Pension Protection Fund

Consultation document

Levy rules 2023/24

Foreword

Today, we have published the conclusions of our funding strategy review and confirmed our new funding objective. The review reflects our strong financial position and the reduction in the risks we face. Its clear conclusion is that we are now able to move to charging a significantly lower levy without risking our ability to pay member benefits.

We have also been considering what our funding conclusions should mean for our methodology – how we charge the levy. Our expectation that levies will be materially lower in future presents an opportunity to change our methodology to ensure it remains fit for purpose. We believe we should be moving over time to a levy methodology which is simpler, places more weight on underfunding and less on insolvency risk, makes greater use of a scheme-based levy, and differentiates between schemes of very different sizes. We have shared our emerging thinking with our Industry Steering Group, and publicly in Looking at our future funding approach (Kate Jones and Oliver Morley's blog post of 14 July).

This consultation document seeks views on how we plan to change our methodology for 2023/24 to reflect our first steps to a future levy.

We are proposing to collect £200m in 2023/24, a reduction of almost 50% compared with 2022/23. Some of this reduction reflects a fall in scheme risk, but in addition we are taking active steps to reduce levies and to change the distribution of the levy in line with our long-term vision. There are two parts to this.

- First, we are reducing the sensitivity of the levy to changes in insolvency risk by halving the incremental increase between levy bands. This will reduce the volatility of bills and is a first step to enabling a simpler approach to insolvency risk in the levy
- Secondly, we will ensure across the board reductions by reducing the Levy Scaling Factor by 23 per cent and Scheme-based Levy Multiplier by 10 per cent.

This means that almost all schemes are expected to see their levy fall in 2023/24.

We hope this policy package will be welcomed by stakeholders and recognised as a first step toward what we expect will be a lower and simpler levy in the longer term. I am looking forward to hearing stakeholders' views. We will publish our conclusions in due course.

David Taylor
Executive Director and General Counsel

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1. Key proposals

This document sets out our proposals and the underlying analysis for the 2023/24 levy rules. These rules will determine how levy bills to be issued in autumn 2023 will be calculated. The headline proposals are:

The Board's Levy Estimate, policy and levy parameters

- We intend to set the Levy Estimate at £200 million, a reduction of £190 million on 2022/23.
- Consistent with our long-term intention to reduce the sensitivity of levies to insolvency risk, we have changed the levy rates for levy bands 2 to 10, halving the band-to-band increase in levy rate.
- The Levy Scaling Factor ('LSF') will be set at 0.37 (2022/23 comparator 0.48) reducing risk-based levies by 23 per cent other things being equal.
- Scheme-Based Levy Multiplier ('SLM') to change to 0.000019 (2022/23 comparator 0.000021) a 10 per cent reduction.
- The risk-based levy cap to remain at 0.25 per cent of scheme liabilities.
- As previously indicated, the limit on increases in levy from the prior year (the 2022/23 adjustment) will not be continued.

More about our analysis and rationale for decisions, along with information about other subjects under consultation can be found in the following sections of this consultation document.

Our policy framework considering our funding strategy review

2. Implications of the funding strategy for how we charge a levy

2.1. Context

2.1.1. Our Funding Strategy establishes a framework for deciding the amount of levy that we need to collect. As of 31 March 2022, we had reserves of £11.7 billion. Our current level of reserves mean that funding is close to what we expect to need to meet the Financial Resilience test and we are now able to take active steps to bring the levy we charge down. Our funding position relative to the Financial Resilience test may vary from year to year (for example our funding declined in the year to March 2020 and may do again in the future). However, our central expectation is that - on balance - and over time our funding will improve further. Given this, we believe it is appropriate to significantly reduce the rate at which we collect levy, while at the same time ensuring that we can charge a higher levy if needed.

2.1.2. We appreciate the desire for stability and predictability within the levy and therefore we will endeavour to avoid adjusting our strategy based on short term volatility in our funding unless we see a material deterioration in our financial resilience.

2.1.3. Our expectations about the role of levy over the coming years – and the potential evolution of risk in our universe – have significant implications for how we charge the levy as well as the level at which it is charged. A key point to consider is whether an approach that is fit for purpose at present – and enjoys general stakeholder support – remains the best fit when the levy that we are charging is expected to be of a different magnitude.

2.1.4. Moving to a new purpose for the levy therefore presents an opportunity to re-think our levy methodology. In doing so, we have aimed to look over a multi-year period, recognising that, for example, there may be a case for a levy design that requires legislative change. We are aiming to ensure that changes made in the short-term are consistent with that direction of travel – so that, for example, we can ensure that steps to reduce the overall amount we collect and to change the distribution of the levy are integrated – so as not to unnecessarily cause volatility.

2.2. How is our levy charged now and the challenges this brings

2.2.1. We have charged a pension protection levy since the second year of operation of the PPF, in 2006/07. As required by the Pensions Act 2004, this is a primarily risk-based levy, assessed by reference to the funding position of the scheme, its investment strategy, and the risk of insolvency of the scheme's sponsoring employer(s).

2.2.2. The Pensions Act 2004 also sets limits on how much we can charge and how much we can alter that total from year to year. In particular:

- The amount we can increase the levy estimate from year to year is limited to 25 per cent. This would prevent us charging a levy again if we ever set a levy estimate of zero and constrains the speed with which the levy can be raised if reduced to a nominal level. There is scope for the Secretary of State to alter the percentage by Order but removing the limit entirely would require a change to primary legislation; and

- The proportion of the levy that can be charged based on scheme size, (the 'scheme-based levy'), is limited so it can only make up 20 per cent of the total levy.

2.2.3. The legislation also requires that our risk-based levy be calculated by reference to the risks of employer insolvency and funding level[1]. We have sought to make the levy mathematically proportionate to risk - so not only do schemes we see as riskier pay more, but their 'premium' is intended to be directly proportional to a numerical assessment of that risk (referred to as 'risk-proportionate'). Such an approach helped maintain support for the levy when it was introduced and when charged at high levels. However, the legislative limitations – and the realities of the population we protect – make a purely risk-proportionate approach more problematic than it might appear. These challenges may increase as the amount collected reduces and eligible schemes become more well-funded rendering annual collection more volatile.

2.2.4. Over the years we have actively solicited stakeholder feedback when developing policy and it has always been the PPF's ambition to accommodate any suggestions for creating a better levy. This has often meant newly introduced rules created a greater level of distinction among levy payers. This approach to developing the levy has added to the complexity[2], resulting in a set of calculation rules (and guidance documents) that run to around 500 pages. Small and medium enterprises in particular tell us they are concerned about the administrative burden this brings. As the amount of levy PPF collect falls, this raises the relative cost of such admin burdens.

2.2.5. In the early years of the PPF, we made changes to the methodology of the levy every year, in large part because changes in risk would otherwise have led to the total amount we collected (the quantum) varying dramatically. In 2012 we moved to seeking to limit substantive methodology changes to every three years – mimicking pension schemes' own triennial valuation cycles - and smoothing measures of risk. This has made our overall collection less prone to volatility, but we still find that individual schemes' bills can be highly variable.

2.2.6. We have taken steps to ensure the levy is affordable (including a cap on the highest levies) and in our investigations of the causes of sponsor failure the levy has not been reported to be a factor[3]. However, some stakeholders have told us that in some cases, levy - when taken together with other pension costs - can be a real constraint on the ability of a business to invest and grow. Furthermore, the complexity of the levy might require levy payers to seek external professional advice.

2.2.7. A particular source of comment has been our assessment of insolvency risk and the use we make of these assessments in our levy calculation. Looking first at the assessment itself, we have built our own model based on the insolvency experience of our universe. Inevitably, as for any statistical model, there is a limit to the extent that the model can take account of the individual circumstances of employers, and this means that some stakeholders will take issue with a rating – particularly as the way that we use the scores generated can mean a small

[1] Investment risk and risk reduction measures are optional factors

[2] While it makes sense for each individual change, the process of building changes on to the existing framework (rather than drafting from scratch) has, over time, resulted in rules that are complex to follow.

[3] We perform a qualitative review of administrator/annual reports to help us complete the picture of what factors have contributed to and monitor insolvency events to understand what has caused them.

change in score results in a large difference in levy. Over the years we have reviewed the model to ensure that issues raised are being addressed appropriately.

2.2.8. Annual performance reviews for the model both prior to and following COVID-19 give us confidence that the model continues to perform well[4] in its ability to discriminate between solvent and non-solvent employers. Performance in assessing PPF sponsors has been significantly better than for models built across the whole UK population of businesses and, while there are costs in operating the model, these compare favourably with appropriate comparators.

2.2.9. While performance of the model has been good, we should caution that the insolvency count for every 100 employers has recently been lower than expected. To date we are not observing a rising trend in the insolvency count for DB scheme sponsors similar to that reported by the Insolvency Service for England & Wales across all companies (chart 1 below). As a result, a single insolvency event can have a material impact on model performance, in particular if the insolvency event is associated with an employer considered low risk.

Chart 1: 12 month rolling insolvency rate

2.2.10. As the insolvency experience has continued to be favourable and the amount of levy that we collect falls we expect to consider the case for simplifying this model and/or the case for different approaches to assessing risk recognising that there are costs both to schemes and the PPF in the current system.

2.2.11. The second aspect to the use of insolvency information is the mapping of scores to a limited number of levy bands and the application of a set of levy rates for those bands that then feeds into the levy calculation. When we initially developed our proposals on levy bands and rates, we were balancing four objectives:

[4] See chapter 13 for more details

- The banding structure should be easy to understand –if possible linked to more broadly understood measures of risk (e.g., public credit ratings[5]);
- The insolvency experience should be different for each levy band;
- The levy rates should reflect the range of insolvency risks in the population (with account taken for the proportionately higher contribution of higher quality credits in tail risk scenarios of concern to us); and
- volatility of bills should not be excessive, particularly where there is a small movement in measured risk, limiting so called 'cliff-edges'.

Experience since we originally developed the system has shown that it is impossible to achieve all these objectives simultaneously. For example, in originally designing our proposals we prioritised the first three objectives – proposing six bands linked to broad credit ratings – and aimed for a range of levy rates reflecting the range of insolvency risks in the universe. However, consultation responses showed stakeholders felt the resulting increases in levy rate from band to band created unacceptably high cliff edges. As a result, we subdivided the bands to create ten bands – and we still receive suggestions that we should go further and have more bands with smaller increases from band to band (as recorded in our 2019 Consultation).

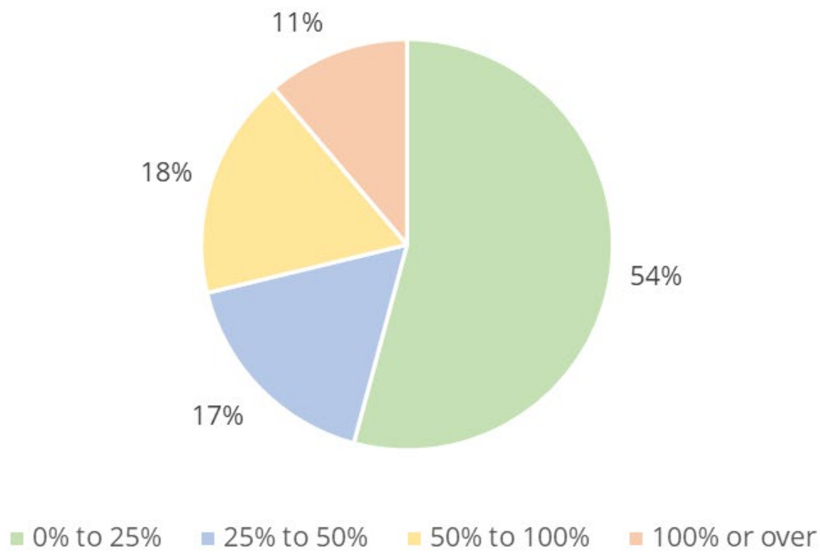
2.2.12. We have found that, while the insolvency experience for sponsors in each band does rise when moving to a higher-risk band, the difference in annual insolvency experience between bands associated with investment grade credit risk is not statistically significant in all cases at a 95% confidence level. Part of the reason for this is that the PPF-Specific model is successful in discriminating between solvent and insolvent employers, so that insolvency rates for the better levy bands are low.

2.2.13. Changes in levy band are significant drivers of volatility in levies – particularly for schemes paying a material levy[6]. Chart 2 below shows in the years since 2016/17 only just over a half of risk-based levies have been within +/- 25 per cent of the preceding one and 11 per cent have been 100% or more higher or lower (note that this does include schemes moving into or out of full funding – so where the comparator is zero).

