Pension
Protection
Fund

Annual Report & Accounts 2013/14

Protecting people's futures

Pension
Protection
Fund

Annual Report & Accounts 2013/14

Annual report presented to Parliament pursuant to Section 119(5) of the Pensions Act 2004 and Accounts presented to Parliament pursuant to paragraph 22(6) (b) of Schedule 5 to the Pensions Act 2004.

Ordered by the House of Commons to be printed on 17 July 2014.

HC 489

Any enquiries regarding this publication can be referred to us at 0845 600 2541.

This publication is also available for download from our website at **www.pensionprotectionfund.org.uk**.

Print ISBN: 9781474108577
Web ISBN: 9781474108584

Printed in the UK by Williams Lea Group
on behalf of the Controller of Her Majesty's Stationery Office.

ID 27061401 07/14

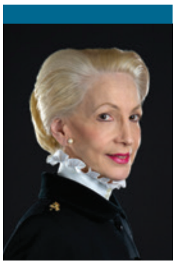
Printed on paper containing 75% recycled fibre content minimum.

Contents

We protect millions of people throughout the United Kingdom who belong to defined benefit schemes.

The top team

Chairman



Lady Judge CBE

Chief Executive

Alan Rubenstein

Executive Board Members

Martin Clarke

David Heslop

Andy McKinnon

Non-executive Board Members

Dick Barfield

John Bevington

Alan Jenkins

Tom Joy

Sharmila Nebhrajani OBE

Arnold Wagner OBE

Baroness Warwick of Undercliffe

Directors

Katherine Easter

Sara Protheroe

David Taylor

Barry Kenneth (joined 3 June 2013)

Chairman's statement

Lady Judge CBE
Chairman

Both the levy and our investment strategy continue to play an important part in helping us remain financially resilient and on track to meet our 2030 Funding Strategy target.

Looking back on our progress over the last year I take great pride in the achievements of the PPF and feel confident about its future.

As discussed last year, we determined that the PPF could deliver an enhanced and more efficient service to our members if we in-sourced many of our important functions. Accordingly, we have recently moved into a new building designed to support the in-sourcing of our member services. Over the coming year we will be recruiting approximately a hundred new staff to bring about this transformation in our approach to these important functions, and I look forward to the contribution they will make toward our goals.

A major focus during the past year has also been the development of a new levy framework in partnership with Experian (our new insolvency risk provider), our Industry Steering Group (which brought together representatives from key collective stakeholders), and a range of other experts.

We have made great strides over the current three year levy cycle and our levy payers have indicated that they appreciate the stability we have delivered during what has been a period of economic uncertainty. In the past they have also requested that we provide greater clarity about the various factors which affect their levy bills. As a result of these comments I am pleased to report that the model we have developed and on which we consulted this summer, and which will be finalised in the autumn, will provide both greater transparency and predictability for levy payers.

Both the levy and our investment strategy, which continues to be recognised as best in class both nationally and internationally, play an important part in helping us remain financially resilient and on track to meet our 2030 Funding Strategy target.

In keeping with our role, we strive to maintain best practice in managing our risks. This goal is central to the PPF's success. As a consequence, in the past year the Board determined that it was appropriate, with the growth of our assets and the in-sourcing of our member services, to introduce a Risk and Audit Committee with a clear mandate to oversee the risks across the business. With our increase in size and scale we have also implemented an enhanced risk management framework which has been embedded throughout all areas of the PPF.

I am also pleased that our financial position strengthened again during the year. As you can see, we are reporting a surplus in our Annual Report and Accounts and continued improvements in our estimated probability of success. Our financial results demonstrate that we are making good progress towards our target of being self-sufficient by 2030. Many of the specifics of our achievements are set forth in the Chief Executive's Report, which I am pleased to say highlights our continued excellent performance in all areas of our statutory functions.

Chairman's statement

It is important to remember that the mission of the PPF is part of the larger pensions landscape. This is an exciting time for all those involved in UK pensions. Whether it is the liberalisation of defined contribution benefits announced in this Spring's Budget, or the Government's intention, as set out recently in the Queen's speech, to permit increased risk-sharing and innovation in the private pensions market, public engagement with pensions has rarely had greater necessity or coverage. When viewed alongside the success of auto-enrolment and the work being done to simplify the State pension, we understand that we are in the midst of a genuine transformation of the pensions landscape. I believe that if delivered successfully, it will provide members both greater certainty and greater flexibility in their retirement planning, whether they are in a workplace or private pension scheme.

We are pleased to have a role to play in this process and hope to be able to share our knowledge and experience to achieve better outcomes for UK pension schemes and their members.

I continue to believe that our heightened engagement is important and that we should be encouraged by the Government's drive and will for reform. We understand that both the US and Europe are watching the UK's pensions reforms with great interest because they face the same challenges as we do in their own countries.

Finally, I would like to thank our entire Board, our Executive team and all people at the PPF for their extraordinary efforts and dedication in delivering our mission to provide our members with the service, security and confidence they need in their most difficult times. I would particularly like to take this opportunity to thank Martin Clarke, our Executive Director of Financial Risk, who is leaving us at the end of July to take on another senior government position. Martin has made a very important contribution to the PPF over many years and I wish him well in his new challenge. Furthermore, I would also like to congratulate Sharmila Nebhrajani who was appointed OBE in this year's Queen's Birthday Honours list.

In conclusion it gives me great pleasure to say that as we enter calmer economic waters, the UK's pensions lifeboat continues sailing steadfastly towards its goal of self-sufficiency by 2030.

Chief Executive's review

Alan Rubenstein
Chief Executive

We were delighted that our successful and innovative investment approach was recognised with a number of awards during the year, including IPE's 'European Pension Fund of the Year', the first time this award has been made to a UK organisation.

It has been another year of significant achievement and growth for the PPF.

We have continued to develop in scale, in membership and in our operational capability. By the end of the year we were protecting over 199,000 members, were managing over £16 billion of assets, with a funding position of 112.5 per cent, and reported a surplus of £2.4 billion.

A major contributor to the strength of our balance sheet continues to be our investment strategy. Across 2013/14 our assets outperformed our liability benchmark by 2.9 per cent, whilst our total asset return was a small negative of 0.7 per cent. Key contributors to our outperformance were the results from our global equity portfolio and material contributions from our alternative credit and property portfolios. In the same period our liabilities decreased, principally due to the effect of higher gilt yields and updates to our mortality assumptions. We were delighted that our successful and innovative investment approach was recognised with a number of awards during the year, including IPE's 'European Pension Fund of the Year', the first time this award has been made to a UK organisation.

During the year we have benefitted from the upward trend in the economy, and following a record year for claims in 2012/13, our experience over the last 12 months has been lighter. This has been mirrored by a marked improvement in scheme funding more generally, as measured by the PPF 7800 index. While challenges remain, our current assumption is that this trend will continue, with a steady improvement in our risk profile.

We are working harder than ever to ensure that the PPF operates as efficiently as possible so that we can maximise the Fund's size and scale. By making our assets and levy collections work as effectively as possible we can continue to offer value for money for our levy payers and ensure our members can remain confident in the protection we offer them.

In 2014 we expect to reach our long-held target of completing 75 per cent of scheme assessments within two years. Getting to a position where we can deliver this has been a long journey, and has required support and engagement with schemes, advisors and trustees to understand our processes and greatly improve data standards. Delivering this plays a significant part in our members' experience. We know that providing people with certainty about their future as soon as possible gives them real confidence about planning and living their retirement.

We have achieved these changes by transforming the way we manage schemes. A major focus to support this has been on extending our approach to partnership working during the year. We have set up three new panels for trustee advisory, audit and assessment legal services, all of which will help make sure assessment processes are completed quickly and efficiently.

The largest single insolvency we have had to deal with during the year was UK Coal. It became clear in July 2013 that the scheme would have to enter the PPF because of the size of its deficit.

Chief Executive's review

We were satisfied that when we agreed an innovative plan to allow the business to continue it offered better long-term returns for the PPF than simply letting the company collapse into insolvency. It also meant that 7,000 pension scheme members would be protected by the PPF, with 2,000 jobs secured in the company.

It is unfortunate that since then a combination of adverse exchange rates, poor international coal prices and challenging operating conditions have severely damaged the company's long-term prospects, which has required an alternative approach going forward. However, this will not result in any additional liabilities for the Fund, while we expect to make a recovery from any restructuring that is at least as valuable as if UK Coal had passed into immediate liquidation last July.

