Pension
Protection
Fund

The 2019/20 Pension Protection Levy Policy Statement

December 2018

Foreword

I am delighted to introduce our Policy Statement, which concludes the development of the levy rules for 2019/20.

Our consultation document – published in September – set out our view that the changes we had made for 2018/19 were working well. We were therefore able to propose minimum change for 2019/20 (consistent with our general approach of keeping our rules as stable as possible over a three year period). We were pleased that respondents agreed with this assessment and valued our focus on stability.

The consultation also sought views on how we could reflect the emergence of propositions for commercial consolidation, and suggestions as to how we could improve payment processes to better support levy payers.

There was broad support for our proposed approach to consolidation vehicles – which we have further developed in the light of comments received and through work with the Pensions Regulator and DWP. I am confident we have a robust approach which will allow us to set a risk reflective levy for any commercial consolidators that arise in 2019/20. However, we do recognise our approach will need to develop as the market and regulation take shape.

Responses have also helped us identify some improvements we will make to payment services for next year's invoices and we will continue to explore this area with stakeholders including small and medium enterprises. With a largely stable methodology, we will focus our resources on further improving our service to levy payers.

David Taylor
Executive Director and General Counsel

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1. Introduction and Executive Summary

1.1. Introduction

1.1.1. On 19 September 2018 we published our consultation on the Levy Rules for 2019/20 which closed on 25 October 2018. We received a total of 33 responses. These were considered by the Board in determining the final Levy Rules.

1.1.2. This document summarises the responses we received, our analysis of the issues raised, and conclusions reached.

1.2. The Levy Rules (the Determination) for 2019/20

1.2.1. The Levy Rules that will govern the calculation of the levies for 2019/20, as specified in the Board's Determination under section 175(5) of the Pensions Act 2004, are published alongside this Policy Statement, together with guidance for schemes on how to meet the requirements of the Levy Rules. A list of the documents published is included in section 7.

1.3. The Board's Levy Estimate and the levy parameters

1.3.1. We announced in the Consultation Document that the Board proposed a Levy Scaling Factor ('LSF') of 0.48 and Scheme-based Levy Multiplier of 0.000021. We also announced that the Levy Estimate – the amount we estimated these parameters would raise – was £500 million for 2019/20.

1.3.2. We are now confirming that for 2019/20 we will use the LSF of 0.48, the Scheme-based Levy Multiplier of 0.000021, and the Levy Estimate of £500 million.

1.4. Consolidators/SWOSS

1.4.1. A key focus of the Government's recent White Paper on defined benefit pensions was the emergence of commercial models of pension scheme consolidation. Government is developing new legislation to provide a robust regulatory regime for these vehicles – and published a consultation on 7 December on design of the regime. In parallel, however, we are aware of proposals to launch consolidators within the existing regulatory environment.

1.4.2. How we levy commercial consolidators will be informed by the regulatory regime that is established. However, given the pace with which propositions may come to market we needed to act to ensure we could charge an appropriate levy in the near term. We, therefore, set out in the September consultation document our proposals for charging a levy appropriate to a commercial consolidation vehicle. We are clear that this may only be an interim approach and is likely to need development as the regulations and propositions take shape.

1.4.3. Most stakeholders were supportive of our proposed approach. There was some challenge from those seeking to set up consolidation vehicles, including concern that our approach could lead to excessive levies by comparison to conventional schemes. We do not consider this to be the case and believe our proposals lead to an appropriate risk reflective levy charge. We are therefore retaining the core methodology we set out in September.

1.4.4. However, consultation responses have led us to make some adjustments. Most significantly, we see merit in points made that current risk reduction measures (Type B contingent assets and Asset Backed Contributions (ABCs)) won't support recognition of the buffer funds that are likely to be an integral part of consolidation models. We are therefore taking a principles based approach to the recognition of buffer funds in the 2019/20 levy. This will mean we are able to recognise buffer fund assets in our levy calculations as long as they are held securely and able to be accessed by the scheme itself when required. We have also adjusted some specific elements of our calculation methodology – as set out in section 2.

1.5. The measurement of insolvency risk

1.5.1. We received very few responses that raised points about aspects of the PPF-specific model for insolvency risk (the Experian model). In the light of the substantial changes made for the 2018/19 levy (the start of the third triennium) - which saw a significant shift in levies from small and medium enterprises (SMEs) to larger sponsors - this is a very positive outcome. It strongly supports the findings of our review of the model's performance following the changes, which concluded the model was operating as expected.

1.5.2. There was general support for our intention not to extend the use of the credit model to utilities. We are, therefore, confirming this decision. A change to S&P's processes for calculating Credit Model scores is being made, and section 3 of this statement provides more detail on this.

1.6. Contingent assets

1.6.1. In our consultation we confirmed our proposals for contingent asset recognition in 2019/20 (previously set out in December 2017). Schemes that are seeking levy credit for 2019/20, will need to re-execute those Type A and B contingent assets that include a fixed sum maximum amount element, using the standard form agreements currently available on our website. The re-executed versions must be certified by 31 March 2019 (and hard copies must then reach us by 5pm on 1 April 2019), if they are to be recognised in the levy. Comments we received were generally positive about the efforts we have made to publicise the requirement, and the approach we proposed for schemes.

1.6.2. We also sought feedback on aspects of the testing of guarantor strength which had changed for 2018/19. We set out in section 4 the responses received and lessons learnt from our review of the reports submitted to us.

1.7. Levy payment and longer term plans

1.7.1. We sought views on levy customer service and payment processes – including payment by instalments. From the responses, we have identified changes we will introduce for invoicing in 2019, helping ensure invoices reach the right person as quickly as possible and reviewing (and publicising) our existing policies on payment plans and waiving interest. Beyond this, there were mixed responses in relation to substantive change in our payment processes, particularly any move to more widespread payments by instalment. We will be undertaking further work in this area – particularly with SME levy payers – to understand the extent to which the changes we are making for 2019 address any issues and the case for further change.

1.8. Other

1.8.1. We received a number of comments on other issues in the consultation, for example in response to questions on certifying deficit reduction contributions and block transfers, and our conclusions are set out in section 6.

2. Charging a levy for consolidation vehicles and schemes without a substantive sponsor (SWOSS)

2.1. Summary of consultation proposals

2.1.1. The Government's White Paper on DB pensions indicated an intention to bring forward policies to support and encourage the consolidation of DB schemes. A consultation on the regulatory regime was published on 7 December 2018, alongside which TPR issued Guidance for Superfunds, which is designed to set out the issues TPR will consider and the information that may be required to support clearance applications / authorisation. We encourage stakeholders to engage with the DWP consultation on the regulatory framework.

2.1.2. Reflecting that consolidation vehicles may emerge within the existing regulatory framework – in respect of which we may need to charge a levy in 2019/20 – we consulted on a proposed levy approach.

2.1.3. Our proposed levy rule for consolidators was based on our existing methodology for schemes without a substantive sponsor (SWOSS) with some adjustments to reflect the particular characteristics of consolidators and to ensure there is no cross subsidy from existing levy payers. We proposed to:

- Increase the levy for a consolidator in the (perhaps unlikely) event that there is no requirement for the arrangement to wind-up if funding falls below a minimum threshold.
- Implement asset stresses and a recalculation mechanism to reflect respectively the risks associated with profit extraction and new transfers in.
- Put in place appropriately prudent assumptions for consolidators if they do not provide key information (particularly valuations) at the required frequency.
- Recognise risk reduction measures (currently excluded from recognition for SWOSS) provided they fell within existing levy rules, and made use of PPF standard form agreements.

2.1.4. For both consolidators and other SWOSS we proposed to: ensure the impact of the levy on assets is reflected in the calculation; make no assumption of assets out-performing liabilities (by using a variant of the Black-Scholes formula - the Garman-Kohlhagen formula - as suggested to us in a previous consultation), and reflect the impact of any expected increases in liabilities for existing members over the year for which the levy is charged.