[5] Public agency ratings are recognised and accepted in the corporate debt markets because of the depth of their issuer and default databases and because such ratings have been tested and validated over time

[6] Schemes that are close to fully funded may see a significant percentage increase in levy from year to year, but will typically pay a very low levy due to that low underfunding risk

Chart 2: Average percentage change in risk-based levy from year to year



2.2.14. Reviewing the current arrangements, we note that small changes in assessed risk lead to a 50 per cent or more increase in bill if they move a company into the next levy band (with a 14-fold increase from bands 1 to 10) - though of course this also means that levies reduce dramatically as levy band improves. Around 40 per cent of employers will move levy band each year, with similar numbers moving up and down.

2.3. Changes in our universe

2.3.1. The last few years have seen significant changes in the risk profile of the PPF universe – with fewer insolvencies for every 100 employers and significant improvements in the funding position of many schemes. While we cannot assume that insolvencies will remain low, it is fair to assume, all else being equal, that the trend toward improved funding is most likely to continue as the regulatory regime – reinforced by the new DB funding code – requires sponsors to address funding deficits. We also consider it likely that schemes will seek further opportunities for risk reduction and risk settlement in light of better funding positions and maturing memberships.

2.3.2. If outcomes follow this path, then the risk-based levy would likely be collected from a smaller number of schemes as a greater number of schemes are funded sufficiently well on a s179 basis that the underfunding calculated for levy purposes is zero. Currently nearly 40 per cent of schemes pay no risk-based levy and, were we to ever want to return to charging a levy at current levels with such a risk outlook, this could mean those remaining underfunded schemes would pay much higher levies than today.

3. A future levy

3.1. What objectives should we have in designing the levy?

3.1.1. As we expect to charge a much lower levy in the future it will be important to ensure that the cost and complexity of operating the levy remains appropriate for schemes and for us. This points to a simpler methodology.

3.1.2. We also need a levy system that can flex depending on where the PPF's funding is in relation to our needs. The risk of needing to respond to a funding challenge is low and might be expected to decrease over time. It is also worth noting, the levy is not our only lever in responding to increased funding demands in the future – a shift in investment strategy might be an alternative action. However, we consider it essential that a future PPF Board should have the flexibility to use the levy if needed.

3.1.3. Any future material rise in levy may be driven by a change in the PPF's financial resilience, for example due to an outsized claims experience, rather than an increase in risk amongst surviving schemes - and the projected fall in the number of risk-based levy payers could pose challenges when looking to charge a sizeable risk-based levy (unless the formula introduces an additional factor to inflate liabilities or tougher stress factors).

3.1.4. So, there is a need for change (and a real opportunity), but legislation gives us some limitations. We recognise we need to work with DWP and stakeholders to identify areas of possible legislative change.

3.1.5. In developing our approach, we think it is helpful to set objectives for a revised methodology. We consider there are two objectives that are of critical importance:

- The new levy needs to be flexible:
  - capable of working regardless of where we are relative to our funding resilience test (e.g., scalable, and able to fit with the different potential circumstances and reasons for charging). This could mean a very small (but largely risk-based) levy, in line with our central expectations. However, if PPF funding fell to an unacceptable degree, a more substantial levy might be needed, with more or less focus on future scheme risk depending on how the funding need has arisen and the circumstances at the time
  - continuing to be an appropriate way to distribute the levy as our universe changes over time.
- The levy methodology should be simpler and easier for schemes to engage with - this might mean for example considering the need for information from schemes that is only used in the PPF levy, and/or reducing need to actively monitor levy inputs. This will entail a move away from seeking to make the levy fully risk proportionate though the levy will remain reflective of risk (see paragraph 2.3.3).

3.1.6. In meeting these core objectives there are several supplementary objectives we need to have regard to:

- The levy must comply with the legal requirements – recognising that these requirements may evolve.
- Levy design should aim to avoid undue volatility in bills, while recognising that levies should increase as risk worsens and reduce as risk reduces.
- The design should be informed by stakeholder views – and aim to balance the interests of different levy payers and of our members.
- The levy should align with behaviours expected by the Regulator (encouraging schemes to focus on funding).
- Were changes in the data collected for levy purposes to be made, it would be important to have regard to wider uses of the data within the PPF and beyond (for example to monitor risks) so that other objectives are not undermined through simplification.

3.2. What does this mean for the design of the levy?

3.2.1. Development of the levy will take time, and links to developments surrounding the need for legislative change in partnership with DWP. However, we have identified four key design principles that we believe should inform how we evolve our levy methodology:

i. Increased flexibility in the amount of levy we aim to collect;

ii. Increased flexibility to charge on the basis of the size of the scheme ('scheme-based' levy);

iii. Rebalancing the risk-based levy to emphasise underfunding and a lesser focus on employer insolvency; and

iv. We should be open to using different approaches to how the levy is calculated depending on scheme size.

These four design principles are explored below.

(i) Flexibility on the amount we collect

3.2.2. In line with the PPF's funding strategy, the Board should have open to it the option of charging a zero levy, or a very low levy, without compromising the possibility of charging a higher levy at a later date, should our financial resilience deteriorate significantly. While the likelihood of this happening is low, and expected to reduce over time, we consider it would be prudent to set levies with regard to that possibility. Full flexibility on this would require a change to the Pensions Act, and potentially operational developments.

(ii) More flexibility on scheme-based levies

3.2.3. We also consider there is a case for seeking flexibility on the proportion of the levy charged on a basis reflecting the size of the scheme. In the unlikely event that the PPF were to return to charging a material levy, the most likely cause is a decline in the PPF's funding (for example in response to an outsized claims experience) – rather than a general rise in the risk we cover (although both events are not mutually exclusive). In such circumstances it could be more appropriate to recover what is in essence a sunk cost from schemes generally rather than increase charges on what could be a small sub-set of schemes. By contrast, a significant movement in longevity risk might affect both the level of PPF reserves and increase risk in the universe long-term, pointing to a more risk-based response in terms of levy. The balance between size-based and risk-based levies should therefore depend upon the circumstances at the time but could point to a levy largely based on size of scheme, spreading costs evenly. And in the shorter term, a levy reflecting the size of scheme can be seen as contributing to the cost of operating the PPF which should be shared, and this may make the case for a more modest rebalancing.

3.2.4. If we were not able to secure more flexibility in relation to the use of the scheme-based levy, there are other mechanisms that could be used to ensure we were able to respond to a funding challenge. We could ensure that the risk-based levy continued to be charged across a wide proportion of the universe – for example strengthening the stresses applied to reflect investment risk or scaling up liabilities (as was done in the early years of the levy). However, altering the balance between scheme-based and risk-based levies would be a simpler and more transparent way to achieve any required increase in levy.

(iii) Rebalancing the calculation – making the levy less sensitive to insolvency risk

3.2.5. Rebalancing the calculation with a greater relative emphasis on underfunding and a lesser emphasis on insolvency risk is considered a better match with our risk - and recognises the intrinsic uncertainty of insolvency risk assessments[7]. A levy with a greater emphasis on underfunding would help maintain incentives to reduce the size of deficits in pounds, irrespective of covenant strength or funding level. It would also support objectives of simplicity – allowing in future for simplifications in our approach to insolvency risk - while retaining the principle that those posing a greater risk to the PPF pay higher levies and vice versa.

3.2.6. Rebalancing between underfunding and insolvency risks and reducing the sensitivity of the levy to insolvency risk could in principle be achieved in a number of ways (e.g., by having a component of the risk-based levy that only takes into account the amount of underfunding). However, a more straightforward way to achieve our intention is to adjust the levy rates that are applied for each levy band - so that a move from one band to the next, in isolation, has a more limited impact on schemes' levy bills.

3.2.7. We consider that reducing the emphasis on insolvency risk should combine with a reduction in the number of different levy bands into which employers can be placed. As noted in chapter 2, even with the current approach to measurement, the number of levy bands makes it challenging to demonstrate that the differences we observe in insolvency rates are statistically significant in some cases. Any simplification in assessment of insolvency risk would be likely to make it harder to draw fine distinctions in risk– reinforcing the case for a simpler banding structure.

[7] There is a parallel here with the large exposure framework for banks, to protect them from traumatic losses caused by the sudden default of an individual counterparty, and which requires them to measure (and limit) their exposure to a counterparty, ignoring the probability of default. The potential impact of outsized claims on the PPF is a risk we monitor and which we identified when responding to TPR's consultation on the DB Funding Code.

3.2.8. Work on how we might assess insolvency risk in the longer term, and on the right number of levy bands will be taken forward over the coming years and is likely to require input from a range of stakeholders. However, there is merit in taking a step to soften the scale of increases from band to band now – moving us in the direction required for a simpler levy and reducing the amount we collect, in tandem.

(iv) Different rules for different sizes of scheme

3.2.9. A risk-based levy that necessarily has elements of complexity can be an operational burden for schemes. Smaller schemes, with slender resources for advice, may need to use those resources to manage their levy bill rather than measures that could focus on member outcomes (e.g., more investment advice). We believe in the future our levy should be different according to the size of the scheme to reflect this. As the levy falls, we will come to a point where the smallest schemes will contribute a negligible amount (and the risk they present is similarly negligible), but the costs to them of engaging with the levy system could become disproportionate – this suggests moving away from the risk-based levy or even the levy altogether for these schemes. In contrast the largest schemes – some of which pose systemic risk – might pay a higher levy.

4. Next Steps

4.1. Our flightpath to change

4.1.1. To support further reductions in levy in future years, we are working with the DWP to explore legislative change so that we have the ability, in the unlikely event it is needed, to raise the levy again more freely. For example, the current cap of 25 per cent on year-on-year increases in levy when considering reducing levy by materially more at this stage.

4.1.2. We've started to engage with stakeholders on how to turn our broad design principles into more detailed plans. In particular, we've been holding ongoing discussions with our Industry Steering Group. Our Chair Kate Jones and CEO Oliver Morley also published a blog setting out some initial thinking on our funding strategy following the publication of our Annual Report and Accounts for 2022/23. We would be interested to hear views on simplifications that could be made to the current methodology.

Consultation question:

Do you have any views on what the priorities should be for simplification of the levy methodology?

Proposals for the 2023/24 levy

5. Key policy

5.1. Our first steps to a future levy

5.1.1. In the light of our funding position, we can substantially reduce the levy we collect for 2023/24. We are proposing to set our levy estimate at £200 million this year. This is a reduction of £190 million compared to the 2022/23 levy estimate, and £420 million compared to the 2020/21 estimate.

5.1.2. While we will be developing our long-term model with input from stakeholders, we see the merit in making changes consistent with our long-term direction of travel now. This will mean that changes to the distribution of the levy occur at the same time as the overall reduction in collection. This will help minimise the extent to which distributional changes lead to instability in levies.

5.1.3. Our future of levy design principles call for us to reduce the sensitivity of the levy to changes in insolvency risk. In 2023/24 we will move towards this by halving the relative increases between levy rates for each levy band.

5.1.4. Alongside this change, we are also intending to reduce levies across the universe taking account of the outcome of the Funding Review. Therefore, we are also proposing to reduce the Levy Scaling Factor by 23% and Scheme-based Levy Multiplier by 10%. This will ensure that all eligible schemes – barring idiosyncratic factors – will see a reduction in their levy bills.

5.2. Our key policy proposals for 23/24

Levy estimate

5.2.1. Scheme funding has improved over the past 12 months, and as a result our current exposure to claims has declined. Our 7800 index shows that the scheme funding ratio improved from 104.2 per cent in July 2021 to 118.2 per cent in July 2022. Even without active measures to reduce the levy, this and other changes in data would have reduced the levy estimate to around £320 million.

5.2.2. Our current level of reserves are close to what we expect to need to meet the Financial Resilience test set out in our Funding Strategy statement. Given this, and a lower expectation for future claims, we believe it is appropriate to reduce the rate at which we collect levy. Accordingly, we propose to reduce the levy we expect to charge in 2023-24 to £200 million, which compares to a targeted collection of £390 million for 2022-23.

5.2.3. This means that we have also taken active steps to reduce levies, by around £120 million.

5.2.4. The Board anticipates that in future years the levy estimate is likely to reduce further – including as a result of further policy changes, though this may depend on the position in terms of our funding resilience target.

Insolvency risk and levy rates

5.2.5. To meet our design criteria, we propose to reduce the sensitivity of the levy to insolvency risk by adjusting the levy rates that are applied for each levy band.

5.2.6. Following the principle that schemes that pose more risk pay more levy, the levy rates rise for each of the ten bands. For levy bands 1 to 4, increases are relatively limited (averaging around 14 per cent). These relatively limited increases were intended to give some recognition that the difference in annual insolvency experience between bands associated with investment grade credit risk is not statistically significant at a 95 per cent confidence level – which in future we might more fully address by simplifying the mapping of insolvency risks to levy bands.

5.2.7. For levy bands 5 to 10, the differences in levy rates between neighbouring bands are more material, meaning that cliff edges are more pronounced when moving to a neighbouring levy band. In practice this means that even a small change in insolvency risk can increase the levy by 50 per cent or more (or conversely, lower the levy by a third). The steepness of the change, combined with the high number of companies that move between levy bands each year (20 per cent improve and 20 per cent worsen by one or more bands), means that the presence of material cliff edges is a significant driver in volatility for schemes with material levies.