2013/14 was the second year of the first three year levy cycle which was designed to provide levy payers with predictability and stability over the three year period. I am pleased to report that despite the uncertain economic environment over that three year period, we are on track to deliver. In September 2013 we confirmed our intention to leave the rules unchanged for the final year of the levy framework and a levy estimate of £695 million for the 2014/15 year. I am pleased to say that thanks to the improvements in scheme funding we have seen over the last twelve months, we currently expect actual levy collections for 2014/15 to be closer to £650 million, a reduction which I am sure will be appreciated by levy payers.

Since July 2013, when we appointed Experian as our new insolvency risk provider, we have been working with our Industry Steering Group and a range of other experts to develop our proposals for the next three year levy cycle which will begin in 2015/16. Our basic aims remain the same, to provide levy payers with predictability and stability, but in addition we intend to improve both transparency and risk measurement.

The new model will deliver this but it will look and feel different. Over the remainder of the year we will be consulting on and finalising the New Levy Framework which we published in May. A significant aspect of our revised approach is that we have been able to develop a model that is based solely on the experience of sponsors of defined benefit schemes, something that has only now become possible, thanks to the accumulated history of claims experience we now have.

The approach for the model we have developed follows an industry standard approach, but crucially is based solely on the population of PPF eligible schemes, combined with our experience of insolvency over the PPF's lifetime. As result it provides a more predictive 'failure score' for employers of PPF eligible schemes. One benefit of our new approach is that we have been able to reduce the number of factors that feed into a PPF specific scorecard, to between five and seven components. These components will be driven purely by financial data, excluding a number of other factors which form part of the standard models, but which analysis shows are better indicators of insolvency risk for younger, smaller companies, rather than the group with defined benefit pension schemes. This responds directly to one of the most common complaints about the previous model.

Chief Executive's review

Moving our member services in-house will continue to be a significant part of our work over the coming year. It is, after all, the biggest operational development we have undertaken since our inception in 2005. Throughout the year we have been focused on getting the preparatory work right, because at the heart of this change is our commitment to our members, and we want to ensure that when we 'go live' we deliver an excellent customer service built around their needs.

Our move to a new modern building will provide us not only with the platform to supply our member services in-house, but importantly will also help deliver the facilities and systems we need across the breadth of our growing operational requirements.

As an organisation we are committed to creating a culture for our staff to strive for excellence, to feel their contributions are valued and to develop to their full potential. We believe by fostering this environment our people will live our values and fully support and deliver our strategic objectives. Therefore it was a real highlight of the year that we were named amongst the Sunday Times Top 100 Best Companies to Work For in the Not-For-Profit Sector for 2014. This was a big step forward for us (in previous years we have been in the One To Watch category) and demonstrates our continued desire to make the PPF a great place to work.

On that note, I would like to thank all the PPF staff for their hard work and commitment over the past year. It is they who truly make this a great place to work. I look forward to continuing to develop this strength in the year ahead so that we can continue to pursue better outcomes for our members, stakeholders and partners.

As Accounting Officer, I endorse the statements contained in the Directors' Report and Strategic Report.

Alan Rubenstein
Accounting Officer
10 July 2014

Directors' Report
This is what we do

Fraud Compensation Fund

We also pay compensation to members of work-based pension schemes of all types whose employers become insolvent and their schemes have lost out financially because of dishonesty.

The compensation is paid for through a separate levy on all pension schemes.

Financial Assistance Scheme

The Government handed over responsibility for the day-to-day running of the Financial Assistance Scheme (FAS) to the PPF in July 2009, although all FAS activities remain funded by the taxpayer rather than by a levy.

The FAS pays financial assistance to people who belonged to certain defined benefit pension schemes which are ineligible for PPF compensation.

We protect around 11 million people throughout the United Kingdom who belong to defined benefit, eg final salary, pension schemes.

If their employers become insolvent, and their pension schemes cannot afford to pay people their pensions, we will compensate them financially for the money they have lost.

More than a hundred and fifty thousand people now receive compensation from us, and hundreds of thousands more will do so in the future.

We get the money we need to pay compensation in a number of ways. We:

- charge a levy on all eligible pension schemes
- take on the assets of schemes that transfer to the PPF
- recover money, and other assets, from the insolvent employers of the schemes we take on, and
- invest all income and assets as part of a prudent yet innovative strategy, aimed at making sure we can pay members' compensation for as long as they are entitled to it.

The PPF is a public corporation, set up by the Pensions Act 2004, and is run by an independent Board. It reports to Parliament through the Secretary of State for Work and Pensions.

Further information relating to how we manage the organisation can be found in the Strategic Report, Governance Statements and the Financial Statements and accompanying notes.

Directors' Report
Financial performance and highlights

Review

Andy McKinnon
Chief Financial Officer

Our financial position continued to strengthen during the year, as evidenced by the increase in our funding ratio to 112.5 per cent. Returns from our investment portfolio surpassed changes in our liabilities and the return on our risk-seeking assets once again generated a positive return in excess of target.

A further 107 schemes made a claim on the Pension Protection Fund in a moderate year for claims. Levy collections were reduced by 11 per cent while total compensation paid to members rose by 34 per cent.

We were able to further reduce the average administration cost per member from £81 to £79 as part of our ongoing commitment to maintaining tight control over the resources allocated to running an operation that is growing both in scale and complexity.

	At 31 March 2014	At 31 March 2013	
Likelihood of meeting target of being financially self-sufficient by 2030	90 per cent	87 per cent	↑3pts
Funding level calculated on an actuarial basis	112.5 per cent	109.6 per cent	↑2.9pts
PPF investments	£16.25 billion	£14.86 billion	↑9%
Actuarial liabilities for members transferred to the PPF	£12.86 billion	£11.83 billion	↑9%

	Between 1 April 2013 and 31 March 2014	Between 1 April 2012 and 31 March 2013	
Total compensation paid to members	£445 million	£332 million	↑34%
Total net income generated	£642 million	£669 million	↓4%
Total levies raised, including Fraud Compensation Fund (FCF)	£577 million £nil (FCF)	£644 million £4 million (FCF)	↓11%
Operating costs	£48 million	£45 million	↑7%
Value of new claims from schemes entering PPF assessment	£619 million	£1,028 million	↓40%
Investment return	(0.7) per cent	11.1 per cent	↓ 11.8pts
Total assets from transferred schemes	£1.34 billion	£2.15 billion	↓38%

Directors' Report
Financial performance and highlights

David Heslop
Chief Operating Officer

Our role is to ensure that we pay the right compensation and assistance at the right time to all our members. Of the £1.2 billion in compensation we have paid since we were first set up, over a third was paid out in 2013/14.

We aim to provide reassurance to pension scheme members by moving schemes through PPF assessment and FAS wind-up processes as quickly as possible and to the highest possible standards. We achieved our target of completing the wind-up of 125 FAS schemes during the year, and were assisting 160 schemes in PPF assessment by the end of the year.

PPF

Between 1 April 2013 and 31 March 2014:

- 27,109 people transferred to the PPF, making a total of 199,127 deferred and active members
- 33,048 people were members of schemes that completed the PPF assessment period during the year, and
- the excess of assets over liabilities in respect of those schemes already transferred into the PPF has increased from £3.3 billion to £3.6 billion, corresponding to an increase in the funding ratio from 127 per cent to 128 per cent for schemes already transferred.

Since 2005, we have paid out a total of £1.2 billion in compensation, of which £445 million was paid out in 2013/14.

By the end of the year, we were supporting 160 schemes in the assessment period with assets of £5.3 billion and potential liabilities to the PPF of £6.5 billion.

FAS

Between 1 April 2013 and 31 March 2014:

- 125 FAS schemes completed wind-up which meets the target we set ourselves at the beginning of 2013/14 of 125. As a result, £436 million of scheme assets had transferred to the Government
- the number of people receiving FAS assistance increased from 30,927 to 40,894 and the FAS paid out £159 million, and

This means that since FAS started, a total of £479 million has been paid out. 1,298 schemes had looked to qualify for the FAS, and by 31 March 2014 1,052 of these schemes had actually qualified.

Strategic Report
Our strategic framework

Review

David Taylor
Director of Strategy and Legal Affairs

At the beginning of 2012/13, we reshaped our strategy around three key updated objectives. These were designed to reflect a mature organisation which has significant experience of managing risks in the defined benefit pensions universe. They are focused on meeting the challenges of significant growth in the future.