2.1.5. We have developed our policy as a result of formal and informal consultation and engagement with DWP and TPR.

2.2. Consultation responses – overview

2.2.1. We received 22 responses which covered the issues we set out in relation to a levy for consolidators and other SWOSS. Most responses focused on the specific questions that we asked – although some made more general points. Overall, respondents supported our proposed approach. However, three responses from entities seeking to establish commercial consolidators raised a range of points. In particular, two of the three argued that we should not be charging a levy based on the Black-Scholes methodology, because – in their view – this approach would lead to a disproportionately high charge.

2.2.2. We also received a small number of responses whose main purpose was to express concerns about the risks posed by the commercial consolidation model – either because of the introduction of commercial incentives or of the reduction in certainty of paying benefits relative to securing them through buy-out.

2.2.3. A number of the responses didn't explicitly address the broader subject of whether our option pricing approach was appropriate. However the authors engaged with the questions asked in a way that implied they agreed with the broad thrust of using option pricing, which had been extensively trailed in advance of formal consultation. This is consistent with our broader informal engagement, in which most stakeholders were supportive of the approach.

2.3. Use of Black-Scholes Methodology

2.3.1. Concerns about the use of the SWOSS methodology (based on the Black-Scholes formula) fell into three categories.

i) A view that the Black-Scholes formula was unnecessary for commercial consolidators and that we should be calculating levies based on our levy rules for conventional schemes. This was based on consolidators having a legal entity that was an employer and was capitalised, meaning – it was argued – it had more value than some "standard" employers;

ii) That the methodology didn't recognise the improvement in security that could be delivered as schemes transfer into consolidators; and

iii) That the levy charge resulting from our proposals would be disproportionate including, for example, in comparison to the levy that would be charged on a band 10 employer sponsoring a scheme with the same funding level.

2.3.2. On the first concern, our firm view is that there is a fundamental distinction between a SWOSS or consolidator and a typical eligible scheme. This justifies a different approach to assessing their levy. A consolidation vehicle (or SWOSS) only requires a fall in funding (for the scheme, and any associated buffer fund) to result in failure as there is no "real" employer. By comparison, where there is a substantive employer, funding and sponsor insolvency are separate risks. This distinction justifies a levy for consolidators primarily focussed on funding and recognising that solvency of the insubstantive "employer" is a function of funding not an independent risk.

2.3.3. It should be noted that we are not suggesting that a consolidation vehicle will necessarily pose a higher risk than the conventional scheme it replaces, nor are we in any way seeking to charge a high levy in all cases in order to restrict the growth of the consolidation model. Rather, we are simply saying that a different methodology for assessing that risk is required.

2.3.4. On the second point of concern, that the levy methodology would not recognise improvements in security as schemes transfer to a consolidator, we do not believe this to be the case. On the basis of our conversations to date with promoters and our internal modelling we think it likely that consolidators could be sufficiently well funded that they pay little – or even no - risk-based levy on set up. The levy charged could therefore be a substantive reduction on that charged to transferring schemes. This reflects the expectation that significant capital will be injected by both the ceding employer and third party investors providing an overall improvement in security.

2.3.5. Based on that expectation, we have modelled what we consider a reasonable case study: to consider the impact of a marginally under-funded scheme (we assumed 95 per cent funded on a s179 basis) with a typical investment strategy, which post-consolidation had combined scheme and buffer assets of around 115 per cent on a s179 basis[1]. Even if the ceding employer is assumed to be of average insolvency risk for our universe, rather than having poor covenant, the move to a consolidator could be expected to substantially reduce the levy the scheme is charged. The example is included at Appendix A.

2.3.6. On the third point, it is the case that our methodology would impose a higher levy charge on a consolidator than on an identically funded "conventional" scheme with the same investment strategy (even where that employer is considered to have a weak covenant e.g. in band 10). We believe, however, this is appropriate. Even a band 10 employer (an employer with an insolvency risk of 3 per cent or higher) may be able to support a scheme whose funding position deteriorates - indeed many do - but a special purpose vehicle cannot.

2.3.7. A comparison calculation for a conventional employer of average insolvency risk (Band 5) and a consolidation vehicle funded at 105 per cent[2] (and both using an investment strategy similar to the PPF) is shown at Appendix A. At this funding level the consolidator would pay a levy much higher than the conventional scheme, but one which is still less than 0.5 per cent of assets. This reflects that in the event that each scheme's funding fell sufficiently to render it underfunded the consolidation vehicle would be expected to be wound up (and therefore claim on us), whereas the conventional scheme is assessed as having a less than 0.25 per cent risk of insolvency and so triggering a claim.

2.3.8. A particular concern raised was that where the funding of conventional schemes is such that we would charge no risk-based levy, consolidators would still be required to pay a relatively low levy. This essentially reflects that the Black-Scholes methodology provides a more sophisticated approach to assessing funding risk than we apply to other schemes. We believe that is entirely justified because funding risk is the only thing that matters for consolidators (as can be seen in the above example, the risk presented to us of conventional schemes with a surplus on a s179 basis is made even smaller by the presence of a substantive sponsor even where the covenant is weak). We also consider these schemes are a new kind of risk – not envisaged when the pension protection regime was set up – and it is important to charge a

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[1] This is a conservative estimate of likely initial funding for a consolidator expressed in terms of s179 liabilities. Funding could be considerably higher, with a commensurately lower (even nil) risk-based levy.

[2] The suggested trigger for insolvency of the non-substantive employer in the DWP consultation.

fully risk reflective levy so that conventional schemes aren't expected to provide a cross-subsidy.

2.4. Definition of a consolidation vehicle

2.4.1. In the consultation we set out our proposed definition, and invited comments. Most responses were supportive of the proposed definition of commercial consolidators – but a number of comments suggested that we might look at tightening the definition as it could capture other schemes.

2.4.2. We recognised that the definition was drawn quite broadly in the consultation document, and we see the desirability (at least in the medium term) in tightening the definition. However, given the significant uncertainty about how the market in consolidation will develop we think a flexible approach is necessary for now – and we intend to retain the definition as drafted but use the discretion it provides to exclude schemes that we consider ought not to be covered. This will include schemes where the original covenant has not been altered – such as master trust arrangements.

2.4.3. If there are schemes or sponsors that are undertaking activity they think might bring them within the definition, we would encourage them to discuss their plans with TPR and us.

2.5. Buffer funds

2.5.1. Our consultation recognised that a key feature of consolidation proposals being developed is the use of buffer funds, held outside the scheme, but available if funding falls, as a risk reduction tool. Our consultation invited comments on whether it would be appropriate to recognise buffer funds using our standard risk reduction measures, such as Type B contingent assets.

2.5.2. A number of responses (including, but not limited to, those promoting consolidation vehicles) have suggested that our standard contingent assets are unlikely to fit the consolidator model currently developing. They argue that these funds will need to be able to be invested flexibly so that the investment strategy can develop over time and they can respond to market movements. It was argued that our standard form contingent assets would not allow this.

2.5.3. In view of the likely size of buffer funds - relative to scheme assets – and their centrality to the proposition - we are reluctant to exclude their recognition for levy purposes if this can reasonably be avoided. However, we are not attracted to seeking to modify the existing contingent asset standard form arrangements in the short term. Doing so would impact arrangements available to many other schemes – and there would be practical risks in trying to do so given the time available and the prospect that the position in relation to consolidators will continue to develop.

2.5.4. Under the new regulatory regime we expect that each buffer fund structure will be subject to an assessment as part of the authorisation regime, under which TPR will need to assure itself that the buffer is fit for purpose i.e. that it does provide the necessary level of security for the scheme. Given the challenges of fitting consolidators into any standard approach, at least in the early years of development, we think it appropriate to adopt a similar bespoke approach (and it is manageable to do so given limited numbers). We therefore propose to assess each buffer fund proposal on its merits and where we are satisfied about the security of the arrangement, treat their assets as scheme assets for the purpose of the levy.

