Deficit-Reduction Contributions Appendix

Summary

This is the Deficit-Reduction Contributions Appendix to the Board's Determination under section 175(5) of the Pensions Act 2004 in respect of the 2018/19 Levy Year. It sets out how the amount to be certified should be calculated, and how that amount should be communicated to the Board, in respect of Deficit-Reduction Contributions under Rule G1 of the Levy rules for the 2018/19 Levy Year.

What is in a Deficit-Reduction Contribution Certificate?

1. For the purposes of Rule G1.2 the certificate to be Submitted for Rule G1 must contain:

    - the effective date of the Section 179 Valuation or Post-Transfer Valuation to which the certificate relates (date 1) – see paragraph 2 below for clarification;
    - the last calendar day of the month before the date of the certificate (date 2);
    - the amount of the Deficit-Reduction Contributions;
    - the methodology used to calculate the Deficit-Reduction Contributions (Option Alpha or Option Beta, as set out in this Appendix), and whether actuarial certification applies under Option Beta;
    - the date of the certificate;
    - a statement that the amount certified has been calculated in accordance with the appropriate methodology (Option Alpha or Option Beta as indicated) of this Appendix; and
    - where Option Beta is selected, a statement that the Scheme satisfies the eligibility conditions to adopt this methodology as set out in paragraph 6 of this Appendix.

    Note that some of these contents will be generated automatically by Exchange. The remainder must be entered by:

    - a Fellow of the Institute and/or Faculty of Actuaries, where Option Alpha is selected;
    - the Scheme Actuary, where Option Beta is selected and the actuarial certification requirements set out in paragraph 23 below apply; or
    - an 'appropriate person' (as defined in paragraph 24 below), where Option Beta is selected and the actuarial certification requirements set out in paragraph 23 below do not apply.

2. The certificate should relate to the valuation that will be transformed by the Board to smoothed and stressed Section 179 positions as at Saturday 31 March 2018 (using the Appendices where appropriate).

3. For the avoidance of doubt, separate certification is required for each separate section or Segregated Part of a Multi-Employer Scheme.

4. The information provided in the certificate must be consistent with the amount of the Deficit-Reduction Contributions most recently calculated in accordance with Option Alpha or Option Beta (as indicated in the certificate) of this Appendix.

5. The date of the certificate means the date on which it is Submitted and the certificate cannot be backdated.

Which methodology may be used?

6. Option Alpha may be used by any Scheme. As an alternative, a Scheme may adopt Option Beta provided it satisfies all the following conditions:

   - the Supplied Liabilities of the Scheme are less than £10 million;
   - no benefits were accrued by any Member under the Scheme in relation to any period between **date 1** and the end of **date 2**, including that period in its entirety; and
   - the Scheme had one or more Recovery Plans in force for some period between **date 1** and the end of **date 2**, including that period in its entirety.

7. If the certificate Submitted in accordance with paragraph 1 above states that Option Beta has been used, but the Board subsequently establishes that one or more of the conditions specified in paragraph 6 above is not satisfied, the certificate shall be deemed invalid.

Definitions

8. For the purposes of both Option Alpha and Option Beta as set out below:

   - **date 1** is the effective date of the valuation to which the certificate relates, as described in paragraph 2 above;
   - **date 2** is the last calendar day of the month before the date of the certificate; and
   - references to the **"accounts"** are to the accounts used for the purpose of the valuation to which the certificate relates.

Option Alpha

9. Certification under Option Alpha must be carried out by a Fellow of the Institute and/or Faculty of Actuaries. This includes, but is not restricted to, the Scheme Actuary.

10. In calculating the amount to be certified under Option Alpha, actuaries should make no allowance for any step change in assets and liabilities arising from the coming into force of section 29 of the Pensions Act 2011. In addition, no account should be taken of assets and liabilities in respect of benefits that, between **date 1** and **date 2**, changed status from money purchase to defined benefit, or changed status from defined benefit to money purchase.

11. In particular, where an underpin or a top-up benefit was money purchase at **date 1** but is not at **date 2**, or was not money purchase at **date 1** but has become so at **date 2**, this should not be reflected in the calculation.

12. No allowance should be made for a situation where a Member retires between **date 1** and **date 2** and converts a fund into a pension through the Scheme, thus moving from money purchase to defined benefit.

13. Contributions, accrual, expenses and augmentation costs must all be measured up to the end of **date 2**.

14. The amount of the Deficit-Reduction Contributions under Option Alpha is calculated as:

$$\mathbf{a - (b + c + d + e)}$$

where **a**, **b**, **c**, **d** and **e** are as described in paragraphs 15 to 20 inclusive.