Our vision to **protect people's futures** continues to be what the PPF is all about – and our mission to **pay the right people the right amount at the right time** remains unchanged since we opened our doors for business in 2005.

But we never let ourselves become complacent. At the beginning of 2012/13, we reshaped our strategy around three key updated objectives. These were designed to reflect a mature organisation which has significant experience of managing risks in the defined benefit pensions universe. They are focused on meeting the challenges of significant growth in the future.

The updated objectives are:

1. Meet our funding target through prudent and effective management of our balance sheet

It is essential that we have the funds to pay members the compensation to which they are entitled. We have set ourselves a target of being financially self-sufficient by 2030 and we measure our probability of success in meeting this target and assess the impact of our decision making by reference to that probability.

2. Deliver excellent customer service to our members, levy payers and other stakeholders

Highlighting the importance of customer service through a strategic objective builds on the work we have carried out in previous years. It also helps prepare ourselves for bringing PPF member services in-house, the biggest strategic change we have ever embarked on.

3. Pursue our mission within a high calibre framework of risk management

Risk management has always been one of our key strategic objectives. At the start of 2013/14, we began implementing an enhanced risk management framework which will make sure financial and non-financial risk management is embedded across all areas of the PPF.

We constantly measure our performance against these strategic objectives and to achieve them we need to make sure our operations are built on solid foundations.

This means that our people will have the right skills, experience and knowledge that we need, we are demonstrating the efficiency of our processes and continually striving for excellence, and we are communicating what we do, both internally and externally, to provide confidence in our ability to deliver our mission.

Underpinning these objectives are our foundations of people, communications, and efficiency and effectiveness.

Strategic Report

Meet our funding target through prudent and effective management of our balance sheet

Andy McKinnon
Chief Financial Officer

"Managing our balance sheet effectively is both a fundamental part of making sure we are able meet our commitments to our members, and also of ensuring that we achieve our aim of financial self-sufficiency by 2030.

Background

We have set ourselves a funding target of reaching financial self-sufficiency by 2030 by which time our research indicates that future claims on the PPF will be low, relative to the size of our liabilities, and we will be far less reliant on future levy income, if at all.

Meeting this target depends on more than managing our investment portfolio. We also have to transition the investment strategies of transferring schemes to match our own, put levy collections to work with our fund managers quickly, and make sure we get the best deal for members when sponsoring employers fail.

While we finished 2013/14 in a strong position, with a 90 per cent probability of meeting our 2030 target, we have always been mindful that there are clear risks to us over the coming years. Scheme funding remains at relatively low levels which, in the short term, means that we are likely to have to absorb larger deficits from schemes transferring to us than has been the case. Economic growth has improved during the year, but sustained recovery remains uncertain for a number of sponsors of defined benefit pension schemes.

Managing our balance sheet properly is a critical and fundamental part of making sure we meet our commitments to our members.

Funding for the future

To be financially self-sufficient, we must be fully funded, with limited exposure to market, inflation and interest rate risks, and hold reserves that are sufficient to protect against unexpected levels of residual risk such as future claims and the possibility of people living longer than we estimate.

By 31 March 2014, we were 90 per cent confident of reaching our funding target by 2030.

This was supported by a balance sheet which was £2.4 billion in surplus, up £0.6 billion on the previous year. Our investment portfolio has grown from £14.9 billion in 2012/13 to £16.3 billion and we recorded a total return of (0.7) per cent on our own invested assets for the financial year.

Strategic Report

Meet our funding target through prudent and effective management of our balance sheet

Review

Long-term Funding

At the beginning of 2013/14 we were in a strong position to face the financial challenges of the year ahead. Our robust investment performance meant we could offset a record year of claims on the PPF, in excess of £1 billion in 2012/13.

During the year, there was an improvement in two key risk indicators. An increase in long-term gilt yields meant that the funding level of schemes in the PPF universe, as measured by our 7800 index, showed substantial improvement. Also, we saw improvements in the credit ratings of sponsoring companies.

All of this has increased our chances of reaching our self-sufficiency target. Furthermore, in tests carried out in 2013/14, our funding target remains achievable even under stressed scenarios.

However the recovery outlook, both for funding and insolvencies, remains uncertain and so we continue to be vigilant about the level of anticipated future claims. The new sustainable growth objective for the Pensions Regulator is a particular source of future uncertainty for us which we are not yet able to quantify.

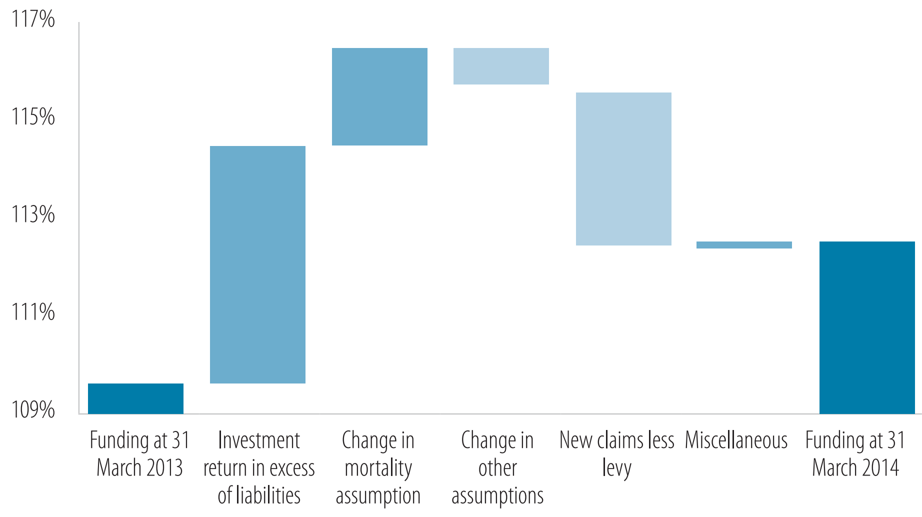
During the year we reviewed the reserves we need to allow for adverse experience once we reach self-sufficiency. We concluded that a target of 110 per cent funding in 2030 remains appropriate for the time being, and we have also now included an explicit allowance within this reserve for operational risk as well as longevity and future claims risks.

Our financial position

Following our record claims year in 2012/13, we enjoyed a period of comparatively light claims experience during the year, with the significant exception of the UK Coal pension schemes in July 2013.

We have built up a large body of knowledge from our experience over the last nine years and continue to use this to improve the accuracy of our actuarial valuations. This year, for instance, we have changed our approach to the mortality assumptions for schemes in assessment which are now based on the actual experience of our members.

This, combined with our investment performance, has resulted in an improved funding level of 112.5 per cent, representing a surplus of £2.4 billion.



Strategic Report

Meet our funding target through prudent and effective management of our balance sheet

Barry Kenneth
Chief Investment Officer

Our investment strategy remains robust as it has done throughout the global financial crisis and the early stages of recovery. Our invested assets have outperformed their liability benchmark by an average of 2.6 per cent during the past three financial years.

Investment performance

Our investment strategy continued to be a major contributor to the solidity of the balance sheet, as the value of our investments increased relative to the value of our liabilities.

The target growth rate of assets continues to be 1.8 per cent a year relative to our liabilities, within the conservative risk constraints set by the Board.

During 2013/14, our invested assets beat our liability benchmark by 2.9 per cent (2012/13: 4.6 per cent). Our total asset return excluding the LDI hedging programme was 3.4 per cent, and (0.7) per cent including the LDI hedging programme. The LDI hedging programme is designed to offset the movement in liabilities as a result of interest rate and inflation movements. The combination of interest rates and inflation rates during the year resulted in a reduction in liabilities.

Our global equity portfolio was again the key contributor of financial outperformance delivering 19.5 per cent. We also had material contributions from our alternative credit and property portfolios.

Our investment strategy remains robust as it has done throughout the global financial crisis and the early stages of recovery. Our invested assets have outperformed their liability benchmark by an average of 2.6 per cent during the past three financial years.

We continued to develop our investment strategy during the year by restructuring our global equity portfolio to a lower volatility based strategy, restructuring our panel of Global Tactical Asset Allocation (GTAA) Managers to broaden the sources of return from this sector, and appointing a new panel of global real estate managers. We are also evolving our fixed income strategy to include more illiquid investments and have procured managers in order to help exploit this opportunity.

Our assets continued to grow substantially through the year, incorporating the transfer of assets from schemes entering the PPF (£1.3 billion), levy collection (£0.6 billion) and net investment returns ((£0.1) billion).