5.2.8. As one of our objectives is to limit levy volatility, we drew on previous stakeholder feedback regarding cliff-edges and our experience of the 22/23 adjustment where we limited bill increases from 2021/22 to 2022/23 by 25 per cent.

5.2.9. As a result, we have developed a proposal which would limit volatility if a sponsoring employer moved one levy band. We considered capping the increase by 25 per cent between each band. However, if we implemented this approach, we would be making no change for those schemes in bands 2 and 3 where the increases are already below 25 per cent – and where we expect to move to a simpler banding system. We could also be making a greater proportionate reduction for those changes in risk that the evidence says are most significant.

5.2.10. So, instead, we are proposing to halve the relative increases between each levy band, altering levy rates for levy bands 2-10. This option reduces the sensitivity of the levy to changes in insolvency risk across the full range of schemes meaning that those in bands 2 & 3 benefit too.

5.2.11. This also reduces the volatility where an employer moves between more than one band. For example, the difference between levy band 1 and 10 is now four times, rather than 14 and difference between levy band 4 and 6 is now 44% compared to more than double.

5.2.12. We set out the current and proposed levy rates below in table 1.

Table 1: current and proposed levy rates

Levy band	Current Levy Rates	Proposed Levy rates - Increments between levy bands halved
1	0.0028	0.0028
2	0.0031	0.0030
3	0.0035	0.0031
4	0.0040	0.0034
5	0.0053	0.0039
6	0.0081	0.0049
7	0.0126	0.0063
8	0.0176	0.0076
9	0.0239	0.0089
10	0.0383	0.0116

5.2.13. Our proposed reduction in levy rates will reduce levies by around £60 million.

Levy scaling factor and Scheme based levy

5.2.14. We are proposing to reduce the levy scaling factor from 0.48 to 0.37, a reduction of nearly a quarter. Taken together with the reduction in scheme risk seen so far this year (and an assumption that this will persist), this is likely to reduce risk-based levies for schemes with band 1 sponsors by around 40 - 45 per cent. This reinforces reductions for those schemes in levy bands 2 to 10.

5.2.15. A scheme-based levy is paid by all schemes in our eligible universe with nearly 40 per cent of schemes being sufficiently well funded that they only pay a scheme-based levy. Consistent with our policy intent for the scheme-based levy to make up a larger proportion of an overall smaller levy, we are also reducing the scheme-based levy multiplier. The proposed scheme-based levy multiplier would be 0.000019 for 2023/24 – which other things equal will reduce a scheme's scheme-based levy by 10 per cent.

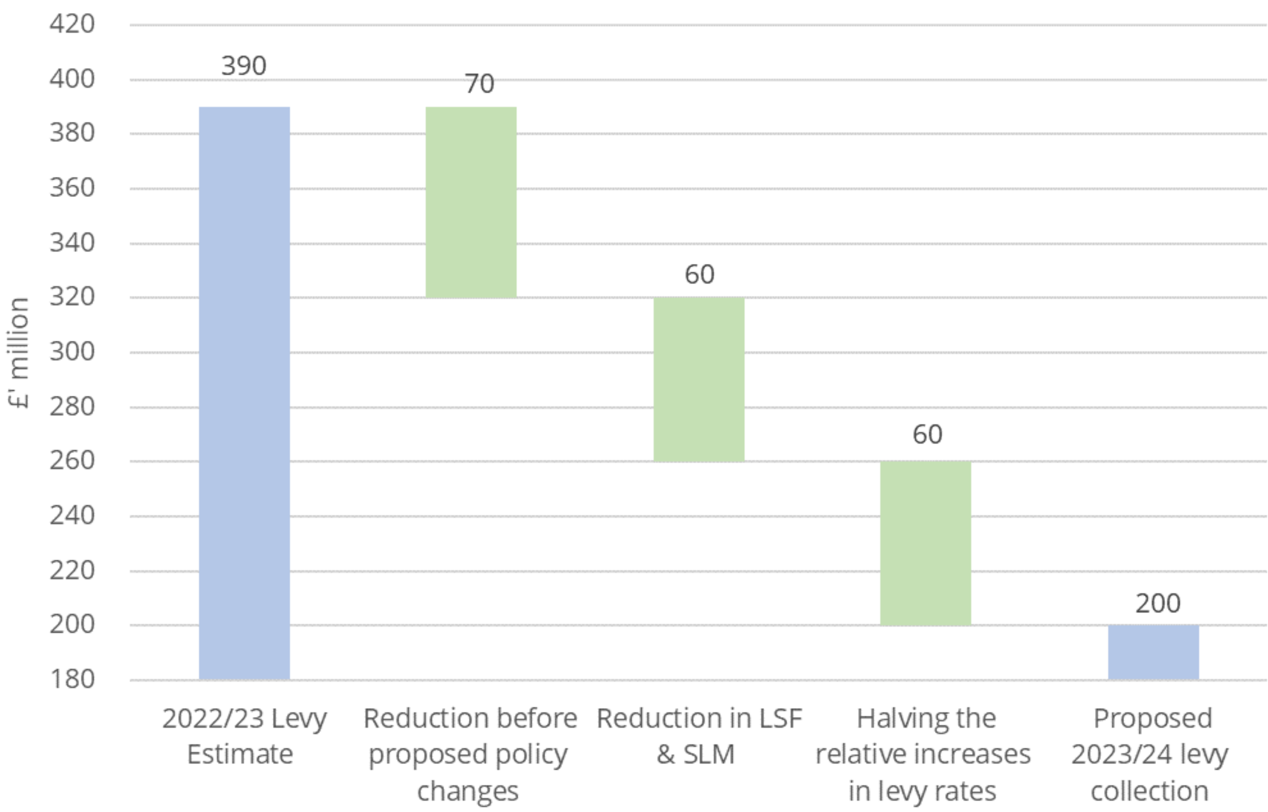
5.2.16. We expect the changes to the levy scaling factor and scheme-based levy will reduce the levies by around £60 million compared to 2022/23.

5.3. Impact assessment

5.3.1. We have carried out an impact analysis to show the projected impact on levy bills for 2023/24 of known changes in the environment (including economic market data and information on insolvency scores to end-July 2022). We set-out a summary of the impact assessment below with further detail available in the technical appendix.

5.3.2. Chart 3 below shows the evolution of the Levy Estimate from 2022/23 to the expected 2023/24 levy collection on the proposed policy.

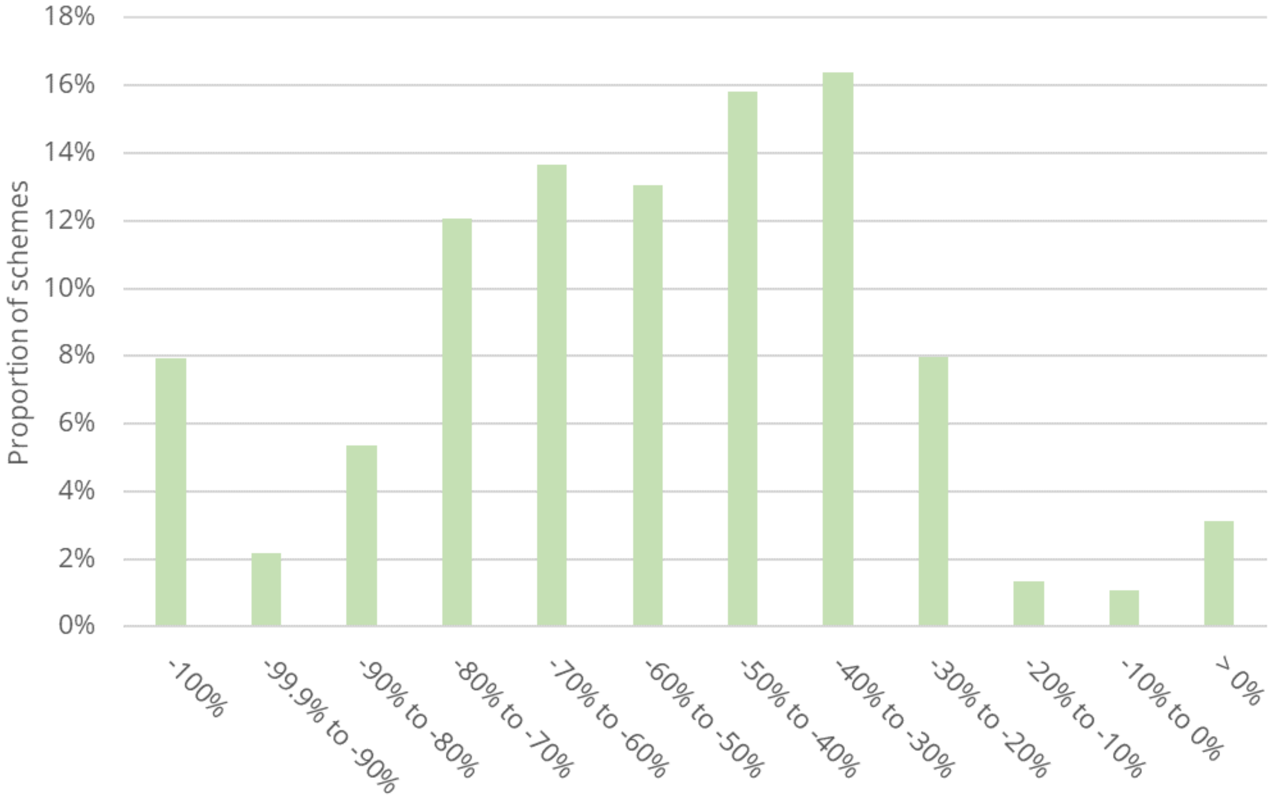
Chart 3: change from 2022/23 Levy Estimate to proposed 2023/24 levy collection



5.3.3. Chart 4 below shows the expected change in levy from 2022/23 to 2023/24 for all schemes that paid a risk-based levy last year. The great majority of schemes are projected to see a fall in levy compared to 2022/23, due to the reduction in assessed underfunding risk and the main policy proposals. The key features seen are:

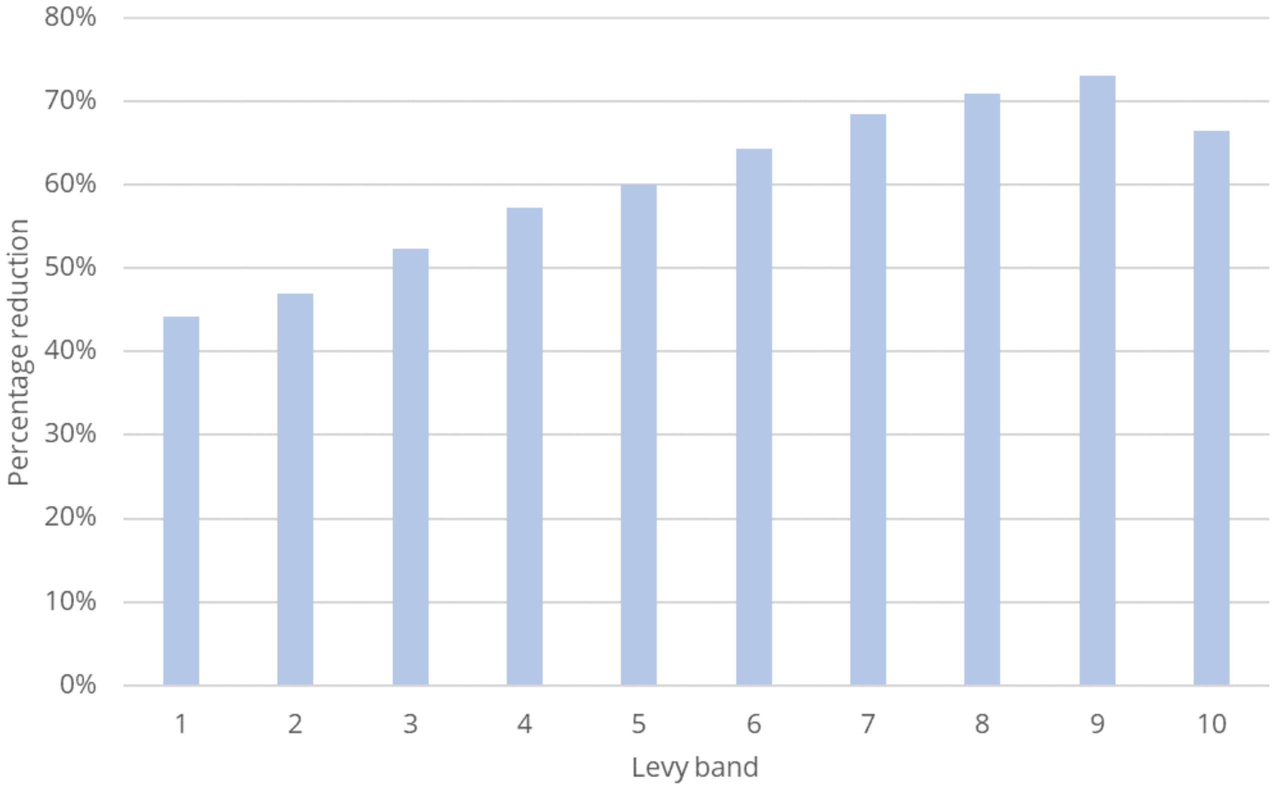
- Over 96 per cent of schemes paying a risk-based levy are expected to see a risk-based levy that is lower in 2023/24 than 2022/23, with an average reduction in risk-based levy of over 50 per cent.
- The average relative cost of levy bills (measured as the risk-based levy as a proportion of smoothed liabilities) will reduce from 0.06% to 0.03%.
- A small number of schemes will see risk-based levy increases due to the impact of the 2022/23 Adjustment, or where there has been a significant worsening in the sponsors' insolvency scores.