2.5.5. Under our proposed approach, buffer fund assets would be considered as if they were assets of the scheme – and so, above all, there must be a high degree of certainty that, if needed, the assets would be available to the scheme and that value cannot "leak" from the buffer. Beyond that it is not, primarily, our or TPR's intention to place restrictions on the types of asset that can be held. Rather, our main concern is to ensure that the level of investment risk within the buffer fund (that forms the basis of authorisation) cannot be increased following authorisation without appropriate checks and balances.

2.5.6. How these concerns will be addressed is likely to vary from proposition to proposition. Our rule, therefore, sets out at a high level the requirements for recognition. We then expect to assess proposals against the same key principles that TPR will use in considering propositions[3]. These are that:

- Buffer fund assets cannot be released outside of defined circumstances (e.g in line with a defined profit extraction rule)
- The risks within buffer fund investments cannot be increased after initial assessment without a re-assessment of financial sustainability (through the significant events framework)
- Risk within buffer fund investments cannot be increased after authorisation without TPR confirmation that financial sustainability criteria would continue to be met.
- Changes in buffer fund asset allocation cannot be made without consultation with scheme trustees; and
- There is a robust, legally enforceable mechanism for the assets of the buffer fund to transfer to the scheme if there is a trigger event.

2.5.7. In order to allow an assessment of the extent to which these principles are met, we would expect trustees to obtain (and share with us) advice that tests are met. For example, we might look for a legal opinion regarding limitations on asset release from the buffer / that assets would transfer to the scheme on the occurrence of a trigger event or other appropriate professional opinion on the risk characteristics of the initial investment strategy.

2.5.8. In assessing proposals against these principles we will have regard to the requirements of TPR (and in due course regulations) in relation to buffer funds. We will aim to carry out any assessment required for levy purposes alongside TPR clearance / authorisation activity in order that engagement is as streamlined as possible.

2.5.9. We consider that this principles based approach is most suited to the initial stages of the development of the consolidation model, but we would expect to

[3] Set out in 'Guidance for Superfunds seeking to launch' - published on 7 December 2018

develop the principles over time, and could develop standard forms in future years.

2.5.10. To assess the impact of our proposals in combination, we compared the levy for a consolidation vehicle with a buffer recognised on our principles based approach[4], to a conventional levy on our existing rules (where it is assumed that - as consultees suggest - the buffer is not able to be recognised). In the cases where the consolidator's funding (including buffer) was at likely levels, the levy was lower than the conventional levy, illustrating the importance of a bespoke approach to recognising consolidators and their buffer funds (shown at Appendix A).

2.6. Winding up triggers

2.6.1. We would expect that promoters of consolidation vehicles will put in place arrangements to protect the members of the scheme, and the PPF, in the event of failure of the investment strategy - as envisaged in DWP's consultation. There may be a number of triggers included in the consolidator design – for example limiting the writing of new business or which may provide for transfer of funds from buffer to scheme to protect members. From a levy perspective our interest is in triggers that address scheme failure and act to wind-up the scheme – and critically also the employer (since legislation specifies that it is employer insolvency that triggers an assessment period) - and so limit the potential for further falls in funding after that point.

2.6.2. In our consultation we explored two ways of recognising whether a suitable wind-up trigger is in place – adjusting the strike price used in the calculation, or charging a higher scheme-based levy in the absence of a trigger. Responses were strongly in favour of using an adjustment to the strike price.

2.6.3. We have decided that where a wind-up trigger provides sufficient protection, we would expect to recognise it through setting a strike price for the calculation of the levy at below 100 per cent of s179 liabilities. This will be achieved using the same formula for adjusting s179 labilities as is currently used in the SWOSS appendix.

2.6.4. We intend to do this by setting a rule that provides a discretion for the Board to apply the discount where suitable arrangements are in place, backed by high level principles to guide what would be considered by the Board to be suitable. This will again provide flexibility as arrangements develop. The key principles, which are also set out in TPR's Guidance, include:

- the trigger has to be at a level the Board considers suitable and expressed in relation to PPF liabilities.
- the trigger will need to act automatically.
- that when funding drops below that level then scheme wind-up and the insolvency of the sponsoring employer will be triggered within an acceptable period. (As noted in the DWP consultation, this is likely to require a trigger that acts on the employer directly)

[4] We assumed an investment strategy similar to the PPF, a suitable wind-up trigger and provision of data net of capital extraction (see below).

- the Board considers the rule to be suitably defined and permanent – so any ability to alter the trigger would need to be constrained
- a requirement for adequate monitoring arrangements.

2.6.5. In reaching a view of what is acceptable, the Board will have regard to guidance / requirements from TPR – and at a minimum the wind-up trigger will have to meet any requirements of the regulatory regime.

2.7. Information requirements

2.7.1. We proposed a set of annual information requirements, and the use of prudent assumptions where information that we specify for use in the levy calculation is not available. There was widespread support for this in principle, though one response suggested that if the consolidator has liabilities below £1.5 billion there would be a case to ensure the information requirements are proportionate.

2.7.2. Our view is that the additional information that we propose to require should not be disproportionate for a consolidator scheme – not least since such a scheme will need to have a good understanding of its investment risk to operate – and as our approach on investment risk uses standard industry measures. We therefore intend to implement the information requirements as proposed.

2.8. Profit extraction

2.8.1. We set out a potential approach to dealing with the possibility that assets reported alongside an s179 valuation at the start of a levy year are removed in accordance with arrangements for distributing surplus capital to investors. It was never our intention that this approach would charge in relation to the long-term possibility of assets being paid to investors – since the levy is charged annually – only the 'in-year' effect.

2.8.2. We consider that there is a straightforward way for a consolidation vehicle that does aim to return assets to investors before liabilities are discharged to avoid paying a higher levy as a result of our rule. This would be for profit extraction only to be allowed at a fixed point in the year and for the s179 valuation supplied each year to be net of profit that is available for payment to the investors. Our rule will allow for a consolidation vehicle that supplies valuation information net of profit extraction possible in the levy year to be treated as having no capacity to extract profit.

2.9. Adjustments to the existing SWOSS methodology

2.9.1. We received very limited comments on our proposals for adjustments to the existing methodology.

2.9.2. We received a few comments which argued that our proposal to use an iterative approach to calculation could lead to significant levy increases which would potentially lead to scheme failure. An iterative approach is appropriate because the scheme pays the levy out of its own assets rather than (for a conventional scheme) there being a sponsor which can contribute to the costs of the scheme including the levy. As a result, for a SWOSS the act of paying the levy makes the scheme a higher risk than when that levy was calculated.

2.9.3. At the levels of funding at which we are led to believe consolidation vehicles are to be established, adjusting scheme funding iteratively to remove the levy makes a negligible difference to the levy charged. However, if funding is markedly lower the impact can be larger – and as we noted in September the calculation may not converge to a finite higher levy. We have looked further at this and conclude that the point at which convergence does not occur is around 94 per cent of s179 liabilities – markedly below the level we expect the regulatory regime to require wind-up triggers to be set. In other words, where the iterative approach does not converge, consolidators pose an unacceptable risk to their members and PPF levy payers and would not be permitted to run. Thus we are retaining this iterative approach.

2.9.4. We also received a handful of comments on our proposal to reflect the impact of any expected increases in liabilities for existing members (sometimes referred to as 'PPF drift'). It was argued that this potential for liabilities to increase also applied to conventional schemes (though for conventional schemes further employer contributions may counteract the impact). In addition we have found that, in practice such changes can be offset by factors such as the tendency for members to take lump sums, which would not be recognised in our proposed methodology. It is also unlikely that the proposal as consulted on would materially affect levies when consolidators are set up, given their likely initial funding, but it would increase the complexity of assessing liabilities.

2.9.5. We have therefore decided not to include any estimate of the increase in liabilities over the year in our levy methodology for 2019/20, though we may introduce such an adjustment in a later year.