Strategic Report

Meet our funding target through prudent and effective management of our balance sheet

Recoveries

Recoveries from insolvent employers continued to be an important income stream. We have now made, or expect to realise in the future, £1.6 billion in recoveries since we were first set up.

About a third of this money has come from restructuring deals affecting companies which otherwise are certain to become insolvent and whose pension scheme members we are responsible for compensating. We will support such deals only if they offer a better return to the pension scheme as a creditor than if the company were to become insolvent in the usual way.

One of the highlights of the year involved the Kodak Pension Plan in October 2013. We provided formal consent to the transfer of members of the plan to a new pension scheme set up in the wake of the global restructuring of the Eastman Kodak company and the UK-based sponsor of the scheme, Kodak Ltd.

Plan members voted overwhelmingly for the launch of the new pension scheme in which they will receive better benefits than if the scheme entered the PPF. We saw this as an innovative outcome which not only works in the best interests of the pension scheme members but, because we no longer faced taking the full liabilities of the scheme, also meant good news for our levy payers.

Another prominent deal of the year was one which we struck with UK Coal in July 2013 after it became clear that it was inevitable that the pension scheme would have to enter the PPF due to the company's insolvency as a result of a fire in one of its deep mines.

This innovative restructuring of the company's mining operation not only meant that its 7,000 pension scheme members would be protected by the PPF but it also secured 2,000 jobs. Unfortunately, external economic factors led to a further restructuring of UK Coal after the year end. Although this will mean the PPF will not enjoy the benefit of future cashflows, the overall outcome is expected to be no worse than if insolvency had occurred in July 2013, as noted in the Chief Executive's review.

Transfers and transitions

During the year, we collected £1.3 billion in cash and other assets from schemes which entered the PPF. To transfer these assets into the PPF's investment strategy economically and with minimal risk, we transition them in batches throughout the year.

In 2013/14, we completed two large-scale transitions which totalled £1 billion worth of assets. Such transitions, which are carried out by specialist managers under the close supervision of our in-house team and independent advisors, involve a complex series of transactions between many different fund managers and portfolios.

Fund managers

Assets under management now amount to over £16 billion.

During the year we continued to develop the GTAA panel, appointing a further nine managers. This enlarged panel will form part of our alternatives portfolio and provide a flexible approach to the growing needs of the business.

GTAA differs from traditional approaches to fund management. As an asset class it tends to have enhanced diversification properties, which helps control the level of risk that we face and this fits in with our overall low-risk investment philosophy.

Strategic Report

Meet our funding target through prudent and effective management of our balance sheet

We also announced during the year that we are looking to recruit additional real estate investment managers to meet our growing and diverse needs.

During the year we looked to increase our investments in property through pooled funds in Asia Pacific, Europe and the United States and therefore sought to recruit additional managers. In April 2014 we confirmed the appointment of six managers to our Global (excluding UK) Real Estate panel.

Our website includes details of the PPF's new and unique approach to rating its external managers for their commitment to responsible investment. Fully integrated into our wider performance monitoring framework and covering the entire range of asset classes in which the Fund invests, it is based on five performance areas: alignment, ESG (environmental, social and governance) integration, stewardship, resources and reporting.

Best practice

We continually strive to learn from developments and best practice of other industries, and this year we developed our own ORSA (Own Risks and Solvency Assessment), a formal risk management process that is being adopted by insurance companies in response to strengthened European solvency and reporting requirements.

Awards

During the year, our investment strategy continued to be well-recognised and highly praised in the industry.

November 2013
Investment Pensions Europe Awards 2013
Gold Award - Best European Pension Fund

November 2013
Investment Pensions Europe Awards 2013
Best UK Fund

November 2013
Investment Pensions Europe Awards 2013
Silver Award - Best Public Pension Fund

May 2013
AICIO European Innovation Awards 2013
Public Pension Scheme Above
15 Billion Euros

May 2013
Portfolio Institutional Awards 2013
Best Implementation of Responsible Investment

May 2013
Financial News Excellence in Pensions 2013
Best Investment Strategy (DB)

Review

Strategic Report

Meet our funding target through prudent and effective management of our balance sheet

Jeff Wickett
Head of Levy, Risk and Facilities

"As previously indicated, we announced in September 2013 our intention to leave the rules for the levy unchanged for the 2014/15 levy year. We therefore maintained our commitment to keeping the rules the same to provide the predictability individual levy payers look for.

Setting and collecting the pension protection levy

Setting the levy

2013/14 was the second year of the new levy framework which was designed to make bills more predictable than ever before by limiting changes within the three year levy cycle, something levy payers have been asking for. Our formal levy estimate for 2013/14 was £630 million. Subsequent to the levy estimate for 2013/14 being set we revised our forecast downwards to £605 million as a result of the original underfunding and insolvency risk estimates being reduced.

As previously indicated, we announced in September 2013 our intention to leave the rules for the levy unchanged for the 2014/15 levy year. This is the third year of the new framework and the PPF maintains its commitment to keeping the rules the same to provide the predictability individual levy payers look for.

The pension protection levy estimate for 2014/15 is £695 million, an increase of about 10 per cent on the 2013/14 levy year. We confirmed this in December 2013 when we published the 2014/15 levy determination. However, we also stated that we would actually collect a lower sum if trends in scheme funding continue. As at the time of writing there is nothing to change our view that a lower collection than the estimate is likely.

We said at the time that the risks we face as an organisation remained high, with low bond yields and substantial scheme deficits still part of the landscape. The increase is in line with our expectations which we signalled to levy payers was likely when announcing the previous year's levy estimate and again in June 2013.

We also highlighted that while the overall levy will rise by about 10 per cent, individual bills will vary, with a greater average increase, reflecting changes in individual risk and the smaller pool of eligible schemes.

Collecting the levy

In the previous year, we invoiced 90 per cent of schemes by the end of October and said that we would want to improve on that in 2013/14. This we achieved by invoicing the same number of schemes by the end of September, bringing the total invoicing period for the large majority of schemes down to one month.

Schemes will therefore have a better idea when their invoice will arrive as well as how much it is likely to be. The invoicing period is now matched with a shorter collection period so that our investment team can put money to work as soon as possible. This not only benefits our members but also provides certainty to our levy payers.

Strategic Report

Meet our funding target through prudent and effective management of our balance sheet

Experian

We announced in July 2013 the appointment of Experian as our new insolvency risk provider, replacing Dun & Bradstreet. The changeover is due to take place from the year 2015/16 which marks the start of the new three-year levy cycle.

Assessing the risk of an employer becoming insolvent, which could mean its pension scheme entering the PPF, is at the heart of how we calculate individual levies and how we assess our overall risk. Therefore it is essential that we have the most suitable supplier to meet our future needs.

We decided to appoint Experian following a rigorous tendering exercise and tasked them to work with us, and industry stakeholders, to develop a PPF-specific insolvency risk model. This took several months to develop and we believe that a model built to high standards, and based on actual PPF insolvency data and our own cross-section of risks, is a much more appropriate model than a proprietary model based on a more general and not strictly representative population of risks.

It will, among other things, enable levy payers to better predict their failure scores, provide greater transparency about how their scores are calculated, offer improved appeals and monitoring arrangements and generally provide stability over time for levy payers.

Levy payers need to be aware that there will be differences in the scores when they access them because they will be overwhelmingly driven by financial data, but we will be providing levy payers with the opportunity to understand their new scores and, where necessary, challenge them before they are used for levy calculations. This is a major change for the PPF in calculating and setting individual levies that will be more predictable and stable than ever before.

Levy payers were able to get their new insolvency scores from May 2014 but we will not be using Experian scores to calculate individual levies until the 2015/16 levy year, the start of a new three-year levy cycle. We expect to use monthly scores for the six month period from October 2014 to March 2015 for the purpose of 2015/16 invoices.

Strategic Report

Meet our funding target through prudent and effective management of our balance sheet

Contingent assets

Schemes certified 827 contingent assets to us for the 2013/14 levy year, which resulted in a total levy reduction of £138 million.

On the back of our guidance to levy payers, published in 2012/13, to put in place and certify guarantees where they reflect a real reduction in risk, we tested a number of contingent assets for guarantor strength, partly through reference to published data and partly at random.

Among those schemes we chose to test, there was a significant failure even among those we chose randomly. Overall, about half the Type A contingent assets tested were rejected. This resulted in a total increase in the levy of £14 million which is small by comparison with other factors influencing total collection.