15. **a** is the contribution paid by the Employer(s) and employees (and, where relevant, HM Revenue & Customs in respect of age-related National Insurance rebates) to the Scheme before the end of **date 2**. Allowance should be made only for cash contributions that have been received, irrevocably and in full, by the trustees before the date of the certificate.

    a should include:
    - contributions to the Scheme in respect of Scheme expenses, (where such expenses are paid out of Scheme assets), but excluding contributions in respect of expenses related to investment (including, but not limited to, investment management expenses, investment advice fees, investment consultancy fees and custodian fees);
    - contributions in respect of augmentations to benefits;
    - contributions in respect of the cost of accrual of Scheme benefits between **date 1** and the end of **date 2** that are shown as a liability in the **accounts** at **date 1**; and
    - contributions paid on or before **date 1** if such contributions have not been recognised as an asset in the **accounts** at **date 1** on the grounds that they are payable for a period starting after **date 1**.

    a should exclude**:**
    - contributions recognised as an asset in the **accounts** at **date 1** (even if they are not paid until after **date 1**);
    - contributions in respect of the cost of accrual of Scheme benefits after **date 2** but paid before that date;
    - contributions paid to offset the impact of transactions not reflected in **b, c, d** or **e**; and
    - any payments made to the Scheme trustees to facilitate the purchase of an interest in an ABC Arrangement, together with any subsequent coupon payments made to the Scheme trustees in respect of an ABC Arrangement.

16. **b** is the cost of accrual of Scheme benefits, (subject to the adjustments described in paragraph 4.4.1 of the Section 179 guidance version G7), on a Section 179 Valuation basis between **date 1** and the end of **date 2**. In calculating the cost of accrual:
    - when applying the compensation cap (the first adjustment detailed in paragraph 4.4.1 of the Section 179 guidance version G7), the new cap formula set out in paragraph 4.9.9[1] of G7 should always be used;
    - allowance should be made for salary increases over the period from **date 1** to the end of **date 2**;
    - no allowance should be made for salary increases from after **date 2** to expected retirement date;
    - no allowance should be made for any increase in section 179 liabilities for service before **date 1** resulting from salary increases between **date 1** and the end of **date 2**;
    - any step increase in liability arising when a Member attains normal pension age[2] between **date 1** and the end of **date 2** should not be included;
    - the effective date used in calculating the cost of accrual should be the date halfway between **date 1** and the end of **date 2**; and
    - version G7 of the Section 179 Valuation guidance and version A8 of the assumptions guidance should be used.

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[1] Updated on 1 March 2018

[2] The Board has published the opinion of Andrew Simmonds QC on this term which represents how this should be interpreted.

17. **c** is the amount of expenses (if expenses are met out of Scheme assets) incurred between **date 1** and the end of **date 2,** but excluding expenses related to investment (including, but not limited to, investment management expenses, investment advice fees, investment consultancy fees and custodian fees).

    c includes:

    - premiums for life assurance benefits, where these are paid out of Scheme assets;
    - Value Added Tax included in expense invoices settled from Scheme assets; and
    - expenses associated with the discharge of liabilities, where such expenses are paid out of Scheme assets.

    c excludes**:**

    - expenses related to investment (including, but not limited to, investment management expenses, investment advice fees, investment consultancy fees and custodian fees).

18. **d** is the cost, measured on a Section 179 Valuation basis, of any augmentations granted between **date 1** and the end of **date 2**.

    d includes:

    - benefits for which the Board does not provide compensation (e.g. an augmented lump sum on death in service) and benefits in excess of PPF levels of compensation;
    - the cost of discretionary pension increases granted;
    - increases to the compensation which the Board would be required to provide to Members in the event of its assuming responsibility for the Scheme, where such increases arise from amendments to accrued Scheme benefits;
    - enhanced early retirements made using an augmentation power in the Scheme rules;
    - enhanced early retirements which require the trustees or employer to exercise discretion or grant consent in granting the benefit;
    - benefit augmentations which commence or are discharged after the end of **date 2**, where consents from all parties (Member(s), trustees and Employer(s)) for the augmentation to be implemented were obtained before the end of **date 2**; and
    - benefit augmentations which commence or are discharged between **date 1** and the end of **date 2**, where consents from all parties (Member(s), trustees and Employer(s)) for the augmentation to be implemented were obtained before **date 1**.

    d does not include:

    - early retirements which are an application of the Scheme rules and which do not require the satisfaction of any conditions (e.g. consent, discretion or use of an augmentation power) and which would therefore be deemed to be retirement at normal pension age; and
    - the cost of benefit increases that arise as an entitlement under the Scheme rules without the need for the fulfilment of any conditions or the exercise of a discretion.