3. Insolvency Risk

3.1. Introduction and summary of responses

3.1.1. We introduced several changes to the calculation of insolvency risk for the start of the third triennium (levy year 2018/19). These were:

- rebuilding five of the eight scorecards used in the PPF-specific model that Experian use to score most scheme sponsors.
- using public credit ratings where employers have them, and the S&P Credit Model for regulated banks, building societies and insurance providers.
- The identification of a small group of employers who, if they met certain criteria, could apply to be confirmed as Special Category Employers.

3.1.2. For 2019/20 we consulted on whether the credit model should be extended to utilities – setting out our view that this was not merited.

3.1.3. 15 responses commented on our insolvency risk methodology, most of which covered whether we should extend the use of the S&P Credit Model.

3.1.4. Although we did not specifically ask stakeholders to comment on the performance of the model overall, the small number of responses on specific elements of the model is notable. Allied to our early assessment of the model's performance (included in the consultation document) we are therefore confident that the model remains fit for purpose.

3.2. Use of the S&P Credit Model

3.2.1. All responses on whether to extend use of the S&P Credit Model to regulated utilities agreed that we should not. We will not therefore change the scope of employers scored by the S&P Credit Model.

3.2.2. Although it is not a policy change, we wanted to take this opportunity to make stakeholders aware of a change to the S&P Credit Model that is expected to take effect for scores generated in 2019/20 (and so affecting levies in 2020/21). This change stems from S&P's annual validation of their model. The results, published in 2018, confirm that for the insurance sub model, performance is very good. For the banks sub model, a bias of one notch has been detected. In other words, the banks sub model generates scores that are on average 1 notch better than the S&P Global Ratings, for rated banks. S&P is expected to recalibrate the banks sub-model as of March 2019.

3.2.3. When the recalibrated model goes live it is likely to result in a worsening in letter grade scores of one notch for most banks / building societies scored by the Credit Model. PPF will apply the recalibrated banks sub-model as of the date of introduction. If the recalibrated model is not introduced by April 2019 we plan to backdate scores for April 2019 and later months once it is introduced (the draft 2020/21 rules would include any amendment).

3.2.4. For completeness it is intended that the "What-If-Tool" will also be run on the basis of the recalibrated model as of the date of introduction.

3.3. Comments on variables used in the PPF-specific Model

3.3.1. It was notable that in this year's consultation we received few responses relating to the Experian model generally or to specific scorecards or variables.

3.3.2. Inevitably, in a statistically based model that investigates correlation and not causation, and is applied across over 14,000 employers, there is a limit to the extent to which we can reflect circumstances that may only apply to small numbers of employers. However, we do investigate the concerns of those with unusual circumstances, and make changes if there is evidence to support doing so.

3.3.3. This year, we received three comments about the log creditor days variable, which is based on the ratio of trade creditors to turnover[5].

3.3.4. One response asked about the different scoring between employers on "Scorecard 2 – Non-Subsidiaries <£30m" with a small balance of trade creditors compared with those reporting zero. The evidence shows that those reporting zero creditor days have an insolvency experience almost three and a half times higher than those with a small trade creditor balance relative to turnover. We concluded it is appropriate for the model to distinguish those with small balances and those reporting zero.

3.3.5. We received two submissions that argued that, for businesses operating on a commission basis, accounting standards could lead to an inflation of the log creditor days ratio (and hence worsen their score). For such a business, accounts turnover is limited to commissions earned while trade creditors reflect the total value of the transactions. It was argued that it would be better if the total value of the transactions on which commission was earned is treated as turnover for the purpose of the model's calculations.

3.3.6. There are a number of reasons not to adjust the figures used. First, it would mean departing from the treatment expected in accounting standards.

3.3.7. Secondly the variables in a credit scoring model work together. So, one should not look at a variable in isolation without considering interaction with or impact on other variables. In this case, the requirement to capture balances held for customers in trade creditors will mean that other variables are increased which tend to improve the score (e.g. total assets).

3.3.8. Thirdly we use the PPF-specific model to score most of the employers that sponsor defined benefit pension schemes. Within each industry or micro-segment of this universe there are insufficient data points (i.e. employers and/or insolvencies) to produce a statistically driven model. The PPF-specific model therefore was developed taking substantial segments of the population together and as a consequence is unlikely to be able to capture all the unique characteristics of each micro-segment or business.

3.3.9. A final consideration specific to the log creditor days variable is that its raw value (before log transformation) is capped at 365 days. This mitigates the impact of outliers. We investigated the level at which the cap is set. The distribution of values for this variable means a cap at 365 days affects around 5 per cent of employers scored, which we consider a reasonable definition for an outlier. Capping the variable at a lower level could increase the proportion of employers affected materially, and ought in principle to be taken account of

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[5] Strictly, it is the log of ((trade creditors divided by turnover) multiplied by 365).

in designing the coefficients used for all of those scored on the variable. This is the sort of change that we think is most appropriately considered when we are rebuilding a scorecard. Accordingly, we consider the points stakeholders have made as ones that we should take into account when reviewing whether a rebuild is necessary (which we will next be doing for the period beginning 2021/22).

3.3.10. Accordingly, we have not changed the log creditor days variable for 2019/20.

3.4. Trend variables

3.4.1. One stakeholder questioned an "unknown" score being assigned to a trend variable when an employer moved from filing consolidated to non-consolidated accounts (where all consolidated group companies, other than the employer, were dormant). Companies House define a company as dormant if there have been no 'significant' transactions in the financial year.

3.4.2. It was suggested that consolidated accounts, that only include dormant subsidiaries, and non-consolidated accounts for the top company alone may record the same value for profit and loss variables. In such a scenario it was argued that trend variables could be calculated despite the different types of accounts in the comparator years.

3.4.3. We have considered this request and concluded that where there are change variables, and where both types of accounts are recording an identical value for the past year (N-3) because any subsidiary companies consolidated are dormant, schemes can notify Experian by 31 March 2019 and if accepted Experian will override any "unknown" scores previously calculated.

3.4.4. Where it is clear in the relevant accounts that the status of any subsidiaries is dormant and that the variable values are identical on a consolidated or non-consolidated basis this can be done by the employer notifying Experian (enclosing suitably marked up accounts). Where it is not clear, the employer's auditor will need to provide confirmation of these requirements.

3.5. Guaranteed Minimum Pensions (GMPs) equalisation and insolvency risk scores

3.5.1. The Lloyds High Court ruling on 26th October 2018[6] concerning GMP equalisation will mean that some scheme employers may need to make accounting adjustments to reflect higher scheme liabilities at the next opportunity. In turn this could lead to a worsening in insolvency risk scores (particularly, for example, if it is sufficient to change a period of profitability into a loss). We are aware of estimates that this could increase scheme liabilities by between 0.5 per cent and 4 per cent - and on average by around 2 per cent.

3.5.2. We have been asked whether we would be willing to allow an adjustment to avoid a worsening in score for affected employers. Considering whether the ruling results in material changes to the calculation of insolvency risk scores

[6] *Lloyds Banking Group Pensions Trustees Limited v Lloyds Bank PLC and others* [2018] EWHC 2839 (Ch) available at http://www.bailii.org/ew/cases/EWHC/Ch/2018/2839.html

we start from the position that using financial data as reported provides a better view of a company's financial health and renders different companies' accounts more comparable.

3.5.3. We do not believe that allowing an adjustment for the impact of this decision would be appropriate. The ruling effectively confirms a liability that the scheme (and its sponsoring employer) has. It could be argued that the scoring of the employer in the past (excluding these liabilities) was too generous and understated its insolvency risk.

3.5.4. Taking this into consideration we will not adjust data items where an employer makes an accounting adjustment for GMP equalisation.

3.5.5. Please see section 6.4 below in relation to our approach to s179 valuation guidance and this case.

3.6. Impact of PPF levy on insolvency experience

3.6.1. One response asked if there was a link between the PPF Levy charged and the subsequent insolvency of scheme employers – i.e. is the levy itself a material contributor to employer insolvency? We have reviewed the most up to date evidence which re-affirms our view that it is not.