Fraud Compensation Fund

We are responsible for providing compensation to work-based pension schemes where the sponsoring employer has become insolvent and the scheme has suffered a loss through fraud or dishonesty. The compensation is paid out from the FCF.

During the year, we decided that we would not have to raise a fraud compensation levy for 2014/15. The levy that was raised during 2012/13 has left the FCF adequately funded based on known claims and expected recoveries from third parties. We will continue to keep the position under review for future years.

The levy is collected on our behalf by the Pensions Regulator.

Strategic Report

Deliver excellent customer service to our members, levy payers and other stakeholders

David Heslop
Chief Operating Officer

Our announcement to bring PPF member services in-house demonstrates our commitment to enhance even further the customer service we provide to our members. We also give priority to our levy payers, which has involved a significant investment in collaboration and consultation to make sure we understand their needs.

Background

We have always been a member-focused organisation dedicated to providing them with confidence about their future and delivering on our mission to pay the right people the right amount at the right time.

Our announcement that we have embarked on the biggest strategic change to our organisation since we began in 2005 by planning to bring PPF member services in-house demonstrates our commitment to enhance even further the customer service we provide to our members.

This is also achieved by transforming the way we manage schemes through our assessment process and our focus continues to be on implementing our approach to partnership working and seeking to complete most scheme assessment periods in less than two years.

We recognise that members are not our only customers. We also give priority to our levy payers, which has involved a significant investment in collaboration and consultation to make sure we understand their needs. We constantly aim to provide levy payers with greater certainty and predictability over their levy bills.

Delivering a positive experience for our members and levy payers is also about our people. We need to make sure our people are the best they can be and we remain committed to keeping and developing a high-calibre, customer-focused workforce.

Strategic Report

Deliver excellent customer service to our members, levy payers and other stakeholders

Certainty for members through improved assessment processes

Panels

We remain committed to improving our operating model and systems not only to provide certainty to schemes and members but also to provide value for money.

That is why we announced in January 2013 that we would be expanding the range of professional panels we use to manage schemes through the PPF assessment and FAS wind-up processes.

In 2013/14 we set up two new panels in addition to our exisiting actuarial and specialist administration services panels:

Trustee advisory panel – four firms were appointed to this panel which began work in September 2013. All panel members work with insolvency practitioners, incumbent scheme trustees and other panel members before, during and after the assessment period as well as during FAS wind-ups.

Audit services panel – six firms were appointed to this panel in December 2013 and are expected to complete timely and accurate audits of the accounts required throughout the assessment process. The panel members work collaboratively with all interested parties to progress schemes through assessment and wind-up as soon as possible.

In April 2014 we launched an assessment process panel. Six firms were appointed to this panel whose purpose will be to aid and support the efficient and timely transition of schemes into the PPF and through the FAS wind-up by focusing on three discrete assessment tasks: admissible rules, equalisation and benefit specification.

This initiative has helped make sure assessment periods are now usually comfortably completed within two years.

Strategic Report

Deliver excellent customer service to our members, levy payers and other stakeholders

Data

Ensuring the quality of data we receive from schemes is adequate has been one of the hardest tasks facing us since we were set up nine years ago.

Putting the size of the task into perspective, we worked out that each member requires 190 individual pieces of data. If you multiply that by the number of our members currently, we are looking at some 35 million pieces of information which need to be accurate and up-to-date.

When the PPF was formed, schemes rarely had up-to-date information for all their members. Now, thanks to a lot of hard work in conjunction with the Pensions Regulator and the schemes themselves, the quality of data is much improved.

Although still not perfect, it has meant the time it takes to see schemes through assessment has reduced. This has in turn reduced the costs incurred which has meant that when schemes transfer to us, liabilities are less. This is good news for us and for our members.

However, we want to provide even greater certainty to our members and schemes have an important role in helping us achieve this. To support this, we have been developing a range of processes which will improve data quality. Also we have been at great pains to emphasise with our new panels how much importance we place on making sure we are working with the right data at all times.

Other issues

During the year, we made further in-roads into older cases which have yet to complete assessment or wind-up. Most of these cases are difficult to progress any further because of legal, dividend or other insolvency related issues, though we strive constantly to find cost-effective and pragmatic routes to resolution.

We also introduced an internal case management system which helps us make sure that we have a consistent approach when seeing schemes through assessment and wind-up, and processes which capture costs more effectively.

Strategic Report

Deliver excellent customer service to our members, levy payers and other stakeholders

Sara Protheroe
Director of Customer Experience

We have always put our customers at the heart of everything we do and in 2014, we plan to start bringing PPF member administration services in-house. This means we will be providing customer services to members directly, giving us greater control and flexibility over the service we provide.

Bringing member services in-house

In 2014 we plan to start bringing PPF member administration services in-house. This means we will be providing customer services to members directly instead of using an external supplier and, as a result, will have greater control and flexibility over the service we provide. This was not a decision we took lightly and was made only after months of detailed analysis, research and discussions with a range of experts.

To ensure that we have a shared understanding of what we are setting out to achieve, we have developed a vision that sets out our ambitions for our members, our people and the services we provide.

- **Our members** will experience exceptional service. They will be able to:
  - trust us because we do what we say we'll do
  - choose how they interact with us, and
  - obtain accurate and relevant information that is easy to understand.
- **Our people** will be proud to be part of the team. They will:
  - trust, encourage and inspire each other
  - be motivated and take personal responsibility for our work, and
  - have opportunities to develop skills and knowledge.
- **Our services** and the way we operate will be innovative. We will:
  - challenge the way things are done and make quality our priority
  - adapt our services to meet our members' needs, and
  - be recognised for delivering excellence.

As our vision sets out, we want to offer innovative services. We will enable multi-channel access so members can interact with us as they prefer: by telephone, internet, email or letter, whichever is most convenient at the time. A member should be able to go online and do everything from changing their bank details to setting up their retirement payments, should they choose to do so. Technology and customer service expectations are constantly evolving and we want to develop a service that responds flexibly to a changing environment.

Our vision also talks about providing accurate and relevant information that is easy to understand. We have invested significant time in developing a new range of member communications, including letters, forms and brochures, to accompany the launch of the new service. We have designed these communications to be clear and free of complicated language. We believe that all our communications will show empathy, and at the same time demonstrate that we are experts, so members will feel that they can trust us.

Strategic Report

Deliver excellent customer service to our members, levy payers and other stakeholders

Software support

In May 2013, we reached an important milestone with the award of a 10-year pensions administration and payroll software support contract.

We awarded the contract to specialist systems provider Civica, whose other clients include some of the largest pension schemes in the country, blue chip companies and public sector bodies.

Civica was chosen after a competitive tender process, and its software and support services will be used by our team when it starts to provide new in-house services to its hundreds of thousands of members.

Recruitment

To make sure we can provide members with a customer experience tailored to their needs, we need the right PPF team on hand to answer people's queries, and to ensure that we pay the right people the right amount at the right time. We are recruiting up to 100 extra staff externally and it is essential that they are all highly skilled, experienced and committed to delivering the best customer experience. In return we will provide a motivating, empowering environment in which to work, with opportunity for growth and development. Our values at the PPF define the way we work and we will be using these as the basis for attracting, training and retaining the best people.

This major project began during the latter half of 2013 and continues through 2014. We are phasing recruitment to match our controlled, phased approach for bringing member services in-house. This means that that we will have the right numbers of staff for each phase.

So far, we have recruited and redeployed 74 people to a number of roles and we expect 65 more people to be recruited later in the year, including transferring staff internally.

We are looking to obtain Institute of Customer Service accreditation for the customer services element of our training, to demonstrate our investment in our people, and to show that they are trained to an industry-recognised standard.

Customer services

Our dedicated Stakeholder Support Team continued to provide the main point of contact for industry professionals and employers, among others. During the year it handled 10,068 telephone calls and 2,506 letters and emails.

Our payments administrator customer services team handled 99,272 written enquiries and 69,259 telephone enquiries for both PPF and FAS throughout 2013/14.

A series of telephone feedback, surveys and other mechanisms recorded a 93 per cent satisfaction rating at the end of the 2013/14 year.

Strategic Report

Pursue our mission within a high calibre framework of risk management

Martin Clarke
Executive Director for Financial Risk

We are committed to using our experience and evidence of the pensions system to interpret the effects of the current economic environment, advise on policy initiatives and help to identify trends and challenges to the system.