Chart 4: change in risk-based levy from 2022/23 to 2023/24 on proposed policy



5.3.4. The reductions in levy from the proposed policy changes will benefit all schemes that pay a risk-based levy, all else being equal. Although those schemes with sponsors in the higher levy bands will benefit most from the halving of the relative increases between levy bands, as chart 5 below demonstrates, all levy bands are expected to see a material reduction in levy on average, with the schemes with the sponsors allocated to the strongest levy bands expected to see a reduction in risk-based levy of 40-45 per cent.

Chart 5: percentage reduction in risk-based levy by levy band from proposals



5.3.5. Our analysis has focused on schemes paying a risk-based levy, for whom changes in levy may be considered material. However, nearly 45 per cent of schemes are projected to pay only a scheme-based levy (SBL) for 2023/24. We expect that almost all schemes will see a decrease in SBL due to the reduction in the SLM, and generally decreasing liabilities for levy purposes, though it is possible that some schemes will see an increase due to idiosyncratic effects (e.g., due to a block transfer). Schemes are expected to see, on average, a reduction of over 10% in scheme-based levy.

Consultation questions:

Do you agree with our proposal to reduce the cliff-edges between levy bands so that a small movement in insolvency risk has a lower impact on bills?
Do you agree with our proposal to reduce the Levy Scaling Factor?
Do you agree with our proposal to reduce the Scheme Based Levy Multiplier?

6. Other policy

6.1. Summary of other policy changes

6.1.1. The Pensions Regulator is planning to introduce, for the 2023 Scheme Return, the updated asset categorisation which TPR and PPF jointly consulted on last year. Accordingly, we are updating our asset and liability stress factors.

6.1.2. We commissioned an independent review of our overall system of stress factors, partly driven by the new asset classes being introduced and because we would periodically expect to carry out a comprehensive review (with the last such review taking place in 2017).

6.1.3. The main change coming out of the latest review is to apply one asset stress for all quoted equities at -16 per cent, thereby bringing down the stress previously applied to UK equities.

6.1.4. Overall, we do not expect the updated stress factors to materially impact the Levy Estimate, albeit individual schemes with a greater allocation to certain types of assets may be more impacted (some positively and some negatively).

6.2. New asset class breakdown and associated stress factors

6.2.1. In 2021, the PPF and TPR issued a joint policy statement following a public consultation on proposals to update the asset information collected from defined benefit pension schemes.

6.2.2. A tiered approach to data collection was confirmed where schemes are categorised by size of liabilities – retaining a simple set of information for smaller schemes (tier 1), with more granular information required from larger schemes (tiers 2 & 3).

6.2.3. We confirmed then that the first time the new asset information was expected to be used for levy purposes, we would consult on the levy rule changes necessary to facilitate the use of the new asset information – in particular, our asset stress factors. TPR intend to implement the new asset classes in the 2023 Scheme Return and accordingly, we are now consulting on how we will incorporate this new information into 2023/24 levies.[8]

6.2.4. An independent review of our overall system of asset and liability stress factors was carried out earlier in the year by Barnett Waddingham LLP to consider whether our current approach remains appropriate, and what stress factors should be used when new asset class data is available from schemes.

6.2.5. In the main, Barnett Waddingham LLP supported the retention of our overall framework for stressing schemes' funding positions for levy purposes, with the main change being a reduction in the negative stress which is applied to UK equities, bringing it into line with the other quoted equity classes. A fuller explanation of our policy proposals following the review can be found in the technical appendix at the end of this document. A summary of our proposals is set out in table 2 below.

[8] If the new asset class categorisations are not incorporated into 2023 scheme returns, any rule documents will revert to the basis set out in the 2022/23 Determination.

6.2.6. Given our objective of simplicity for a future levy system, we have considered if there is merit in simplifying the data used for levy purposes (i.e., not using the full granularity made possible by the new information).

6.2.7. Approaches were considered whereby data transformation could be implemented to align new data collected by TPR with the dataset collected currently, or to map all tier 2 data to align with tier 1. We concluded however that any form of additional data transformation would be more likely to create additional complexity for stakeholders (rather than reduce it). We are therefore proposing to implement all policy changes set out for asset class data collection, with the below stress factors applied.

Table 2 - Proposed liability and asset stress factors

	Current stresses 2022/23 levy	Tier 1 proposed stresses 2023/24 levy	Tier 2 & 3 proposed stresses 2023/24	Comments
Liability stress factors				
Interest rate	-75bps	-74bps	-74bps	This is the nominal rate stress factor.
Inflation	-14bps	-11bps	-11bps	Based on nominal rate stress factor less a corresponding real rates stress factor.
Asset stress factors				
Fixed interest bonds				
UK Government	15%	17%	Short (<5yrs): 2% Medium (5-15yrs): 6% Long (>15yrs): 17%	Stress factor methodology unchanged. Tier 1 schemes assumed to hold over 15-year gilts.
UK investment grade (exc. UK Govt.)	3%	3%	<10yrs: 2% 10yrs+: 5%	Stress factor methodology unchanged.
Non-UK investment grade	New asset category	3%	<10yrs: 1% 10yrs+: 4%	Based on iBoxx $ Corporates – Annual Yield Index. For Tier 1 schemes, the same factor is used for all investment grade credit (excluding gilts).
Sub-investment grade	New asset category	-6%	-6%	Based on the average volatility of high yield bonds, loans and emerging market debt, with the underlying volatility data derived from, respectively, the iBoxx USD Liquid High

				Yield Index, the S&P Leveraged Loan Index and the Markit iBoxx USD Emerging Markets Corporates Overall Index.
Private debt	New asset category	n/a	-9%	With limited public data available for this class, the proposed stress factor has been based on the annualised volatility of historical quarterly returns on data supplied by Cambridge Associates.
Inflation linked bonds				
UK Government	15%	16%	Short (<5yrs): 1% Medium (5-15yrs): 6% Long (>15yrs): 20%	Tier 1 schemes assumed to hold over 5-year index linked gilts.
Equities				
UK quoted	-19%	-16%	-16%	Stresses for UK, Overseas and Emerging Market equities consolidated owing to the similarity in risk return characteristics, the declining trend in overall equity exposure, and the continuing shift of UK pension funds towards a more globally oriented approach to equity investment.
Overseas quoted	-16%			
Emerging markets	-16%	n/a	-16%	
Unquoted equity	-19%	-19%	-19%	Existing stress factor retained, leading to a tougher stress than public equity classes. This is supported by the independent analysis commissioned.
Other				
Property	-5%	-4%	-4%	Stress factor methodology unchanged.
Annuities	16%	16%	16%	Methodology unchanged.

Commodities	-14%	n/a	n/a	Asset category removed.
Hedge funds	-3%	n/a	n/a	Asset category removed.
Diversified Growth Funds (DGFs)	New asset category	-10%	-10%	Based on 60% of the stress factor for developed market equities.
Absolute Return Funds (ARFs)	New asset category	n/a	-5%	Based on volatility data for a range of funds which DB pension schemes typically invest in, with the proposed stress factor set at the middle of the volatility range. Given the wide spectrum of ARFs, allocations at the higher-risk end of the spectrum will be directed to the "Other" category. Further details will be provided when the Pensions Regulator publishes its scheme return guidance.
Insurance funds	-19%	n/a	n/a	Asset category removed.
Other	-19%	-19%	-19%	Unchanged approach of matching the maximum stress of other asset classes.
Cash	0%	0%	0%	Unchanged approach of having a nil stress.
Asset Backed Contributions (ABCs)	ABCs are deducted from asset allocations before roll-forward and therefore do not have a roll-forward index or stress factor.			

	Current stresses 2022/23 levy	**Proposed stresses 2023/24 levy**	**Comment**
Risk factor stresses for Tier 3 Schemes			
Equities UK Overseas Emerging	 -19% -16% -16%	-16%	Stress factor methodology unchanged except that we have proposed that the equity stresses are consolidated.
Interest rate	-75bps	-74bps	Stress factor methodology unchanged.
Inflation	-14bps	-11bps	Stress factor methodology unchanged.

Credit	+38bps	+37bps	Stress factor methodology unchanged.

Consultation questions:

Do you agree with our proposals to change our approach to asset stresses for:
UK equities?
Private Debt?
Diversified Growth Funds?
Absolute Return Funds?

6.3. The 2022/23 Adjustment

6.3.1. Last year we introduced – for a single year - the 2022/23 Adjustment to support schemes whose levies would otherwise increase significantly as a result of employers, that remain viable, seeing downgrades in insolvency risk scores due to the impact of COVID. Slightly under 10 per cent of schemes will benefit from this in 2022/23.

6.3.2. Our analysis indicates that after taking account of the policy changes proposed for 2023/24, relatively few schemes would benefit if we extended the adjustment for another year. The analysis highlights that where a scheme would benefit, it is not in general due to further increases in insolvency risk. Therefore, in line with our original plan, we will not be continuing the adjustment.

6.4. The PPF-specific model - scorecard 6

6.4.1. Employers are scored using a limited number of variables. The inputs for this are collected by the PPF's insolvency provider from financial accounts filed. When inputs cannot be sourced from the accounts the missing data points are replaced with substituted values. During the recalibration of the PPF-Specific model in 2019 when our insolvency risk provider changed from Experian to D&B, there was an ambition to limit the level of change for our stakeholders as much as possible. Replacement values for missing values were therefore not reviewed (unless for example to take the opportunity to incorporate stakeholder feedback).

6.4.2. We noted in last year's consultation that – upon investigation of scorecards at an individual level - scorecard 6 was not performing as expected. D&B have undertaken a review of the scorecard, with a particular area of investigation being the treatment of replacement values for missing data[9]. In one instance, the 'Debtors' variable was having a very significant impact on scores for a small proportion of employers[10], with investigation concluding that the replacement value appeared to be an outlier[11].

6.4.3. Further analysis was carried out by D&B to recalibrate this replacement value based on data over the full modelling period, and this led to a revised substitute value of 5.64 being calculated. Using this revised replacement value only affected a limited number of scores, with 13 employers previously matched to one of the higher risk levy bands (e.g., levy bands 8, 9 or 10) seeing their levy bands improve by 1 or 2 levy bands but increases the Gini performance from

[9] When credit scoring employers, missing data is replaced with substituted values.
[10] The substituted value being used when credit scoring 13 employers.
[11] A data point that differs significantly from other observations.

42.7% to 47.8%. D&B’s recommendation was therefore that it was appropriate to replace this value with 5.64.

6.4.4. As part of the investigation, replacement values for other scorecards were also considered but no material improvement in model performance was observed.

Other developments

7. Customer service

7.1. Helping with invoicing

7.1.1. Starting with invoices issued from September 2020 (the 2020/21 levy), we started sending electronic PDF invoices to scheme contacts listed on TPR's Exchange database, as well as paper and electronic versions to scheme trustees.

7.1.2. We're continuing to offer this as a standard part of our service, and the hierarchy for contacts that receive the electronic invoice emails start with the Levy Contact and move to the Scheme Contact in the event that a Levy Contact is not present in the Pensions Regulator's Exchange database.

7.1.3. Cyber security - as part of ensuring that electronic communication is safe – is paramount when introducing a new system. To this end, all electronic invoices are issued using a system provided by Mimecast. Mimecast is a cybersecurity provider that helps thousands of organisations worldwide make email safer and bolster cyber resilience. Our invoices will originate from 'noreply@mail.ppf.co.uk'. However, if you are in any doubt about the legitimacy of an invoicing email, please do contact us at information@ppf.co.uk to confirm – as several levy payers did last year.

7.2. Support with payments

7.2.1. We announced in our policy statement for the 2022/23 levy year that we will continue to offer our COVID easement throughout 2022/23 and 2023/24 - to help schemes with sponsors impacted by COVID-19 by giving them longer to pay.