3.6.2. As part of our review of the performance of the PPF-specific model, we reviewed, where available, the statement of administrator's proposals for the insolvencies that we are notified of by Insolvency Event Notices (Section 120 notices). These statements, which are published on the Companies House website, summarise the events leading up to the insolvency. Where there was not a statement we examined published annual accounts.

3.6.3. For the period April 2017 to March 2018 we investigated the insolvency of 42 companies and in 21 cases we identified explanations of the cause(s). None identified the levy as a cause. The five key insolvency drivers listed were:

- Decline in revenues (e.g. due to challenging trading environment, loss of funding)
- Loss making
- Less favourable credit conditions (e.g. loss of trade credit insurance)
- Overstatement of accounts (e.g. due to fraud, irrecoverable debtors)
- Accounting changes (i.e. recognition of the pension deficit)

3.6.4. In two cases the pension fund deficit was referenced – as the company had been required to disclose the pension scheme liability. In one instance this had resulted in the company losing various funding opportunities.

3.6.5. The absence of any suggestion that the levy has been a cause of insolvency is consistent with an exercise we carried out into insolvencies over the period April 2015 – March 2016. That exercise looked at insolvent sponsors assigned a levy band of 5 or better. In four of the five cases, all of which were charities, there was a material decrease in revenues over a relatively short time period, typically related to loss of (government) contracts.

3.7. Special Category Employers

3.7.1. This was a new rule introduced last year. The Consultation for 2019/20 proposed a rule so that employers granted Special Category Employer ("SCE") status for 2018/19 would remain so classified provided that they complete certain confirmation requirements. Two responses argued it was unlikely that employers would change their status. There is a balance to be struck between certainty and bureaucracy and we felt that an annual confirmation (as opposed to a new certification) was a good compromise.

3.7.2. We plan to contact employers with SCE status (for example in January each year), asking for confirmation that no change in the entity's circumstances has taken place and the certificate is still valid.

4. Contingent Assets

4.1. Introduction

4.1.1. In our consultation we focused on two aspects of our approach for contingent assets:

- A requirement to re-execute Type A and B contingent assets with fixed cap elements – in line with the policy set out in our Policy Statement of December 2017 – and what we could do to support that effort.
- Reflecting on the introduction in 2018/19 of a requirement for a report to support certification of Type A guarantees, and whether there is additional guidance we should give on this process.

4.1.2. We have decided to allow hard copy documents supporting contingent assets to be sent to our Croydon office by 5pm on Monday 1st April 2019. The deadline for online actions remains at midnight on 31st March 2019. Please be aware that everything must be completed before the online certifications can be made.

4.2. Re-execution of contingent assets for 2019/20

4.2.1. In the 2018/19 Policy Statement, published in December 2017, we explained that we intended to require schemes with Type A and B contingent assets including a fixed cap element to re-execute them on the revised standard forms (published in January 2018) in order to be recognised in the levy calculations for 2019/20.

4.2.2. We have therefore throughout 2018 been encouraging re-execution where this will be required to allow schemes to continue to benefit from levy recognition. This has been done in a number of ways (for example in an e-mail to all schemes that have certified a contingent asset in the past five years and a short video on our website). We confirmed these proposed requirements in the consultation in September.

4.2.3. The 2019/20 Levy Rules provide that schemes with Type A and B contingent assets entered into before 18 January 2018 that include a fixed sum maximum amount element (including those with a 'lower of' formula) must re-execute onto the standard forms from January 2018 if they wish to obtain levy credit (referred to as the "Re-execution Requirement"). We are pleased to hear the positive feedback on guidance issued so far. We are planning further communications as we move into 2019.

4.2.4. Given the previous communications, by now we anticipate that all schemes who are intending to seek levy credit for Type A and B contingent assets will have established whether the Re-execution Requirement applies to them and we strongly encourage them to plan ahead.

4.2.5. Responses commented on how best to manage the surrounding requirements (e.g. blacklines, legal opinion, guarantor strength reports or other value tests) in regard to re-executed contingent assets (in order to comply with the Re-execution Requirement), and most were supportive of our view of the requirements being broadly the same as if the contingent assets were 'new'.

In particular stakeholders noted the need to be mindful of the complexity and difficulties for schemes that would result if we were to establish another set of contingent asset requirements specifically in relation to the Re-execution Requirements. That said, one respondent did ask whether we would accept 'refresher' legal opinions.

4.2.6. We have decided that schemes will need to meet the 'new' contingent asset requirements when moving across to the new standard forms for Type A and Bs for re-execution purposes for 2019/20. However, we will accept 'refresher' legal opinions and guarantor strength reports in certain circumstances, but the legal opinion and guarantor strength report should be complete and up-to-date by reference to the 2019/20 requirements.

4.2.7. However, the hard copy supporting documents must be full and complete, and so schemes must append any prior opinion or report that they update in this way. We do not have a separate set of requirements for 'refresher' reports – both the guarantor strength report requirements and the legal opinion requirements have to be met in the usual way – and so the adviser will need to be able to make the same judgments (and owe the same duty of care to us).

4.2.8. Some stakeholders made helpful practical points in relation to managing re-execution, particularly in relation to the Type B(ii)(security over property). One response noted that their Type B(ii) may need to be released early (for 2018/19 levy purposes) in order to ensure the timings in relation to the new contingent asset are met (e.g. managing Land Registry practicalities). Where there are no other changes other than the move to the new standard form, we are supportive of this in principle (and we would not expect to change the 2018/19 levy in these circumstances). But we ask that schemes contact us in the usual way for all 2018/19 midyear changes (see Rule G3 of the 2018/19 Determination).

4.3. Drafting comments received on the new standard forms

4.3.1. We are pleased to see that a number of stakeholders have engaged in detail with the new standard forms we published earlier in the year. The comments we have received in relation to them have been helpful.

4.3.2. After having considered the drafting comments, we do not propose to make any further changes to the standard forms at this stage (as we consulted on these towards the end of 2017).

4.3.3. That said, we remind users of the standard forms that there is a mechanism where the standard form can be varied (found in the Contingent Asset Appendix), if:

- the legal opinion provided to the trustees by the scheme's legal advisers has confirmed that the change does not have a materially detrimental effect on the rights of the trustees as compared to the standard form; and
- we have been notified by 31 March 2019.

4.3.4. We consider it helpful to share some of the drafting comments received. Accordingly, we have noted some of the changes raised with us in the relevant (Type A, B or C) Contingent Asset Guidance. Schemes' legal advisers may wish to consider these when they are using the new standard forms. It will be for schemes and their advisers to consider whether they meet the 'not materially detrimental' test in the Contingent Asset Appendix (as summarised in 4.3.3 above).

4.4. Guarantor strength reports

4.4.1. From 2012/13 onward the Levy Rules have required that for a parental guarantee to be recognised for levy purposes the reduction in levy that would apply must be consistent with the reduction in risk offered. This has been reflected in the certification requirements for trustees and the need for them to satisfy themselves that the guarantors would be able to meet the amount guaranteed in an insolvency situation by certifying the 'realisable recovery' under the contingent asset.

4.4.2. In the light of a disappointing number of rejections due to insufficient evidence of the guarantor's ability to meet the certified amount we introduced a new requirement in the 2018/19 levy year. This was that a guarantor strength report, prepared by a professional adviser, was required to be obtained by scheme trustees prior to certification, where the levy benefit of the PPF accepting the contingent asset is £100,000 or more.

4.4.3. For the 2018/19 Levy year all the guarantor strength reports with a levy saving over £100,000 were reviewed, as well as a sample of those with a levy saving under £100,000.

4.4.4. We have reflected internally on lessons learnt in this first year of externally provided guarantor strength reports and note the following themes which providers of these reports and schemes should take account of (we have updated the Guidance to reflect this):

- We expect the provider of the report to be an independent, external adviser.
- The same requirements, as to the nature of the report, apply whether the levy saving is above or below £100,000. For example, the duty of care is still needed where the levy saving is expected to be under £100,000.
- The duty of care requirements cannot be caveated by reference to any separate terms between the adviser and the trustee.
- Advisers should make sure there is clarity over the basis of assumptions used in creation of the reports.