Background

In fulfilling our role to protect millions of people's pensions, we have become a key contributor, together with other bodies such as the Pensions Regulator and trustees of UK defined benefit pension schemes, to making sure that risks to pension provision, in its widest sense, are managed effectively.

We are committed to using our experience and evidence of the pensions system to interpret the effects of the current economic environment, advise on policy initiatives and help to identify trends and challenges to the system.

Internally, we employ an 'enterprise risk management' approach to identifying risks, both financial and non-financial, risk tolerance and risk management. This helps us achieve our goals, identify opportunities for improvement and mitigate the effects of a wide range of risks on the organisation.

We have a cautious risk appetite, preferring safe delivery options that have a low degree of residual risk, with a strong control framework in particular in place for investment operations. This is not designed to stifle initiative, but rather to allow our people to work within a transparent and well-managed structure.

Risk appetite and oversight

Forming the cornerstone for all our risk management activity is our Board's risk appetite statement which is reviewed and refreshed every year. Fundamentally, the Board has a cautious risk appetite for all categories of risk although it has an even more risk-averse approach to our investment operations.

During 2013/14, the Board provided a more detailed appraisal of its risk appetite which provided us with an updated view of how we should effectively take and manage risk within the organisation. The risk appetite can be found on our website at **www.pensionprotectionfund.org.uk/About-Us/Documents/Risk_Appetite_Statement.pdf**

We need to oversee the risks that we are taking and how we are mitigating the external and internal risks that we face. This oversight has been effective in the past and we need to make sure that it remains fit-for-purpose as the organisation grows.

Because our assets have grown significantly and we are on the verge of bringing our member services in-house, we decided during the year that it was the right time to introduce a Risk and Audit Committee with a clear mandate to oversee risks across the business.

This was developed in line with the Walker Report, which recommended measures to improve the corporate governance of UK banks, particularly with regard to risk management, while making sure it remained appropriate for the range of risks faced by the PPF.

We monitor the financial risks that we face at our monthly Asset and Liability Committee (ALCO) and all other risks are monitored at a monthly Risk Management Committee.

Strategic Report

Pursue our mission within a high calibre framework of risk management

Risk management

The way we manage our risk is based on the following principles:

- the executive team, together with non-executive members of the Board, foster a culture to support well-judged decisions about risks and opportunities. This enables innovation to be handled with confidence and recognises that risk management creates and protects value
- the management of risk will be integrated into existing processes
- clear roles will be agreed relating to the accountability, management, escalation and communication of risks, and
- all staff will encourage openness and honesty in the reporting and escalation of risks.

There is a consistent approach to the assessment of risks and opportunities and the effectiveness of risk management will be subject to challenge through regular systematic assessment. In common with many financial services organisations we adopt the three lines of defence model.

First line of defence - the organisation's operational management has ownership, responsibility and accountability for assessing, controlling and mitigating risks.

Second line of defence - risk management functions, legal, finance, HR, IT and other relevant teams put in place, and monitor, the implementation of effective risk management measures and help the risk owners report adequate risk-related information up and down the organisation.

Third line of defence - the internal audit function will, through a risk-based approach, provide assurance to the organisation's Board and senior management, on how effectively the organisation assesses and manages its risks, including the manner in which the first and second lines of defence operate.

This assurance covers all elements of an organisation's risk management framework, ie from risk identification, risk assessment and response to communication of risk-related information, to all categories of organisational objectives.

We have benchmarked our risk management process against a number of similar organisations and pleasingly the framework we have in place reflects best practice we have seen elsewhere.

Our internal audit function is outsourced to Grant Thornton which also provides another source of bringing best practice into the organisation.

Safety of our customers' data is paramount and to make sure we have the right controls in place we test ourselves against industry best practice by continuing to maintain our ISO27001 accreditation.

Our business resilience capabilities have served us well and are being developed alongside the introduction of a new IT system and bringing member services in-house, in particular:

- much improved disaster recovery capability - our new IT service is provided from two live data centres which share the workload in normal running. In the event that we lose service from one data centre, the remaining data centre will instantaneously take over provision of service to all of our users, and
- more in-depth disaster scenarios – we practise these to make sure our business continuity team are able to respond to a wide range of incidents.

Strategic Report

Pursue our mission within a high calibre framework of risk management

Funding and investment risk

Managing risks to our funding and investment strategies are the priority areas for our risk management activity.

That is why, during the year, we increased the frequency of our investment risk monitoring from weekly to daily.

Also, we enhanced our management of liquidity risk to make sure we can meet our liabilities as they fall due, and we extended our investment performance analysis to provide further breakdowns of areas where we gain and lose returns, a development which is continuing to be enhanced.

We improved how we assess the risk of companies becoming insolvent and transferring their pension liabilities to the PPF, and we now have robust metrics for every risk category we monitor.

There are a number of developments which began during 2013/14 and remain in progress, including:

- creating a financial risk practice to provide independent measurement of performance and act as the second line in our three lines of defence model
- operating 21 specific risk policies covering on and off balance sheet financial risks
- reporting these policies to the ALCO each month
- preparing for the new European Market Infrastructure Regulation requirement to centrally clear derivatives
- investigating the greater use of illiquid assets to hedge our liabilities
- developing a Solvency II style PPF-specific ORSA which will document and review our risk management process
- strengthening of our review of the operational risk controls of our external fund managers
- initiating a project to consider a new risk/performance system, and
- benchmarking our funding strategy against ORSA principles which led to changes in our stress/sensitivity tests and operational risk allowances.

Purple Book

We published the eighth Purple Book, alongside the Pensions Regulator, which monitors the risks faced by 6,150 mostly private sector schemes throughout the UK which in turn represent about 11 million people.

This latest edition showed that allocation trends include a move away from equities into bonds, hedge funds and cash deposits. In equities themselves, there was an increase in overseas allocations and a corresponding fall in UK share. Within bonds there was a fall in corporate bond allocation and a rise in government bond allocations for the first time since 2008 when this breakdown became available.

The Purple Book also reported improvements in the economic environment since the end of March 2013, with gilt yields rising sharply and equity markets remaining broadly unchanged, leading to improvements in scheme funding.

The Purple Book provides us with an invaluable barometer about the changes in risk that we face as we seek to achieve our 2030 funding target.

Strategic Report

Foundations - People, Communications and Efficiency & Effectiveness

Katherine Easter
Director of HR and Organisational Development

We were delighted to achieve 'One Star' accreditation in the Sunday Times Best Companies 2014 survey and a place on the Top 100 Best Not-For-Profit Companies to Work For list for the first time.

ICARE

Our ICARE values are at the heart of what we do and we encourage staff to achieve our vision, mission and strategic objectives in a way that reflects these values. Our ICARE Awards recognise where individuals and teams have demonstrated outstanding examples of our values in a particular piece of work or project and the whole organisation joins in with celebrating such successes.

Our values are:

INTEGRITY – DO THE RIGHT THING

COLLABORATION – WORK AS ONE

ACCOUNTABILITY – OWN YOUR ACTIONS

RESPECT – VALUE EVERY VOICE

EXCELLENCE – BE YOUR BEST

Performance and development

As an organisation, we are committed to embedding a culture where people strive for excellence and feel that their contributions are valued. We take performance development seriously and ensure that there are tools in place that support managers and employees to achieve the organisation's goals and mission. Personal performance is measured regularly through our performance development process.

We support a variety of learning and development initiatives both formal and informal to ensure that our people have the necessary skills and knowledge to perform their roles effectively.

Whilst we have continued to recruit experienced people to keep our organisational knowledge current, we have placed great importance on supporting the careers of existing employees. We celebrated our success with an article in our employee newsletter highlighting 27 internal moves and promotions.

We understand that good management is essential to our success and therefore have developed our formal management development programme to recognise management skill with an external award from the Chartered Management Institute.

To make sure our staff are professional and credible in our dealings with all stakeholders, we invested heavily in Continuing Professional Development to support people in their roles speaking privately or publicly on the work of the PPF, among other areas.

Employee Engagement

Important measures of employee engagement are the results of our staff survey. We worked hard last year to improve our engagement scores by sharing the results and team and organisational action plans. We were delighted to achieve 'One Star' accreditation in the Sunday Times Best Companies in the Not-For-Profit Sector 2014 survey and a place on the Top 100 list for the first time. This was a marked improvement on previous years.

Strategic Report

Foundations - People, Communications and Efficiency & Effectiveness

To be recognised as an organisation with very good levels of employee engagement and as one of the best to work for in the not-for-profit sector is a great achievement.