7.2.2. Based on stakeholder feedback, and on what we're permitted to do by legislation, we developed policy which introduced a new payment plan option. Affected schemes or their sponsoring employers can submit a notification form via our website – within 28 days of receiving their invoice – explaining how they have been negatively affected by COVID-19 and request an extension to payment terms. If approved, we will waive any interest charges that would have normally accrued due to late payment for up to 90 days (as long as payment is made within those 90 days).

7.2.3. Where schemes/employers need longer than 90 days (or there are other reasons why they would face particular difficulties paying on time) applications can be made under the existing payment plan process.

7.2.4. Our policies, FAQs and forms relating to payment plans and our COVID-19 easement can be found on our website at ppf.co.uk/levy-payers/pay-your-levy/help-paying-your-levy.

8. Draft Levy Rules 2023/24

8.1. Introduction

8.1.1. We have moved away from publishing a full suite of draft documents with our consultation, instead opting to publish only the draft Determination and Appendices where substantive change has been made.

8.1.2. The main changes to the Levy Rules have been to reflect:

- the policy proposals set out in this consultation; and
- amendments associated with the new asset class breakdowns and associated stress factors

Drafting changes can be found in the Determination and Appendices published alongside this consultation document, but a summary of the changes is also set out below. All rule documents will be published when the Determination is finalised.

8.1.3. The Court of Appeal issued its judgment on the Hughes judicial review on 19 July 2021, confirming, in particular, that the PPF is required to disapply the compensation cap when determining compensation payable to members. This ruling has implications for schemes carrying out s179 valuations and last year we updated our s179 valuation guidance to reflect that the compensation cap must not be applied for the purposes of the s179 valuation.

8.2. Other changes

8.2.1. We have also made the following changes:

The Determination

(a) In response to stakeholder feedback, we have amended the definitions of Allocated Members and Member to confirm that the relevant Exchange user-guide and help text should continue to be followed when submitting membership numbers, including in relation to dependants. This remains reflected in Rule E6.1. We have also taken the opportunity to simplify and consolidate the two definitions. No policy or operational change is intended by this amendment.

(b) Rule C1.2 of the Determination has been amended to reflect the change to the scheme-based levy multiplier (refer to subheading 5.2 of this consultation for further information).

(c) Rule C2.2 of the Determination has been amended to reflect the change to the LSF (refer to subheading 5.2 of this consultation for further information).

(d) Rule C2.4 of the Determination has been removed – the rule had been in place for Levy Year 2022/23 to provide support to schemes seeing significant volatility in insolvency risk scores due to the impact of COVID (refer to subheading 5.2 of this consultation for further information).

(e) In line with the removal of the MFR Appendix, the Determination has been amended, in particular Rule D2, to remove references to MFR Valuations.

(f) The Determination has been amended, in particular Rule D3 has been deleted, in line with the removal of the Investment Risk Appendix (refer to chapter 9 of this consultation for further information).

Insolvency Risk Appendix

(g) The 'Log Debtors' variable of Scorecard 6 in Part 2 has been amended to improve outcomes (refer to subheading 6.4 of this consultation for further information).

(h) Table 5 in Part 7 has been revised to reflect our proposed reduction in levy rates (refer to subheading 5.2 of this consultation for further information).

DRC Appendix and Guidance

(i) Both these documents have been amended to clarify that, when certifying DRCs under Option Alpha, contributions associated with liabilities which arise in respect of GMP equalisation should be included to the extent that such liabilities are reflected in the valuation to which the certificate relates. The same principle applies when considering expenses relating to the discharge of liabilities in respect of GMP equalisation.

MFR Conversion Appendix

(j) The MFR Conversion Appendix has been removed as there are no schemes left within its scope.

Transformation Appendix

(k) The Transformation Appendix has been amended to incorporate the asset classes pertaining to each of Tiers 1, 2 and 3, the risk factor stress impacts submitted by schemes in Tier 3, and the asset roll-forward indices as set out in our joint policy statement with TPR last year. In addition, the Transformation Appendix includes the asset and liability stress factors which are summarised in Chapter 6 of this consultation document. The formulae pertaining to the treatment of bespoke stress analyses have been removed, since this regime is replaced by the more granular asset breakdown in Tiers 2 and 3, together with the risk factor stress impacts applicable to Tier 3.

The presentation of the asset breakdown and the asset roll-forward formulae in the Transformation Appendix are dependent on the ultimate presentation of the asset breakdown within Exchange. Depending on how TPR's system build evolves over the coming months, the final version of the Transformation Appendix published in December may therefore incorporate some presentational adjustments from the consultation version. Any such amendments would be purely to ensure that the outputs continue to reflect our policy intention and are consistent with the inputs on Exchange.

Alternative Covenant Scheme Appendix

(l) The Alternative Covenant Scheme Appendix has been amended to incorporate the asset classes, asset stress factors and risk factor stress impacts pertaining to Tier 3 schemes (with the references to bespoke stress analyses removed). As with the Transformation Appendix, it is possible that presentational adjustments may be needed in the final version published in December, dependent on the ultimate presentation of the asset breakdown for Tier 3 schemes within Exchange.

Investment Risk Appendix and Bespoke Stress Guidance

(m) The Investment Risk Appendix and Bespoke Stress Guidance have been removed as this regime is replaced by the new asset class breakdowns and associated stress factors.

Section 179 valuation certificate

(n) We have taken this opportunity to update the section 179 valuation certificate on our website, which forms part of the actuary's s179 valuation report and is sent to the scheme's trustees. This may be found here.

The main changes to the certificate are:

- updates to the tables setting out the historic combinations of valuation guidance and assumptions guidance;
- amended actuarial certification where the permitted flexibilities relating to interim allowances for GMP equalisation have been used;
- changes to the wording around asset adjustments in respect of insured annuities, reflecting that this adjustment should reflect the difference between the value in the scheme accounts and the s179 value (and could be positive or negative); and
- minor typographical corrections.

General

(o) We are reviewing our Contingent Asset standard forms as they reference the existing notifiable events regime. We are aware of the anticipated introduction of new notifiable events, which are not yet in force. We will consider appropriate changes to our Contingent Asset standard forms, including the timing of any changes ahead of the Measurement Time, once the new provisions are in force.

9. Next steps and Key Dates

9.1. Next Steps

9.1.1. We expect to publish our final rules for the 2023/24 levy year in December 2022, along with our policy statement which finalises our proposals for change following feedback to this consultation.

9.2. Key dates

9.2.1. The following table sets out the proposed key dates in the coming year, as reflected in this consultation and our draft determination:

Item	**Key dates and times**
Closing date for the 2023/24 consultation	10 November 2022 – 5:00pm
Publication of final rules and Policy Statement	End December 2022 (expected)
Scheme returns and electronic contingent asset certificates to TPR	31 March 2023 - Midnight
ABC certificates and special category applications to us	31 March 2023 - Midnight
Send contingent asset documents to us	03 April 2023 – 5.00pm
Start of 2023/24 levy year	01 April 2023
Deficit-reduction contributions certificates to TPR	28 April 2023 - 5.00pm
Send exempt transfer applications to us	28 April 2023 - 5.00pm
Certify full block transfers with TPR	30 June 2023 - 5.00pm
Publication of Mean Scores	July 2023
Invoicing starts	Autumn 2023

10. Consultation Arrangements

10.1. Timing and responding

10.1.1. The consultation runs from 29 September 2022 to 5pm on 10 November 2022. Please ensure your response reaches us by the deadline. Submissions can be made online:

www.ppf.co.uk/levy-payers/help-shape-our-rules

10.1.2. There are two versions of online submission available to you, 'quick' and 'full':

- The 'quick' submission allows respondents to review a summary of key proposals set out in our consultation, and the opportunity to give their views. It is designed to take only 10 to 15 minutes to complete. This version is designed for those who may not have time to respond to our consultations in full.
- The 'full' version sets out all the questions we are asking in this consultation, allowing complete responses, along with free format text fields for additional views to be submitted. This version of submission can either be completed online, or via an offline template which can be downloaded and once complete, uploaded via our website.

10.1.3. Please ensure you state whether you are responding as an individual or representing the views of an organisation. If you are responding on behalf of an organisation, please make it clear whom the organisation represents and, where applicable, how the views of members were assembled.

10.1.4. Under the Freedom of Information Act 2000 (FoIA), all information contained in the response, including personal information, may be subject to publication or disclosure.

10.1.5. The respondent should limit any personal information which is provided or remove it completely. If a respondent requests that the information given in response to the consultation be kept confidential, this will only be possible if it is consistent with FoIA obligations and general law on this issue. Further information can be found on the GOV.UK website:

https://www.gov.uk/make-a-freedom-of-information-request

10.1.6. A summary of responses and the Board's final confirmed policy will be published on the PPF website at:

https://www.ppf.co.uk/

11. Comments on the Consultation Process

11.1. The consultation is being conducted in line with the Cabinet Office's Consultation Principles:

https://www.gov.uk/government/publications/consultation-principles-guidance

The Board would welcome feedback on the consultation process. If you have any comments, please contact:

External Affairs
Pension Protection Fund
Renaissance
12 Dingwall Road
Croydon, Surrey
CR0 2NA
Email: externalaffairs@ppf.co.uk

Technical appendix

12. Asset class information and stressing

12.1. Introduction

12.1.1. On 29 April 2021, TPR and the PPF issued a joint-consultation - 'Proposals to update the asset information collected from defined benefit pension schemes. The proposals aimed to better capture data on investment risk, primarily to support TPR's new DB funding code, without resulting in an excessive administrative burden on schemes. The policy statement concluding the consultation was published on 21 October 2021.

12.1.2. Policy changes were based on categorising schemes - by liability size - into a tiered structure, retaining a simple reporting approach for smaller schemes (Tier 1), with more granular information on asset allocations captured from schemes in Tier 2, and the largest schemes (Tier 3) providing information on the sensitivity of portfolios to investment stresses. Confirmed changes included collecting more detailed information on bonds, and the introduction of three new categories: absolute return funds, diversified growth funds and private debt. The policy statement also set out the concluded approach for keeping a simplified roll-forward methodology used in PPF levy calculations.

12.1.3. We indicated at the time that we would consult as part of our 2023/24 rules consultation on the rule changes necessary to facilitate the use of the new asset information in the levy, in particular the overall system of asset and liability stress factors.

12.1.4. A review has been carried out for us by Barnett Waddingham LLP to consider:

- whether the current approach of setting the stress factors based on historical volatility data remained appropriate (including the period and frequency over which volatility is analysed); and
- the standard and bespoke asset stress factors we should use when new asset class information is provided in scheme returns.

12.2. Reviewing our current approach to stressing

12.2.1. As part of the analysis, the current approach of using historical volatility data to set stress factors for certain asset classes was considered, comparing it to other methodologies (e.g., using proprietary asset-liability models). Alongside this, consideration was given to the reference period of analysis of the market data used to derive the stresses.

12.2.2. The review concluded that it remains appropriate to use historical volatility data, as it provides a more objective measure of future expectations of movements in markets. It is also a more widely applicable measure than using implied volatilities from options markets, as these are only available for a subset of the asset classes under consideration.

12.2.3. It is proposed that risk factors should be based on market volatility data observed between 31 December 2005 and 31 December 2021, allowing for a wider range of economic conditions (such as the volatility experienced during 2020) than the existing data set to 2017.

12.2.4. Other proposals are:

- UK, Overseas and Emerging Market equities, owing to the similarity in risk return characteristics, the declining trend in overall equity exposure, and the continuing shift of UK pension funds towards a more globally oriented approach to equity investment are considered to be more appropriately stressed when consolidated. It is therefore proposed to reference the MSCI World Index for all equities and consolidate to a single stress factor (noting the currency proposal below). The private equity stress is not recommended to be consolidated as the nature of these assets is materially different.
- The current currency approach used for global equities is a 50/50 blend of USD and GBP indices (i.e., assumes 50% exposed to GBP strengthening against USD and 50% currency hedged). We propose moving to an approach that would instead reference 50% of local return indices and 50% sterling return indices for the MSCI global world equity index as this better reflects a typical approach to equity investing, in our opinion. Although this approach would produce a similar implied stress compared to other approaches, we believe this would better protect the stress factors from the impact of a future deviation in USD exchange rate compared to the other currencies that make up the index.
- Analysis shows that there continues to be an argument for adjusting certain individual stresses to allow for diversification relative to growth assets. As such, we believe the current diversification approach used to calculate the growth asset stress factors remains reasonable.
- The current stress for private equity holdings is set equal to the highest quoted equity stress. While the private nature of these assets means that there is, by definition, limited public data on market volatility, consideration was given to using the S&P Listed Private Equity Index Fund. This approach would result in a standalone stress for Private Equity of –26%; however, there are several drawbacks in using this method, including that (i) the index may not be representative, (ii) using a listed proxy for *private* equity adds volatility from being exposed to the daily fluctuations of general public equity markets and (iii) the diversification benefit between public and private equity is likely to be understated by looking at a listed private equity proxy. The advice we received indicated that, for these reasons, a more representative figure would be somewhere between –16% (which is now the highest quoted equity stress) and –26%. Our proposal is therefore to retain the stress at –19%, thereby creating some separation from quoted equities.