4.4.5. In addition, we would draw advisers' attention to the approach expected where a guarantor, which is also an employer, is expected to cease trading in the circumstances a guarantee may be called - as set out in paragraph 5.1.7 of the Guidance. Although the approach expected is not new to 2018/19, a number of reports were rejected due to the advisers misinterpreting the expectation that the guarantor should be able to meet all its own obligations to the scheme, as well as the realisable recovery under the guarantee. Some analyses expected that only a part of the section 75 debt need be met – with the result that the return to the guarantee was in part serving to reduce the proportion of the section 75 debt met by the guarantor.

5. Customer services

5.1. Developing improved customer services

5.1.1. Identifying ways to improve the service we provide to levy payers and their advisers will remain an area of ongoing focus. We are undertaking customer insight work and establishing a forum for SMEs to ensure we fully understand what improvements would be most effective and valued.

5.1.2. We have identified a number of short term actions – which we will take forward - and potential longer term options where we will need to gather evidence and fully assess the case for development.

5.2. Levy Payments

5.2.1. In the consultation we asked a number of questions about how we might help schemes (especially SMEs) plan for and manage payment of the levy. We received fifteen responses on this group of questions.

5.2.2. In response to our question about how we could help schemes plan for the levy there were a range of suggestions. These included requests for improved guidance – on issues such as when invoices were expected to be issued and sample calculations on our website.

5.2.3. We received a number of different views on the desirability and form of providing bill estimates. Some respondents thought those without advisers (particularly SMEs) would benefit particularly from additional information. Some thought that simple 'rule of thumb' calculators should be developed while others suggested more sophisticated and accurate tools/estimates were needed. At the same time, a few argued that this should not be a priority for us – as estimates are available from advisers.

5.2.4. Turning to the issue of payment once the invoice has been issued some respondents stressed the importance of ensuring that the invoices are sent to the most appropriate person – which might vary from scheme to scheme. It was noted that where the invoice does not go directly to the responsible person, the 28 days allowed for payment could become challenging. We use the address provided by the scheme, and below we explain how schemes can ensure the invoice goes to the most appropriate person. We were also asked if we could set out when to expect an invoice.

5.2.5. There were mixed views on whether payment by instalments should be allowed or become standard. A small number of responses argued for an extension of payment by instalments, with a particular focus on SME employers. Conversely, other responses were concerned by the potential added complexity and noted that the costs of administering would ultimately be borne by levy payers as a whole. Those supporting included two of the five responses from SMEs (the others didn't comment on it within their responses). In a few cases those supporting payment by instalments suggested limiting it to schemes experiencing a significant levy increase compared to the previous year.

5.2.6. Some responses felt that the current arrangements, where schemes finding it difficult to pay their levy in full within the standard payment terms, can request a payment plan, worked well and should be maintained.

5.2.7. One area that was questioned was the interest rate charged on late payment. This is set by legislation at 5 per cent above the Bank of England (BoE) base rate[7]. The current HMRC rate of 3.5 per cent was highlighted as a lower rate, but equally statutory interest on late payment of commercial debts is 8 per cent above the BoE base rate.

5.2.8. Since the introduction of interest on late payment, the average time taken by schemes to pay has reduced from 34 days to 24 days. As most schemes have always paid on time, a significant part of this reduction is a reflection of the small minority that consistently paid very late now paying on time. In practice interest is only applied in relatively rare cases – around 3 per cent of schemes and a total value which is immaterial in PPF funding terms[8]. However, it does assist in encouraging schemes to pay promptly –and so any change should be considered in the light of any impact it could have in that respect but is ultimately a decision for Government.

5.2.9. While the rate of interest is outside our control, the legislation does allow us to waive interest in certain circumstances. Below we explain that as part of increasing awareness of the circumstances when schemes can request a payment plan we will provide information about the types of issues we consider when deciding whether to waive interest.

5.3. Immediate actions

5.3.1. Drawing on consultation responses, we have identified the following areas where we believe we can make improvements in the short term.

5.3.2. Ahead of invoicing for the 2019/20 levy year, we will review and publish the criteria we plan to use to assess whether a payment plan should be agreed to; and also the factors that may allow us to decide to waive the interest on payments within a payment plan. In doing so we will of course be bound by the terms of the existing legislation. This means for example we cannot automatically allow payment plans or waive interest in pre-defined circumstances. Instead, we must consider each case put to us on its own merits. Nonetheless, we will be aiming to reassure schemes facing genuine difficulties in paying their levy that payment plans are available to them, and providing increased clarity on the circumstances in which we may waive interest.

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[7] Regulation 19A(4) of The Pension Protection Fund (General and Miscellaneous Amendments) Regulations 2006, as inserted by Regulation 5 of The Pension Protection Fund (Miscellaneous Amendments) Regulations 2010

[8] Since its introduction in 2010 we have collected less than £2m in interest charges - by comparison with c£5 billion of pension protection levy

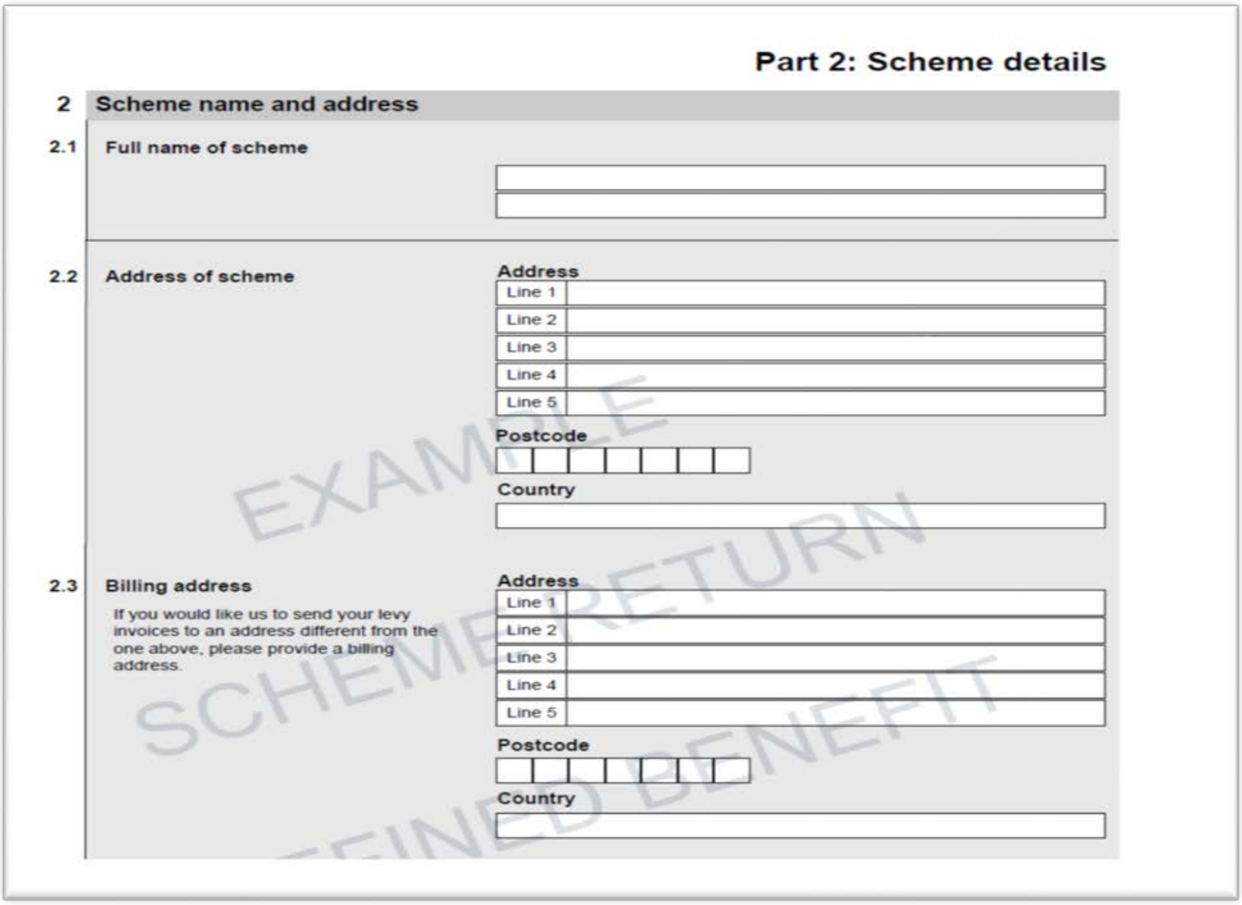
When can a scheme apply for a payment plan?