Each of the eight factors in the survey (Leadership, My Company, My Manager, Personal Growth, My Team, Wellbeing, Fair Deal and Giving Something Back) improved. My Manager and Personal Growth both increased by six per cent, which is particularly pleasing as these were the two areas we decided to focus on in 2013.

We have found that recognition of this sort has a positive impact on greater employee engagement, helping us to recruit and retain the best people.

Statistics

As at 31 March 2014, we had 270 employees, compared to 240 as at 31 March 2013, of which 149 are men and 121 are women. The increase in employee number was largely due to the move to bring our member services in-house. The gender mix of our top team is 11 men and 5 women, and at senior management level and above is 36 men and 24 women.

The number of days we lost to sickness during the year averaged 3.9 days per person (10.5 per cent). This included long-term absences of more than 28 days.

Excluding long-term absences, we only lost 2.4 days per person (6.5 per cent) which compares favourably with the Civil Service average of 7.6 days per person.

Staff turnover fell from 10.5 per cent in 2012/13 to 9.4 per cent in 2013/14.

Strategic Report

Foundations - People, Communications and Efficiency & Effectiveness

Richard Williams
Head of Corporate Affairs

In a period of continuing economic uncertainty and challenges for pension schemes, we believe it is even more important that we continue to provide confidence and certainty to the members that we protect.

Communicating is a two way thing

We have always placed a great emphasis on communicating our actions and the reasons for them to everyone interested in our work. This doesn't just mean levy payers and industry professionals but also the Government, Europe and, crucially, our members.

In a period of continuing economic uncertainty and challenges for pension schemes, we believe it is even more important that we continue to provide confidence and certainty to the members that we protect. Equally, we must continue to listen to our other important interest groups to make sure our plans for future development are transparent and understandable.

Communications channels

Our website remains the first port of call for many professionals seeking information about the PPF. It had 202,459 unique visitors during the year who made 296,562 visits in total.

To coincide with our decision to bring member services in-house, we are planning to launch a revamped corporate website later in 2014.

Also in the year, we issued 44 alerts, press releases, industry bulletins and information notices to the 4,647 people who have registered their emails with us, as well as other interested parties such as professional organisations and the media.

We arranged for either our Chairman or Chief Executive to speak at or attend 56 events during the year and other senior representatives appeared on many more speaking platforms, at conferences or on roundtables.

We published 116 documents which included consultation, decision and guidance documents on issues such as the pension protection levy, revised actuarial factors and our move to a new insolvency risk provider.

Following our move to new offices in April and May 2014, we unveiled a new visual identity which has been designed to reflect and reinforce our core values and demonstrate that we are a forward-looking organisation.

Member communications

All PPF members received a copy of an annual review called 'Member Focus' which summarised what we did in 2012/13. Independent research carried out on our behalf shows that this is hugely welcomed by members as a way of keeping them in touch with what we are up to.

Strategic Report

Foundations - People, Communications and Efficiency & Effectiveness

Community involvement

We have a community responsibility policy which has long recognised that, as a responsible employer, we have a role to play in contributing to the local community and beyond.

During the year, we continued our membership of Croydon Commitment, a charitable business partnership which bridges the gap between the needs of the local community and businesses in the area.

Under its auspices, we prepared and served Christmas dinner for some 100 members of a local drop-in centre for older people.

Efficiencies

During the year, we spent £48 million of administration costs in addition to those costs such as investment management fees that are charged directly to the fund. Our actual expenditure was £19 million under budget.

An important measure of our efficiency is the average administration cost per PPF member, including all those in the assessment period and those who have transferred. This average cost fell from £81 in 2012/13 to £79 in 2013/14.

The PPF's payment practice is to pay our UK suppliers in accordance with the terms of business agreed with them.

As at 31 March 2014, the aggregate amount owed to suppliers, other than fund managers, compared to the total amount billed by suppliers during the year (expressed as a number of days) was 28 days (compared to 35 days as at 31 March 2013).

We have excluded from this statistic supplier invoices which were under query or dispute with the suppliers at the end of the year.

Strategic Report
General information

During the year, we handled a number of appeals, complaints and requests for information.

Reviewable matters – 2013/14 levy year

We run a statutory appeals process in respect of 'reviewable matters' listed in the Pensions Act 2004. Most appeals under this process relate to the pension protection levy.

During 2013/14, we issued 53 review decisions in response to levy appeals, compared with 70 the previous year. In 29 of these cases, the scheme was found to be levied correctly. In the remaining 24 cases, we agreed with some or all of the scheme's appeal. In 10 cases, the applicants further appealed the review decision to our Reconsideration Committee.

We also issued 13 review decisions in relation to other reviewable matters (primarily individuals' compensation) during 2013/14.

Maladministration complaints

We dealt with 8 formal complaints of maladministration during 2013/14. In 2 of the cases our Board found that maladministration had occurred.

Freedom of Information requests

During the year, we received 38 Freedom of Information requests and we disclosed fully the information requested in 22 cases, partially disclosed in 7 cases and did not hold the information asked for in 5 cases.

We declined to disclose information in 4 instances by applying statutory exemptions because the information was restricted, commercially sensitive or too costly to disclose.

We do not charge for disclosing information. In this way, we comply, as a public sector information holder, with the cost allocation and charging requirements set out in the relevant HM Treasury and Office of Public Sector Information Guidance.

General complaints

For PPF and FAS, complaints at Stage One are dealt with by the Complaints Team and by a director at Stage Two. Stage Three are dealt with by an Independent Case Examiner at DWP for PPF complaint cases and by The Independent Complaints Resolution Service for FAS complaint cases.

During the year we received 124 PPF complaints, of which 120 were resolved at Stage One and 2 were escalated to Stage Two. We logged 211 FAS complaint cases, of which 198 were resolved at Stage One, 7 cases were escalated to Stage Two and 1 case was escalated to Stage Three. The remaining PPF and FAS cases were unresolved at 31 March 2014.

For the PPF the focus of complaints was around compensation entitlements, including the way that legislation affects members' compensation. For FAS, complaints were mostly about corrections to estimated payments.

Guidance on how we handle complaints and appeals can be found on our website.

Statutory Reports

Statement of Accounting Officer's responsibilities

Under the Pensions Act 2004, the Board of the PPF is required to prepare for each financial year a statement of accounts in the form and on the basis directed by the Secretary of State for Work and Pensions with the consent of the Treasury. The accounts are prepared on an accruals basis and must give a true and fair view of the state of affairs of the Board and of its income and expenditure, gains and losses and cash flows for the financial year.

In preparing the accounts, the Board is required to comply with the requirements of the Government Financial Reporting Manual and in particular to:

- observe the Accounts Direction issued by the Secretary of State, including the relevant accounting and disclosure requirements, and apply suitable accounting policies on a consistent basis
- make judgements and estimates on a reasonable basis
- state whether applicable accounting standards as set out in the Government Financial Reporting Manual have been followed, and disclose and explain any material departures in the accounts, and
- prepare the accounts on a going concern basis.

The Secretary of State for Work and Pensions has appointed the Chief Executive as the Accounting Officer for the Board. The responsibilities of an Accounting Officer, including responsibility for the propriety and regularity of the public finances for which the Accounting Officer is answerable, for keeping proper records and for safeguarding the Board's assets, are set out in Managing Public Money published by HM Treasury.

Alan Rubenstein
Accounting Officer
10 July 2014

Governance statement

Governance Framework

The Board has eight non-executive members, including the Chairman. There are four executive members, including the Chief Executive.

The Board has established a number of committees so that it can conduct its business in line with its Statement of Operating Principles.

The Board has also given the Chief Executive delegated powers so he can take decisions to ensure operational effectiveness and provide regular updates to the Board provided on performance, risks and strategic briefings. The Chief Executive has established a number of internal committees to oversee operations.

Further details of the governance framework are provided in Appendix 1.

Board Performance

During January and February 2014, the Board and Board Committees conducted an evaluation of their effectiveness looking back over the previous year. This was carried out using a questionnaire, and the Chairman met each Board member to discuss their feedback in relation to the Board meetings. The feedback provided culminated in a report to the next meeting of each committee, including the comments provided (in an anonymised format), and set out an action plan to address any outstanding points.

The Board met 10 times in 2013/14 and a Board training session on risk budgeting and hedging assets with illiquid properties was provided.

Board member details, committee memberships and attendance at Board and committee meetings are set out in Appendix 2.