12.3. Proposed approach for new asset class stress factors

Diversified growth funds

12.3.1. Unlike the majority of the other asset classes considered as part of this review, there are no widely available Diversified Growth Fund (DGF) indices which could be used to analyse the historical volatility of DGFs.

12.3.2. One way to derive an asset stress for DGFs is to consider the historical volatility of popular DGFs that DB pension schemes are invested in. This can then be compared to a 'proxy' DGF based on asset classes for which we already have proposed asset stresses. Although DGFs have allocations to a wide range of asset classes, typically the most predominant asset classes in these funds are equities and credit assets. Two possible ways to derive a proxy DGF stress are to either calculate a stress based on a composite equity and corporate bond portfolio or take a simple proportion of equity risk.

12.3.3. In the below table Barnett Waddingham LLP compare the actual historical volatility of DGFs over various time periods to the equivalent volatility for a 'proxy' DGF using both of these methodologies.

Period	Average DGF volatility*	Method 1: Proportion of equity risk**	Method 2: Equity proportion for equity-corporate bond proxy***
Jan 2006-Dec 2011	11.7%	63%	64%
Jan 2012-Dec 2016	6.2%	52%	56%
Jan 2017-Dec 2021	7.9%	48%	47%
Jan 2006-Dec 2021	**8.7%**	**54%**	**56%**

** Actual observed historical volatility of DGF returns from the universe constructed by Barnett Waddingham's Manager Research Team over various time periods*
*** Volatility of DGFs as percentage of volatility of global equity returns over the relevant timeframe*
**** Implied equity proportion whereby a portfolio comprising of equity and corporate bond would produce the same volatility measure as the average observed DGF volatility over the relevant periods.*

12.3.4. As can be seen in the above table, the two methodologies for the proxy DGF approach produce similar results. This indicates that a range of around one-half to two-thirds of equity is appropriate when considering the stress to apply to DGFs.

12.3.5. Further, the average DGF volatility calculated above is based on a universe constructed by Barnett Waddingham LLP's manager research team. Therefore, there may be an element of survivorship bias (where the less successful and potentially more volatile funds have been selected out of the universe or have closed). This may mean that the above average DGF volatility approaches could slightly understate real world volatility.

12.3.6. As a pragmatic approach, we propose that the stress for Diversified Growth Funds should be 60% of the stress of developed market equities. This is broadly in line with the volatility observed in practice from a population sample of real world DGF funds.

<u>Absolute return funds</u>

12.3.7. There are many different types of funds that can be classified as Absolute Return Funds, which utilise many different types of asset classes and have materially different risk-return characteristics.

12.3.8. Many hedge funds can also be considered to be Absolute Return Funds. Although hedge funds are no longer going to be a distinct asset class for this purpose, it is worth noting that under the current methodology, hedge funds have an asset stress of -3%.

12.3.9. To demonstrate better the wide range of volatilities, the table below sets out the 5-year annualised volatility for the period to 31 December 2021 for popular Absolute Return Funds that DB pension schemes typically invest in (time period selected based on availability of data).

	Fund 1	Fund 2	Fund 3	Fund 4	Fund 5	Fund 6
5-year volatility (% p.a.)	4.0	5.8	3.2	5.4	2.6	9.7

12.3.10. The data shows that volatilities generally range from 2.6% p.a. to 5.8% p.a. over the period being considered, with one fund showing significantly higher volatility at 9.7% p.a. Our proposal is to stress ARFs at the middle of this volatility range, which would be –5%.

12.3.11. We expect that our proposal will be broadly suitable for the majority of allocations to this class. However, there may in a minority of cases be investments at the high-risk end of the Absolute Return Fund spectrum and we expect those holdings to be directed to the “Other” asset class in the Pensions Regulator’s scheme return guidance. We will develop that guidance in conjunction with TPR and would welcome views from investment professionals connected with pension schemes on potential ways to identify the specific characteristics (or lack thereof) which would place certain ARFs more reasonably in the ‘high-risk’ category.

Non-UK investment grade credit

12.3.12. The current methodology used to stress non-growth-oriented credit assets, can be described as:

- Select an appropriate index which tracks the yields of the relevant credit market;
- apply a linear regression model to model the relationship between how the appropriate duration gilt yields move compared to the credit yields using a monthly sampling frequency; and
- calculate the stress factor by multiplying the slope by the duration of the chosen index (reflecting the correlation between the movements in gilt yields and credit yields).

12.3.13. Given the view that non-UK investment grade credit is usually held as a non-growth-oriented credit asset (i.e., although it does offer incremental spread versus gilts the primary reason pension schemes typically hold it is for its liability-matching characteristics), Barnett Waddingham LLP recommended the above approach is used to set the stress factor for this new asset class.

12.3.14. Under the new tiered approach to asset information (for schemes in tier 2 and above) a stress factor is required for non-UK investment grade credit with a duration both shorter and longer than 10 years.

12.3.15. Investing in non-Sterling bonds can introduce currency risk as UK pension schemes' liabilities are typically denominated in sterling. Given that this credit allocation is not growth-orientated, it is likely currency hedging will be employed to manage the impact of any exchange rate fluctuations on the scheme's investments. Therefore, the proposed stress will ignore the impact of currency risk.

12.3.16. There are a few appropriate (widely available) indices which could be used for deriving the stress factors for non-UK investment grade credit and the main index considered is the iBoxx USD Denominated Corporates Index. This is designed to provide a broad representation of the U.S. dollar-denominated global investment-grade corporate bond market, which makes up the largest proportion of the global credit market relative to other denominations.

12.3.17. We have compared the US index to the iBoxx Sterling Denominated Corporates Annual Yield Index and the monthly stresses (for the proposed reference period 1 January 2006 to 31 December 2021) derived using these indices are set out below:

	Slope	Duration	Stress Factor
Proposed non-UK index *iBoxx $ Corporates – Annual Yield Index*	0.4	n/a	**n/a**
Under 10 years		5	**1%**
10 plus years		13	**4%**
UK Comparator *iBoxx £ Corporates – Annual Yield Index*	0.5	7	**3%**
Under 10 years		5	**2%**
10 plus years		13	**5%**

12.3.18. USD-denominated debt is more diversified against changes in UK gilt yields, which means there is less of a 'hedging' effect to offset a rise in credit spreads in a stress scenario.

12.3.19. Taking this into account, we propose that the stress factor for non-UK investment grade credit for tier 2 schemes is calculated using the iBoxx $ Corporates – Annual Yield Index.

Sub-investment grade credit

12.3.20. Given the increased risk associated with sub-investment grade credit assets (relative to investment grade bonds), as well as limited liability matching properties, we see this as a growth-orientated credit asset.

12.3.21. Like the approach taken for other growth asset classes, we recommend using historical volatility data to set the stress factor for sub-investment grade credit. As some of the assets which can be categorised as sub-investment credit are more illiquid than other asset classes (such as public equity), using a daily volatility measure could introduce stale pricing which results in artificially lower implied volatility. Therefore, for sub-investment grade credit, we propose using a monthly sampling frequency to set the stress factor.

High yield bonds, loans and emerging market debt stresses

12.3.22. Sub-investment grade credit can include a wide variety of a different asset classes such as high yield bonds, loans and emerging market debt. Given each of these asset classes behaves in a slightly different way, Barnett Waddingham LLP considered what the monthly implied stress would be for each of these individual sub-asset classes using the proposed reference period (the period 31 December 2005 to 31 December 2021). (Due to the nature of the indices used, data for the entire reference period is not available for the analysis carried out on Loans or Emerging Market Debt.)

	Proposed stress over reference period
High Yield Bonds *iBoxx USD Liquid High Yield Index (January 2006 onwards)*	**-6.9%**
Loans *S&P Leveraged Loan Index (April 2007 onwards)*	**-5.3%**
Emerging Market Debt *Markit iBoxx USD Emerging Markets Corporates Overall Index* *(February 2006 onwards)*	**-4.8%**

Stresses shown include allowance for diversification as per the current methodology for the current growth asset classes.

Overall stress for sub-investment grade credit

12.3.23. As can be seen in the above table, the implied stress for each of the three sub-asset classes is not markedly different. We therefore do not think it is unreasonable to propose combining these asset classes for the purposes of deriving a proposed stress factor through equal weighting of the individual sub-asset classes such that:

Sub-investment grade credit stress =

stress derived from asset class with return of (1/3 High Yield Bonds + 1/3 Loans + 1/3 Emerging Market Debt)

Using the proposed reference period given above, this produces a sub-investment grade credit stress of -6%

12.3.24. In choosing these specific indices, we are implicitly assuming that there is no currency hedging back to sterling for any of the asset classes. Although we do not think this will be strictly true in all cases, we do believe that this is the most common approach adopted by UK pension schemes for these asset classes, and we do not believe this will materially affect the asset stress applied. We also consider the wider availability of these indices to be of higher priority than using a difficult-to-access index.

Private Debt

12.3.25. Given the higher risk nature of private debt, in addition to the illiquid nature of this asset class, we recommend that a negative stress factor is applied to private debt. Similar to other growth assets, we recommend using historical volatility data to derive the asset stress.

12.3.26. The private nature of these assets means that there is limited public data on market volatility, which makes basing the stress factor on observed historical volatility measures more challenging. We have considered a number of approaches to setting an appropriate factor for private debt, including:

Reference public market debt volatility data

12.3.27. One option is to reference a public debt market index, as there are some similarities in the nature of these assets, e.g., the value is contingent on the underlying debt issuers making a stream of interest and capital payments. In terms of which area of the public debt market would be most appropriate as a proxy for private debt, leveraged loans have some similar characteristics to private debt, such as their floating rate nature; the widespread use of covenants; and typically having a higher priority order in capital structures.

12.3.28. The leveraged loan market is dominated by two regions: US and Europe. Anecdotally, Barnett Waddingham LLP note a slight tilt towards European secured loans among their client base. However, in the interests of pragmatism and noting that that there is not a great difference between the implied stress from different regions, they have suggested referencing an equal split of the US and European indices.

12.3.29. Due to the nature of the indices used, data for the entire reference period is not available for the analysis carried out on Loans or Emerging Market Debt.

	Proposed stress over reference period
US Loans *S&P US Leveraged Loan Index (April 2007 onwards)*	**-5.3%**
European Loans *S&P European Leveraged Loan Index (April 2007 onwards)*	**-4.6%**
50% US Loans, 50% European Loans	**-4.7%**

12.3.30. It is worth noting there are some characteristics observed in private debt not seen in the leveraged loan market, which could see some deviation between experienced volatility in practice. For example, private debt funds are typically more concentrated (fewer bond constituents) than public debt indices which can make the performance more sensitive to the creditworthiness of individual debt issuers. In addition, the illiquid nature of these assets introduces an additional element of risk.

12.3.31. The secondary market for private credit is not as deep and established as for other private asset classes. This can cause asset losses where investors become forced sellers.

Reference data collated from pooled private debt holdings

12.3.32. We do also have access to data on quarterly rates of returns from pooled private debt holdings (covering 'Senior Debt', 'Credit Opportunities' and 'Subordinated Capital' funds) from an external third party, Cambridge Associates. We believe this will give a reasonable representation of potential volatility, given it is based on real world private debt data.

12.3.33. We are also satisfied that:

- The benchmark has sufficient historical data to provide an insight into longer-term trends in volatility.
- The impact of survivorship bias is not material. Distortion from survivorship bias can come about due to failing funds falling out of the index leaving only the surviving funds. The longer-term performance is therefore concentrated on the more successful funds and could perhaps underestimate the risk from this asset class.
- The benchmark is representative of the funds that UK DB pension schemes are typically invested in. If the funds used to make up the benchmark are those commonly seen invested in by pension schemes, then the benchmark should provide a reasonable proxy for private debt risk faced by UK DB schemes.

12.3.34. Based on the Cambridge Associates data we calculated the stress factor as a one standard deviation loss from the calculation of annualised volatility of historical quarterly returns over the period from 31 December 2005 to 31 December 2021, giving a rounded figure of -9%.

12.3.35. We are aware that there is a potential downside of using this data as a reference as it is unlikely that many external stakeholders will have access to the benchmark data so this brings lower transparency/predictability on how the stress may evolve; however, on balance it is our view that the quality of the approach is the primary factor and outweighs the drawbacks. Nevertheless, we welcome stakeholder views on our proposals.

13. Insolvency risk

13.1. The PPF-Specific Insolvency risk model

13.1.1. Our insolvency risk model was originally developed with Experian, but is now operated by our insolvency risk partner, D&B. This model assesses the likelihood of the scheme's sponsoring employer becoming insolvent at the end of each month.