If a scheme believes it will have difficulty paying its levy within 28 days please e-mail our credit control team at creditcontrol@ppf.gsi.gov.uk as early as possible after receipt of the invoice.

The request for a payment plan should explain the reasons it is sought, any evidence to support this, and a proposal for payment of the levy.

5.3.3. We also want to help schemes ensure their levy invoice goes to the address they want it to. We are aware from the number of requests we receive for duplicate invoices and other feedback that there may be confusion about how the invoice address is chosen. We use the address provided by the scheme on the Pensions Regulator’s Exchange system: sending invoices either to the scheme address entered there or – if the scheme provides one - their billing address. The billing address is an optional field and at present only around 15 per cent of schemes use this option. (Note: we don’t use the levy contact field, which is used for TPR communications for both DC and DB schemes, since this field could be completed without the scheme wishing the invoice to be sent there).

Screenshot: Extract of Scheme return capturing billing address



Part 2: Scheme details

2 Scheme name and address

2.1 Full name of scheme

2.2 Address of scheme

Address
Line 1
Line 2
Line 3
Line 4
Line 5
Postcode
Country

2.3 Billing address

If you would like us to send your levy invoices to an address different from the one above, please provide a billing address.

Address
Line 1
Line 2
Line 3
Line 4
Line 5
Postcode
Country

5.3.4. We will provide additional information on the expected timing of invoices, the order in which we invoice and reasons why invoices might be delayed, on our website ahead of the start of invoicing. Broadly, we aim to invoice from early September, and invoice larger sums first – though we will aim to batch related schemes together. We will also consider additional information we can provide when elements of the levy calculation change and more 'how to' guides.

5.4. Longer term

5.4.1. We will use customer insight and our new SME forum to better understand the scope, costs and benefits of a range of customer service improvements. We have received a range of suggestions - reflecting that different groups of levy payers may have different needs and preferred solutions. Some suggestions focused on help with understanding particular parts of the levy calculation – for example insolvency risk or underfunding - and that we consider the use of sample calculations/tools. Others requested information/tools that provided an estimate of expected levy ahead of the invoice being issued – with varying views on how accurate this needed to be (bearing in mind all the data used in the calculation may not be available until the end of June each year).

5.4.2. We will therefore consider a range of types of information that we might be able to offer, what form it would take, and if we do seek to develop estimates how precise they would be, who would be able to receive them, and when they would be available.

5.4.3. We will also investigate the possibility of introducing electronic invoices and a wider range of payment methods.

5.4.4. When we have completed these reviews and introduced the most effective measures, we will reconsider whether our additional transparency around payment plans and improvements in understanding about the amount and timing of invoices has been sufficient for those who have supported payment by instalments.

5.4.5. More broadly, we expect to develop proposals for the levy in the years from 2021/22 onward, following the procurement of an insolvency risk services provider for that period.

6. Other changes

6.1. Deficit-Reduction Contributions (DRCs)

6.1.1. Our consultation document asked for suggestions as to how we could increase scheme awareness and take-up of our DRC regime (both Option Alpha and Option Beta where applicable). Several respondents made very helpful suggestions, including bulk emails (either to all schemes or to a targeted population), a webinar and providing a simple Option Beta calculation spreadsheet on our website. We will take forward these suggestions with a view to implementing some or all of them in the run-up to the DRC certification deadline for levy year 2019/20.

6.1.2. Our consultation document also set out a number of clarifications to the DRC rules and guidance under the new certification options introduced for the third levy triennium. We also asked for views on the treatment of Pension Increase Exchange (PIE) options exercisable at retirement under scheme rules (whereby members have the option to exchange future increases for a higher initial pension), and in particular, whether the exercise of such options should be treated as augmentations under our Option Alpha methodology.

6.1.3. Five respondents advocated that such PIE options should not be treated as augmentations, citing various reasons such as inconsistency with the treatment of other member options and disproportionate calculation complexity. Two respondents were of the view that individual PIE options technically constituted augmentations, although one made the caveat that treating them as such could discourage DRC certifications.

6.1.4. We are persuaded by the arguments against treating such options as augmentations, provided the option is to be exercised on a member by member basis at retirement. We have added a sentence to the DRC Guidance to clarify this.

6.1.5. However, we will monitor experience in this area and may reconsider the treatment of individual PIE options when we next review levy parameters more widely, particularly if their availability and uptake become more prevalent.

6.1.6. We also received responses from three stakeholders regarding our clarification of the exclusion of investment expenses and corresponding contributions under Option Alpha. These respondents commented that many investment expenses have no clearly identifiable or ‘matching’ contributions and that in many cases it entails significant effort to isolate and exclude the element of contributions related to investment expenses, for example if the contribution loading is implicit through a reduction in the valuation discount rate.

6.1.7. Our policy intention is that the DRC regime should provide a proportionate means of recognising contributions made between s179 valuations, without entailing arduous calculations for schemes and their advisers. Consequently, we have amended the DRC Appendix and Guidance to clarify that there is no requirement under Option Alpha to identify and exclude any element of contributions in respect of investment expenses when determining the certified DRC amount (and, as already applies, there is no requirement to identify and deduct the actual investment expenses themselves). Although this approach is theoretically ‘over-generous’ (because the relevant element of contributions is recognised but the corresponding expense is not), we are satisfied that it is commensurate with our policy aims and the overall simplifications and approximations necessary to achieve them.

6.2. Block Transfers

6.2.1. We received support for the recent developments in this area including the development of Exempt Transfers, and encouragement to go further in seeking improvements to the ways in which information can be provided following all types of Full Transfer (whether Exempt or not).

6.2.2. We will provide an application form on our website which should be used if a scheme is requesting that a transfer is treated as an Exempt Transfer. The application should be sent to the PPF by 30 April 2019.

6.2.3. We understand that there can sometimes be practical difficulties with certifying contingent assets and deficit reduction certificates on Exchange for Full Transfers and we would encourage schemes to contact us as soon as possible, ahead of the deadlines for submission, if experiencing difficulties, in order to discuss alternative means of certifying (for example by hard copy). We have included fields requesting information on any contingent assets, deficit reduction contributions and asset backed contributions that credit is being sought for within the Exempt Transfer application form.

6.2.4. The Parent Scheme in a self-segregation Exempt Transfer will need to be able to confirm that re-execution and certification of contingent assets as new has taken place on the 2018 standard forms where relevant (see section 4).

6.2.5. We will continue to work with TPR to seek improvements to Exchange functionality for future years. As we explained in the consultation document, where it is not possible to enter data for the receiving scheme on Exchange (for example because the first set of audited accounts have not been produced by 31 March) we are likely to be able to accept asset and liability data provided it is prepared in accordance with s179 valuation guidance principles – i.e. not understating the value of protected liabilities or overstating the assets.

6.3. Brexit

6.3.1. We received nine responses to our question about issues that we should consider in relation to Britain's exit from the European Union. Responses highlighted the uncertainty and potentially negative economic effects, but no suggestions were made of specific legal changes that were needed to ensure existing levy arrangements still operate.

6.4. s179 guidance

6.4.1. We have received requests for guidance on whether and how the outcome of some significant court cases (Hampshire, Beaton and Lloyds) should be reflected in s 179 valuations.

