both the principles underlying that approach, and the ensuing practical outcome of applying those principles in the early years of adopting this new approach.

First, we set out how we calculate the costs we expect to incur in delivering the function. Then we look at possible total income. Finally, we propose how we might

adopt a single approach that gives certainty for our stakeholders whilst delivering the intended outcome of cost recovery over the longer period.

All of this is of course dependent on a large number of assumptions. The changes to DAS are designed to significantly increase the numbers of people able to benefit from the scheme – both by the changes made in October 2018 which aimed to make the scheme attractive to a wider range of people, and by the current set of proposed changes will aim to make it possible for more free and fee-charging advisers to offer the scheme. As importantly, because the fee will be set at the same level regardless, we believe that public sector advisers – having identified DAS as the most suitable option – will be able to pass clients onto fee charging organisations to take forward the detailed administration, knowing this will be at no financial detriment to the debtor. This should both free up a good deal of time for public sector advisers, but might also reduce the overall share of cases actually submitted by that sector – and hence the share in which AiB could be nominated as PD.

### **The annual costs of providing a Payment Distribution function**

This is critically dependent on the volume of cases coming to AiB. For modelling purposes, we have assumed that the share of cases generated by the public sector continues at 26%, that AiB is appointed as PD in all such cases, and that the total number of cases is between 2,500 to 5,000 a year. (For comparison, during 2018-19 the total number of cases was 2,553).

We have held discussions with all those with experience of PD work under the current system, who have suggested that the current operational setup requires around one member of staff per 100 cases. We believe that the new eDEN system offers very significant savings on that model – so that our initial estimates are that we will require three full time members of staff with some limited senior management input. Costs of this level of staffing would be:

Grade	Number	% time	Cost
A3	2	100%	53,609
B1	1	100%	34,598
B2	1	10%	4,378
B3	1	3%	1,756
			<b>94,341</b>

Additional to these variable staff costs are more known IT and licensing costs – the upfront costs of the necessary IT development spread over the number of years of its useful life via our depreciation policies. We have allowed £20,000 a year for these elements.

Finally there is the necessity to consider whether or not it is fair to allocate a share of AiB's general overheads – such as office accommodation, staff training and so on. Depending on the method chosen for allocating such costs, this could range from around £75,000 to £150,000 a year.

**This gives an estimated total annual cost of the PD function as £180-255,000.**

We are aware that the staff costs will build up over time, so that the full staff resource outlined here may not be needed – and the full cost suggested here may not be incurred - until years 3 or 4 of the new system.

**Likely total income received from those cases in which AiB acts as payment distributor**

For illustrative purposes only, and with numbers rounded for ease, the table below is based on the following assumptions:

- AiB will act as PD in 26% of cases (the current share of public sector cases);
- the 20% PD fee will generate an average of £420 per case per year (average), but half this in year one;
- 9% of live load will be revoked each year (current average);
- all cases that are not revoked run for at least 4 years (the current average is 6).

No of New cases pa	2500	3500	4500	5000
<b>Year One</b>				
No of AiB Cases (26%)	650	910	1170	1300
PD Fee (20%)	£136,500	£191,100	£245,700	£273,000
<b>Year Two</b>				
AiB new Cases	650	910	1170	1300
AiB Total Cases	1242	1738	2235	2483
PD Fee	£384,930	£538,902	£692,874	£769,000
<b>Year Three</b>				
AiB new Cases	650	910	1170	1300
AiB Total cases	1780	2492	3204	3560
PD Fee	£611,001	£855,402	£1,099,802	£1,222,003
<b>Year Four</b>				
AiB New Cases	650	910	1170	1300
AiB Total Cases	2270	3177	4085	4539
PD Fee	<b>£816,726</b>	£1,143,417	£1,470,107	£1,633,452

We would take the view that the number of new DAS DPPs generated year on year will grow significantly from the 2500 begun in 2018-19. But we believe this will be offset by AiB being appointed as payment distributor in far fewer than 26% of new cases (and indeed, the proposed changes are in part intended to ensure this).

## Drawing conclusions

The analysis above suggests that, when the new system is fully established, AiB will face costs of around £200,000 per year for delivering the PD function, but could be receiving in the region of £800,000 per annum from PD fee income from cases in which public sector advisers had nominated AiB as PD.

We are also strongly influenced by the analysis in the full consultation paper that suggests the current average fee to a payment distributor is between 5 and 6%. The figures given in the consultation paper are copied below for ease:

Q2 2018/19	Total amount ingathered by the PD	Fee to PD	Percentage
All cases	9,231,843	534,381	5.8%
Public sector	3,672,550	202,017	5.5%

Together, and taking consideration the following:

- though AiB should recover its costs, it does not seem sensible to aim to break even until the system reaches steady state (with then some allowance to “catch up” earlier losses over time);
- that all sides need certainty, so that we do not want to be making constant adjustments to the mechanism that determines how much is returned to the free sector;
- we want something as simple to calculate and administer as possible.

We are minded to propose that in those cases where AiB is appointed as PD, AiB should retain 5% to cover the costs of the PD function, with 15% being returned to the advice sector.

This would be fixed for the first three years of the new system, and then reviewed in the light of real world experience.

**The Working Group is invited to give its views on the approach outlined above and the assumptions that underpin it, and to say whether or not it considers this a reasonable outcome that could be recommended to Scottish Ministers.**

**AiB July 2019**