13.1.2. D&B uses a credit scoring model trained on the universe of DB employers. In developing a predictive credit scoring model, it is preferable not to apply a 'one size fits all' approach, but to segment the population into a number of homogeneous sub-populations, with a separate scorecard being developed for each segment.

13.1.3. Clearly, this could very quickly lead to hundreds, even thousands of truly homogeneous micro-segments being created. In practice, besides the obvious time implications of building so many separate scorecards, the reality is that for the scorecards to be statistically robust, and consider as many variables as possible, it is crucial that there are sufficient data points – and specifically enough insolvent businesses within each segment on which to train the model.

13.1.4. No scorecard can capture each firm's unique characteristics. That said, the model performance review of the scorecards used for levy invoicing, both prior to and following COVID-19, continues to give us confidence that the model continues to be fit for purpose.

13.1.5. D&B assesses the likelihood of the scheme's sponsoring employer becoming insolvent at the end of each month. PPF then take an average over the year and place the scheme in the appropriate levy band.

13.2. Model performance review

13.2.1. The PPF applies a credit scoring model to calculate levy charges. During the year to April 2022 the model continued to be fit for purpose.

13.2.2. Ongoing monitoring of the performance of the credit scoring model is essential to evaluate whether the model continues to be fit for purpose. Performance is principally assessed against three key metrics; critically the ability to discriminate between solvent and insolvent employers, ability to predict the number of insolvencies, and levy band volatility.

13.2.3. The model performed satisfactorily in its ability to discriminate between solvent and insolvent employers. The Gini coefficient which measures this, for all PPF scorecards was 47.3% for the period between April 2021 – March 2022. We also recognise the performance of the model is lower than the previous two years.

13.2.4. We also consider the scorecards' ability to predict the insolvency count correctly by comparing the predicted insolvency rate with actual number in the universe. The expected insolvency rate was between 0.50% -0.85%. However, the insolvency count over the period was 0.24% of the PPF employer universe, which is outside the range. As the model is through a cycle model, we have also considered multi-year performance, the model predicted range was between 0.56-0.81%, however the observed insolvency rate was 0.43%, which is also outside of the expected range. The reason for this, is because there have been fewer expected insolvencies for the two highest risk levy bands. With the insolvency rate running at historically low levels, it is not surprising the insolvency experience for these higher levy bands is also more favourable than the model would predict.

13.2.5. The third key metric we consider is levy band volatility. Fifty-two per cent of the population remained on the same levy band. This is higher than the long-term average of 47.6% though lower than the previous year. While 2.4% of the population experienced levy band movement of five or more levy bands, which is lower than last year.

13.2.6. The level of “Net Change” this year (i.e., losers minus winners) was minus 3.0%, materially higher than last year (minus 1.9%) and more in line with the long-term average (minus 3.3%). A level of minus 3.0% demonstrates that there was some bias in sponsors transitioning to a more favourable levy band.

13.2.7. We also review the individual scorecard performance. Our review found that most scorecards performed well. We identified two scorecards that are not performing as well as they could. Scorecard 6, small group companies is still performing below expectations, though performance has improved compared to the prior year. Due to the low insolvency rate, it is difficult to identify the underlying cause and could be impacted by other factors. The performance of scorecard 5, small group companies was also below expectations. Our investigation identified that the scorecard 5 was impacted by two insolvencies (from a total of four) that were part of the same corporate group.

14. Impact analysis

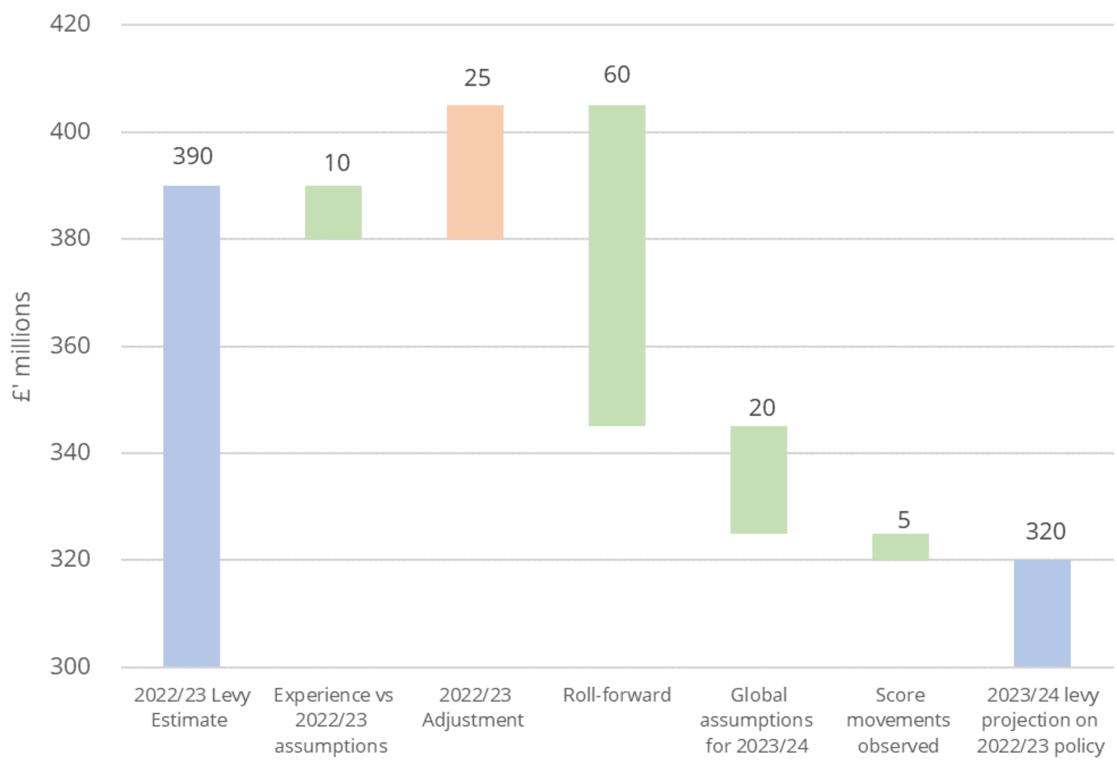
14.1. Change in expected levy collection, before and after impact of policy changes

14.1.1. We have analysed the change from the 2022/23 Levy Estimate to the expected 2023/24 levy collection assuming 2022/23 policy (with the removal of the 2022/23 Adjustment), and then the impact of the policy changes proposed.

14.1.2. Before allowing for the proposed policy changes, the projected 2023/24 levy is £320 million, and the change from the 2022/23 levy estimate of £390 million is made up of:

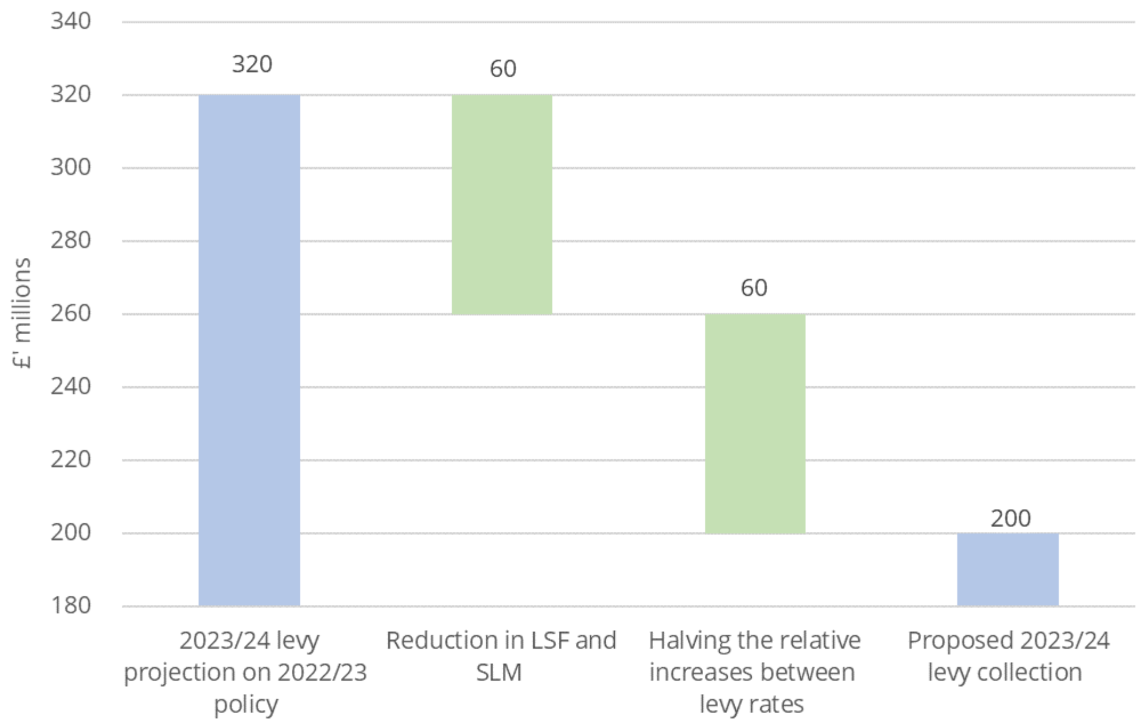
- The impact of incorporating actual 2022/23 data versus the assumptions incorporated into the 2022/23 levy estimate leads to a reduction in levy of £10 million.
- The 2022/23 Adjustment has reduced 2022/23 levies by £25 million.
- The roll-forward, incorporating the change in the Measurement Date from 31 March 2022 to 31 March 2023, decreases levy by £60 million.
- Assumptions for reductions in the risk profile of schemes (as described in chapter 15) for 2023/24 levy purposes reduces expected levy collection by £20 million.
- Observed score movements to July 2022 monthly scores reduces expected levy collection by £5 million.

Change from 2022/23 Levy Estimate to 2023/24 levy projection on 2022/23 policy



14.1.3. The impact of policy changes in aggregate reduces the expected 2023/24 levy collection by £120 million and is split broadly evenly between the reduction in the levy scaling factor and scheme-based levy multiplier and the halving of the relative increases between levy rates.

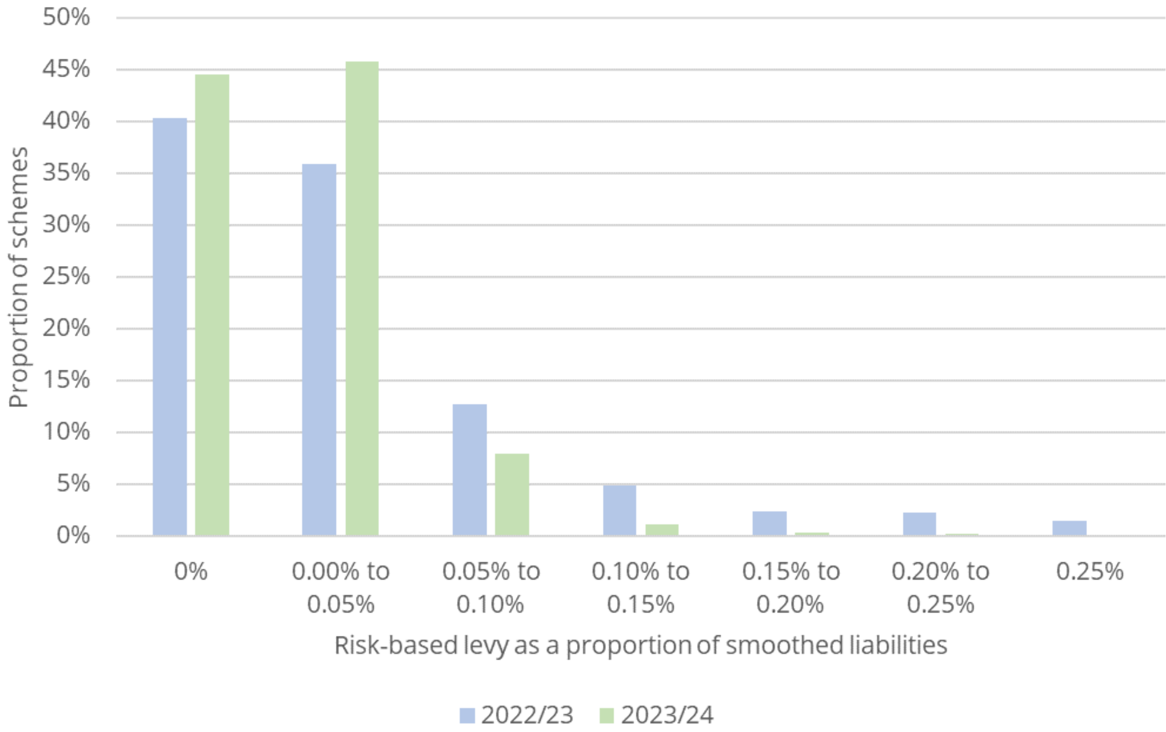
Impact of proposed policy on 2023/24 levy collection



14.2. Impact of policy changes on levy

14.2.1. 96% of schemes paying a 2023/24 risk-based levy are expected to see a reduction in risk-based levy from 2022/23 to 2023/24. The average reduction in risk-based levy, for those schemes that pay a risk-based levy, will be over 50%. The relative affordability of levy bills (measured as the risk-based levy as a proportion of smoothed liabilities) will generally improve across the universe, with the average risk-based levy as a proportion of smoothed liabilities reducing from 0.06% to 0.03%, and c. 90% of schemes paying a risk-based levy less than 0.05% of smoothed liabilities. It is expected that no schemes will have the risk-based levy cap applied in 2023/24.