6.4.2. We have published some initial FAQs indicating how we expect these decisions to have an impact on s179 valuations and we are considering when to issue further guidance.

6.5. Other

6.5.1. We received some suggestions that will be considered when we next review the levy parameters more widely. These included suggestions that we review the thresholds for Option Beta (DRC certification) and the Bespoke Stress Calculation, and consider recognising longevity swaps as a risk reduction measure.

6.5.2. Two respondents suggested that we adopt the A9 version of the s179 valuation assumptions as the output basis for the levy calculations. We have previously set out that we would see the use of a single set of valuation assumptions within a triennium to be an element of the stability of the rules that schemes favour. We also note that most valuations being used are currently still on the A8 basis. We are not therefore making a change for 2019/20. We have expanded the transformation appendix to permit the use of the A9 assumptions as an input basis.

7. Legal drafting / clarifications

7.1. What we are publishing

7.1.1. The Levy Rules that will govern the calculation of the levies for 2019/20, as specified in the Board's Determination under section 175(5) of the Pensions Act 2004, are published alongside this Policy Statement.

7.1.2. Together with the Levy Rules we have published guidance for schemes on how to meet the requirements of the Levy Rules, and to explain how we expect to make use of the areas where the Levy Rules provide us with flexibility. These are:

- Guidance on Asset Backed Contributions
- Guidance on Bespoke Investment Risk Calculation
- Guidance on Block Transfers
- Guidance on Contingent Assets
- Guidance on Deficit-Reduction Contributions
- Guidance on Officer's Certificates certifying secured charges and certain other matters
- Guidance on Accounting Standard Change Certificate
- Insolvency Risk Guidance

7.1.3. In addition we are publishing with this document Officer's Certificates in connection with ABC certification, FRS 102 certification, and mortgage exclusions: and application forms for Exempt Transfers and for entities seeking to be classified as a Special Category Employer.

7.2. Levy Rules and Appendices – drafting changes

7.2.1. In our September Consultation Document we highlighted a number of additional technical drafting changes that we proposed to make to the Determination and Appendices. Other than points addressed already in this Statement, we received little comment on this these points. We have therefore confirmed these changes.

7.2.2. To take account of the issues discussed earlier in this Statement we have made the following changes:

(a) Inserting references to our new website, www.ppf.co.uk.

(b) Referring to our new 'Data Corrections Principles', now known as 'Seeking changes to data used to calculate the levy: practice and principles' (on our website). This is a principles based document on the types of corrections we consider, factors we look at when considering a correction request and when considering a late request.

(c) Changes in regard to Rule E2.3(8) of the Determination and also paragraphs 3.12 and 4.3(a) and 4.9(3)(a) of the Insolvency Risk Appendix to reflect section 3.4 above (regarding a move from consolidated to non-consolidated accounts).

(d) An extension to the hard copy document submission deadline in Rule A2.3(8) to 1 April 2019 (see section 4.1 above).

(e) Minor or typographical changes.

8. Next steps for schemes and key dates

8.1. Introduction

8.1.1. This chapter outlines next steps and key dates for the calculation of 2019/20 levies. We are confirming the main data submission deadline as midnight on 31 March 2019. Please note we have decided to allow hard copy documents supporting contingent asset online certifications at 31 March 2019 to be delivered to our Croydon office by 5pm on Monday 1 April 2019.

8.2. New certificates and re-certifications

8.2.1. The 2018 contingent asset standard form agreements remain available on our website. We are publishing updated certificates for ABCs, mortgage exclusions, and accounting standard changes. We are also publishing application forms for Special Category Employer status and for Exempt Transfers.

8.3. Key dates

8.3.1. For 2019/20 we will use information from the annual scheme return that is submitted via the Pension Regulator's Exchange system to calculate levies.

8.3.2. The deadline for submission is midnight on 31 March 2019, except as detailed below. The ABC certificate can be found on the PPF website and the Mortgage Exclusion (Officer's) Certificates are available on the PPF website and PPF/Experian portal.

Item	Key dates
Monthly Experian Scores	Between 30 April 2018 and 31 March 2019
Deadline for submission of data **to Experian** to impact on PPF-specific Monthly Scores	One calendar month prior to the Score Measurement Date
Submit scheme returns **on Exchange**	By midnight on 31 March 2019
Reference period over which funding is smoothed	5-year period to 31 March 2019

Item	**Key dates**
Guarantor Strength Reports (where relevant) to be completed and Contingent Asset Certificates to be submitted **on Exchange**	By midnight on 31 March 2019
Contingent Asset hard copy documents where required (including Guarantor Strength Reports) to be posted/delivered **to PPF at** Pension Protection Fund Renaissance 12 Dingwall Road Croydon, Surrey CR0 2NA	By 5pm on 1 April 2019
ABC Certificate to be sent **to PPF by e-mail**	By midnight on 31 March 2019
Mortgage Exclusion (‘Officers’) Certificates and supporting evidence to be sent **to Experian by e-mail**	By midnight on 31 March 2019
Accounting Standard Change certificate **to Experian by e-mail**	By midnight on 31 March 2019
Special category employer applications (and confirmation of no change) **to PPF by e-mail**	By midnight on 31 March 2019
Deficit-Reduction Contributions Certificates to be submitted **on Exchange**	By 5pm on 30 April 2019
Exempt transfer applications with supporting evidence **to PPF by e-mail**	By 5pm on 30 April 2019

Item	Key dates
Certification of full block transfers to be completed **on Exchange** or sent to PPF (in limited circumstances)	By 5pm on 28 June 2019
Invoicing starts	September 2019

APPENDIX A – Use of Black-Scholes methodology

Example 1 - scheme with: an average investment strategy (45% hedging bonds and cash, 35% equities, 10% hedge funds and property, 10% other alternatives, no derivatives).

			Standard Risk-Based Levy	
Assets	Liabilities	Funding Level	Band 5	Band 10
£95m	£100m	95%	£50k	£350k

If it is assumed that post scheme transfer to a consolidation vehicle, the scheme is funded at 115% (including assets held in the buffer fund), then the levy is reduced significantly by reference to a scheme with an average insolvency risk. This assumes the investment strategy of a consolidation vehicle would be closer to the strategy of the PPF[9].

Assets	Liabilities	Funding Level	Consolidator Risk-Based Levy
£115m	£100m	115%	£30k

Example 2 – a comparison of: a conventional employer of average insolvency risk (levy band 5) and a consolidation vehicle both funded at 105% (in the latter case, including the buffer fund).
Case 1 - both with an investment strategy similar to the PPF.
Case 2 – both with a lower risk investment strategy - 85% hedging bonds and cash, 15% hedge funds, derivatives.

Scheme Type	Assets	Liabilities	Funding Level	Risk-Based Levy	% of Assets
Case 1 – Conventional Scheme	£105m	£100m	105%	£0	0.00%
Case 1 – Consolidation Vehicle				£440k	0.42%
Case 2 - Conventional Scheme	£105m	£100m	105%	£0	0.00%
Case 2 – Consolidation Vehicle				£10k	0.01%

[9] For modelling we use a portfolio of 55% hedging bonds and cash, 45% alternative / hybrid assets & derivatives which reflects the risk budget of our strategy but not the strategy itself.

Example 3 – Comparison of standard Risk-Based Levy for a scheme with a conventional employer (with insolvency risk corresponding to levy band 10) excluding a buffer fund equal to 15 per cent of liabilities, with a consolidation vehicle including the buffer fund – both using an investment strategy similar to the PPF.

Assets (excluding / including buffer fund)	Liabilities	Funding level (excluding / including buffer fund)	Standard Risk-Based Levy excluding buffer fund	Consolidator Risk-Based Levy
£90m / £105m	£100m	90% / 105%	£280k	£440k
£95m / £110m	£100m	95% / 110%	£190k	£120k
£100m / £115m	£100m	100% / 115%	£110k	£30k
£105m / £120m	£100m	105% / 120%	£20k	£10k

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