The effective date used in calculating the cost of augmentations should be the date halfway between **date 1** and the end of **date 2**. Version G7 of the Section 179 Valuation guidance and version A8 of the assumptions guidance should be used in calculating the cost of augmentations. Where the above provisions require an augmentation to be assessed by reference to PPF compensation levels, the new compensation cap formula set out in paragraph 4.9.9[3] of the Section 179 Valuation guidance G7 should always be used for this purpose.

For the avoidance of doubt, where augmented benefits are granted and discharged between **date 1** and the end of **date 2** (either by payment to the Member direct or to a third party), the cost of the augmentation should be taken as the amount paid to discharge the corresponding benefits, but excluding any associated expenses. The same approach applies where augmented benefits are discharged after the end of **date 2**, but the necessary consents were obtained before the end of **date 2**.

19. **e** is any net benefit outgoings which were paid out before **date 1** but were not reflected in the assets used for the valuation at that date. Where the Scheme holds annuity policies in respect of some or all beneficiaries, the annuity income received by the Scheme should be deducted from the benefits paid out by the Scheme in the calculation of **e**. However, if the annuity income in respect of any Member exceeds the benefits paid out in respect of that Member, the contribution to **e** in respect of that Member shall be nil.

20. Where **a, b, c, d** or **e** cannot be determined exactly, prudent estimation is acceptable, where prudent means that **a** is not overestimated and **b, c, d** and **e** are not underestimated. When applying prudent estimation (as set out in this paragraph), the actuary must have due regard to Rule G1.1(c) of the Determination.

21. No adjustment should be made for investment returns, consistent with the exclusion of investment expenses from the calculations. Therefore, the contributions, expenses, etc. should not be rolled up or discounted in any way.

Option Beta

22. Option Beta is available as an alternative to Option Alpha for Schemes satisfying all the conditions in paragraph 6 above. Certification under Option Beta must be carried out by the Scheme Actuary where the actuarial certification requirements set out in paragraph 23 below apply, otherwise by an 'appropriate person' as defined in paragraph 24 below.

23. The actuarial certification requirements under Option Beta that necessitate certification to be carried out by the Scheme Actuary are:

    - the certified amount of Deficit-Reduction Contributions (**RC + SC** as set out in paragraph 25 below) is greater than £1 million; or
    - the certified amount of Deficit-Reduction Contributions includes contributions not specified in the Scheme's Recovery Plan(s) (i.e. **SC** as defined in paragraph 27 below is greater than zero).

[3] Updated on 1 March 2018

24. An ‘appropriate person’ (who may carry out the certification under Option Beta where the actuarial certification requirements in paragraph 23 do not apply) is any of:

    - the Scheme Actuary;
    - a trustee of the Scheme;
    - a director of a corporate trustee appointed by the Scheme;
    - a director or the company secretary of a sponsoring employer of the Scheme (if such employer is a company);
    - any member of a sponsoring employer of the Scheme (if such employer is a limited liability company); or
    - the general partner of a sponsoring employer of the Scheme (if such employer is a limited partnership).

25. The amount of the Deficit-Reduction Contributions under Option Beta is calculated as:

    RC + SC

    where **RC** and **SC** are as described in paragraphs 26 and 27 respectively.

26. **RC** is the total of the contributions specified in the Scheme’s Recovery Plan(s), (excluding any contributions in respect of Scheme expenses) which fall due between **date 1** and the end of **date 2**, and which were received, irrevocably and in full, before the end of **date 2**.

27. **SC** represents contributions which are not specified in the Scheme’s Recovery Plan(s), but which were received, irrevocably and in full, before the end of **date 2** and which served to either:

    - amend the Scheme’s Recovery Plan in force immediately prior to their receipt; or
    - remove the requirement for a Recovery Plan.

28. **RC** and **SC** should be calculated without reference to the contributions included in or excluded from the asset value in the accounts.

29. It is intended that **RC** and **SC** should be objective, readily quantified amounts, so that estimation is unnecessary. Nonetheless, it is permissible to certify a lower amount than the total of **RC** and **SC**.

30. No adjustment should be made for investment returns. Therefore, **RC** and **SC** should not be rolled up or discounted in any way.