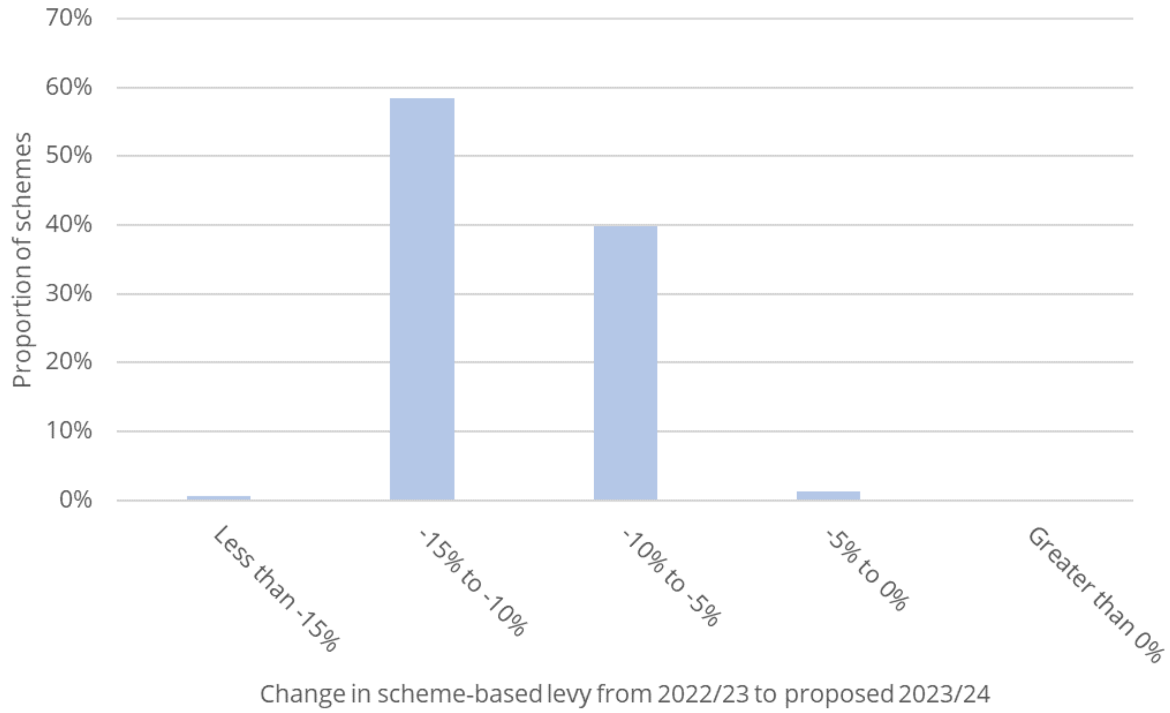
Impact of proposed policy changes on distribution of relative affordability of risk-based levy



14.2.2. Where a scheme sees an increase in risk-based levy, this will generally be because of the removal of the 2022/23 Adjustment, or an increase in insolvency risk.

14.2.3. The reduction in the scheme-based levy multiplier from 0.000021 to 0.000019 will reduce scheme-based levies by almost 10%. Combined with the expected reduction in smoothed liabilities, the majority of schemes are expected to see a fall in scheme-based levy of more than 10%.

Impact of policy changes on scheme-based levy



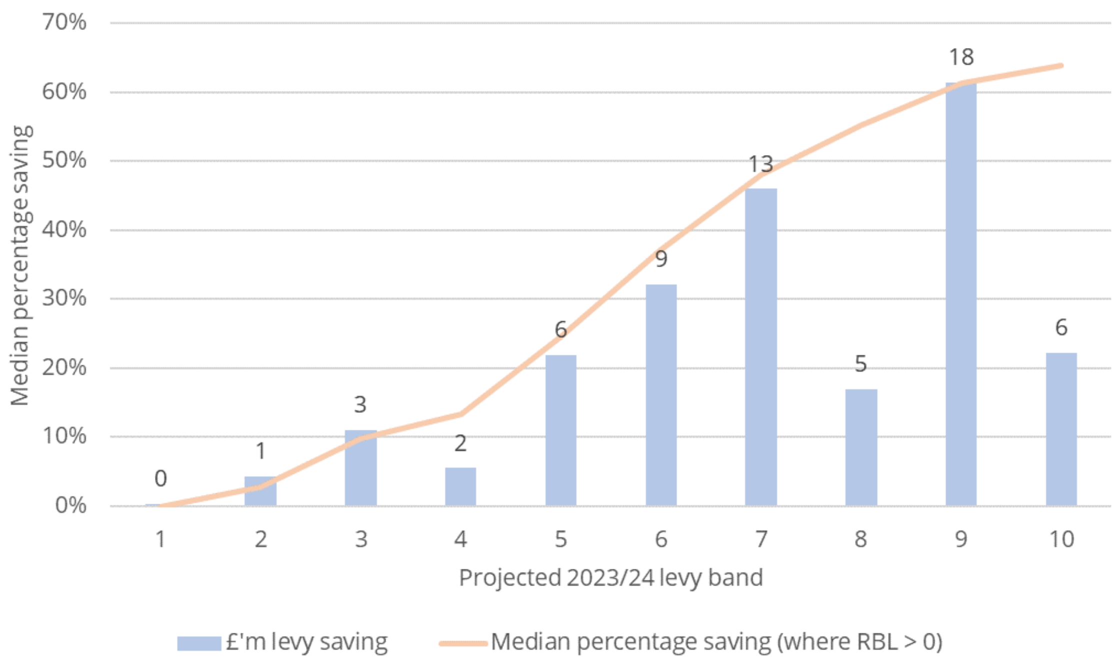
14.3. Impact of policy changes on risk-based levies by levy band

14.3.1. The impact of halving the relative increases between levy bands will reduce levy rates for all employers above levy band 1. To illustrate the impact on schemes, we have assigned a scheme levy band where the Scheme IR (weighted average Levy Rate across employers incorporating the Scheme Structure Factor) is greater than a lower limit and less than or equal to a higher limit, in line with the allocation of levy bands on mean scores. The scheme level allocation is as illustrated below:

Scheme IR Lower Limit	Scheme IR Higher Limit	Assigned levy band	Proposed levy Rates
0	0.0028	1	0.0028
0.0028	0.0031	2	0.0030
0.0031	0.0035	3	0.0031
0.0035	0.004	4	0.0034
0.004	0.0053	5	0.0039
0.0053	0.0081	6	0.0049
0.0081	0.0126	7	0.0063
0.0126	0.0176	8	0.0076
0.0176	0.0239	9	0.0089
0.0239	0.0383	10	0.0116

14.3.2. We have isolated the impact of halving the relative increases in levy rates between bands on 2023/24 risk-based levies – i.e., compared the proposal to using the existing rates. This change reduces levy collection by around £60 million. The chart below illustrates the saving by levy band (we have excluded from the analysis schemes that pay no risk-based levy as their levy band does not affect their levy).

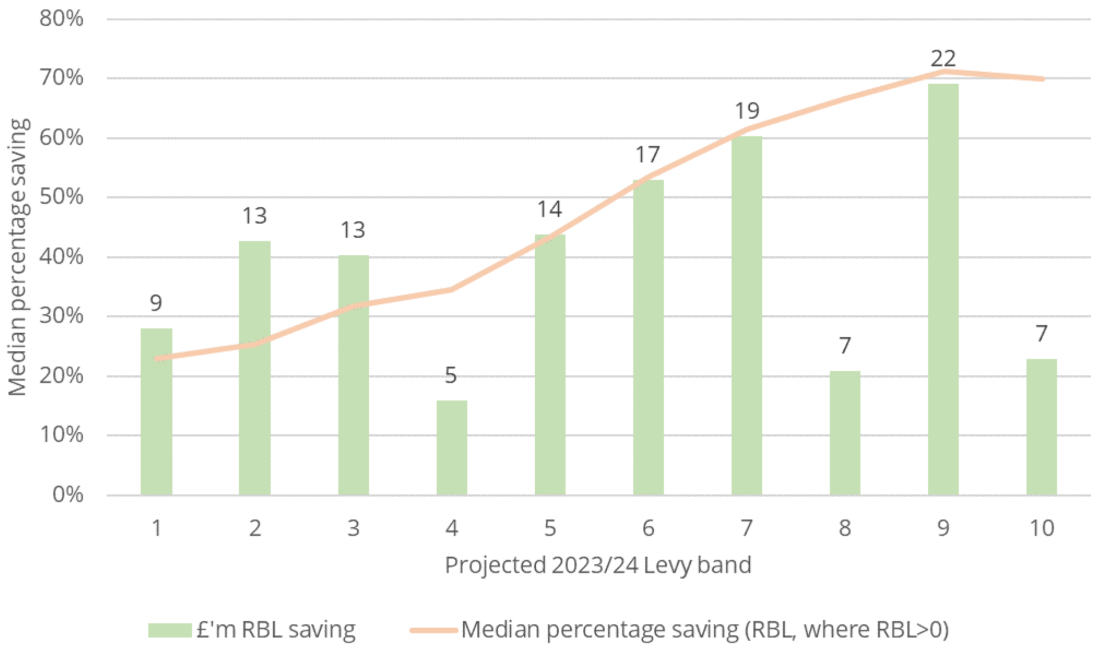
Levy savings from halving the relative increase between bands



14.3.3. More material levy savings are seen at the higher bands where there is a material reduction in levy rates. At these higher bands, aggregate levy saving varies also due to differing starting total levy by levy band. Median percentage saving increases as levy band increases. The increasing trend reflects the bigger reductions in Levy Rates. Savings at the higher levy bands are impacted by a greater proportion of schemes in the highest levy bands receiving the benefit of the RBL cap if the new rules are not in place (so that the decrease is less significant than it otherwise would be).

14.3.4. Further incorporating the reduction to the LSF and SLM, schemes across all levy bands expect to see a reduction in levy:

Risk-based levy savings from proposed policy changes



14.3.5. The combined reductions in levy from the proposed policy changes, together with the expected improvements in funding positions for levy purposes, leads to schemes across all levy band allocations expected to see reductions in risk-based levy as illustrated on chart 5 in section 5.3.

15. Assumptions used to forecast levy collection

15.1. Introduction

15.1.1. Each year, we are required to set an estimate of overall levy collection. We do that by modelling each scheme's expected underfunding and sponsor insolvency scores to arrive at a scheme-level estimate and combine that with the more general trends and impacts we anticipate.

15.1.2. As set out in chapter 5, we have proposed changes to the levy rules, in particular the halving of the relative increases between levy rates, a reduction in the LSF from 0.48 to 0.37, and a reduction in the SLM from 0.000021 to 0.000019. The following subheadings set out our methodology and analysis on these movements that have led to our forecast for levy collection of £200m for 2023/24

15.1.3. We have arrived at the 2023/24 collection after making assumptions about data which will not be known until April 2023 or later.

15.2. Risk reduction

15.2.1. We have retained assumptions that deficit-reduction contributions (DRCs) and new s179 valuation filings will continue to lead to improved funding levels, and hence, a reduction to levy. This has been derived based on recent experience, with consideration of recent increases in yields, and anticipated small off-setting effects of incorporation of G9 into new s179 valuations. For risk reduction measures such as contingent assets, ABCs, and liability hedging investment strategies, given the expectation of increasing funding levels, and the proposed decrease in total levy collection, we have assumed that the reduction in levy from these measures is broadly neutral to that observed in 2022/23.

15.3. Insolvency scores

15.3.1. For 2022/23 levy collection, we have seen aggregate changes in insolvency risk increasing the total levy relative to 2021/22. This is partly due to a net impact of companies being adversely impacted by COVID-19 which were incorporated into accounts filed up to the 31 March 2022 measurement date for 2022/23.

15.3.2. Where the latest accounts were adversely affected by COVID-19, the impact of this will remain at least until new accounts are filed and the COVID-19 impacted accounts will impact 2023/24 mean scores.

15.3.3. Considering the expectation that those companies adversely affected by COVID-19 will see an impact remain into 2023/24, the estimate of levy collection assumes that in aggregate, insolvency risk for 2023/24 remains broadly flat to that observed for 2022/23, incorporating observed score movements to July 2022 monthly scores.