Highlights of Reports

The Board and its committees considered a number of issues during the year which are described more fully in Appendix 3, including:

- 2013 valuation assumptions
- communications strategy
- policy horizon scanning update
- review of strategic investment risks and illiquidity risk
- the appointment of a new insolvency risk provider
- an own risk and solvency assessment
- identified actions in its effectiveness review and altered the remit of the Audit Committee to include risk and form a Risk and Audit Committee
- compliance update including the Bribery Act and Health and Safety matters
- regular progress reports on change processes within the organisation, and
- preparation for the 2015/16 three-year levy cycle.

Governance statement continued

Account of Corporate Governance

The Board is committed to adhering to high standards of corporate governance and reviews its compliance against the UK Corporate Governance Code and the HM Treasury/ Cabinet Office Corporate Governance in central government departments: Code of good practice, annually. Formal reporting of compliance with the HM Treasury/ Cabinet Office code on a 'comply or explain' basis is a requirement and is set out in this statement.

The latest review of compliance with the code was considered by the Chairman, the Senior Independent Director and the Chair of the Audit Committee in February 2012. The Board meets the provisions of the code where they apply to the PPF. The next review of the PPF's compliance against the code will be carried out in 2015.

Full details of the review can be found in Appendix 4.

The risk and control environment

The PPF's approach to risk management follows the guidelines provided by HM Treasury in their document 'Orange Book: Management of Risk – Principles and Concepts.'

During the period under review, we changed our risk categorisation to:

- funding
- operational, and
- environmental.

The Board determines its risk appetite on an annual basis, which is then passed down to risk owners within the PPF who report twice-yearly about how they are adhering to the risk appetite. The risk appetite can be found on the PPF website **www.pensionprotectionfund.org.uk/About-Us/Documents/Risk_Appetite_Statement.pdf**

Significant Risks

We have identified the following risks, managed as part of the normal course of our business, which have the potential to impact on our ability to deliver our objectives and may pose a risk to the achievement of the three-year business plan or the long-term funding objective:

- changes in the PPF's environment arising from adverse economic conditions and/or a failure of the regulatory system may mean we cannot achieve our funding objective by 2030
- significant systemic or idiosyncratic risk materialises, that may significantly and adversely impact PPF's funding plan
- PPF investment strategy could be inappropriate to meet the long-term objectives of the fund leading to the returns we are targeting not being sufficient to fund compensation over the long term
- failure to deliver excellent customer service could lead to member and/or stakeholder dissatisfaction, and
- failure to manage change in our strategic suppliers could lead to operational ineffectiveness and/or reputational damage.

Further details of our risk and control environment can be found in Appendix 5.

Governance statement continued

Ministerial directions

No directions have been issued.

Personal data related incidents

No material data incidents to disclose.

Significant control issues

There are no significant control issues to disclose.

Review of effectiveness

As Accounting Officer, I also have responsibility for reviewing the effectiveness of the system of internal control. My review of the effectiveness of the system of internal control has been informed by:

- the assurances I sought and received from other Board members and senior staff of the PPF which detailed the work carried out to make sure risk management and control is addressed in their areas of responsibility
- the work of the executive directors and senior managers within the PPF who have responsibility for the development and maintenance of the internal control framework
- comments made by the external auditors in their management letter and other reports
- the opinion of the Head of Internal Audit on the overall adequacy and effectiveness of PPF's framework of governance, risk management and control. This states 'It is our opinion that within the scope of work undertaken, and on the assumption that Internal Audit recommendations are implemented, the PPF's risk management, control and governance processes are adequate and effective. The PPF has a control framework in the areas reviewed which we are satisfied are operating as intended to mitigate the risks in the specific area. Where the assurance provided on internal control design or operational effectiveness has been highlighted as less than high, the remediation of identified findings should elevate the assurance to a high level.'

I have been advised on the implications of the result of my review of the effectiveness of the system of internal control by the Audit Committee, the Executive Committee, the Asset and Liability Committee and the Risk Management Committee.

Alan Rubenstein
Accounting Officer
10 July 2014

Governance statement continued

Appendix 1 - Governance Framework

The Pensions Act 2004 requires that the Board has a majority of non-executive members, including a Non-Executive Chairman. All non-executive members were independent at appointment having no current or previous material relationship with the organisation as an employee, officer or contractor.

The Board must appoint a Chief Executive and at least two further executive Board members. There are four executive members, including the Chief Executive.

The Board is required under the Pensions Act 2004 to have a Non-Executive Committee. The functions of the Non-Executive Committee are set out under section 112 of the Pensions Act 2004:

- the duty to keep under review the question of whether the Board's internal financial controls secure the proper conduct of its financial affairs
- the duty to determine under sub-paragraph (5) (a) of paragraph 12 of Schedule 5, subject to the approval of the Secretary of State, the terms and conditions as to remuneration of any Chief Executive appointed under sub-paragraph (4) of that paragraph
- the duty to determine under paragraph 13(3)(a) of that Schedule, subject to the approval of the Secretary of State, the terms and conditions as to remuneration of any member of staff who is also to be an executive member of the Board, and
- the duty to determine under paragraph 13(3)(b) of that Schedule, the terms and conditions as to remuneration of any member of staff of a description prescribed for the purposes of that provision.

The Board is also required to have a Reconsideration Committee to reconsider reviewable matters cases and maladministration complaints.

The Board has also established an Audit Committee and Remuneration Committee as the sub-committees of the Non-Executive Committee and Investment, Nomination and Decision Committees as Committees of the Board. Following the externally-facilitated review of its effectiveness, the Board decided in January 2014 to revise the remit of the Audit Committee and created a Risk and Audit Committee to replace the Audit Committee. Each Committee has a majority of non-executive members. The terms of reference for these Committees can be accessed at **www.pensionprotectionfund.org.uk/About-Us/TheBoard/Pages/TheBoard.aspx** and their activities during the 2013/14 financial year are reported below.

Board procedures are governed by its Statement of Operating Principles and its decision making role by the Schedule of Delegations and Matters Reserved to the Board. The Executive reports to the Board monthly on performance against strategic objectives, the Chief Executive's report and other briefings as required. Papers are circulated a week in advance of meetings and feedback on the quality and timeliness of the information provided was sought as part of the review of the Board and Committees' effectiveness.

The internal committees established by the Chief Executive, their roles and those of individual post holders are set out in the authorisations of the Chief Executive document.

Governance statement continued

Appendix 2 - Board's performance

Board member details, committee memberships and attendance at Board and Committee meetings are set out below.

Chairman
Lady Judge CBE

Chief Executive
Alan Rubenstein

Executive Members
Martin Clarke
David Heslop
Andy McKinnon

Non-Executive Members
Dick Barfield
Ann Berresford (stepped down from the Board on 31 July 2013)
John Bevington
Sir Anthony Holland (stepped down from the Board on 31 July 2013)
Alan Jenkins (joined the Board on 7 August 2013)
Tom Joy (joined the Board on 7 August 2013)
Sharmila Nebhrajani OBE
Arnold Wagner OBE (also Senior Independent Director of the Pension Protection Fund)
Baroness Warwick of Undercliffe

All biographies are on the PPF website
www.pensionprotectionfund.org.uk/About-Us/TheBoard/Pages/BoardMembers.aspx

The following Board members stood down during the year:
Ann Berresford
Sir Anthony Holland

Governance statement continued

Attendance at Board and Committee meetings during 2013/14

	Board	Remuneration Committee	Audit Committee	Investment Committee	Reconsideration Committee***	Nomination Committee	Decision Committee
Lady Judge CBE	10 of 10	2 of 2[1]	n/a	n/a	n/a	3 of 3	n/a
Dick Barfield	9 of 10	1 of 1[2]	3 of 4	5 of 5	n/a	n/a	n/a
Ann Berresford**	2 of 2	n/a	1 of 2	1 of 1[3]	n/a	n/a	n/a
John Bevington	9 of 10	2 of 2	n/a	5 of 5	n/a	n/a	2 of 2
Martin Clarke	8 of 10	n/a	4 of 4[4]	4 of 5	n/a	n/a	n/a
David Heslop	9 of 10	n/a	3 of 4[5]	n/a	n/a	n/a	n/a
Sir Anthony Holland**	1 of 2	1 of 1	n/a	n/a	3 of 3	n/a	n/a
Alan Jenkins*	4 of 7	n/a	n/a	n/a	3 of 5	n/a	n/a
Tom Joy*	7 of 7	1 of 1[6]	n/a	4 of 4	n/a	n/a	n/a
Andy McKinnon	9 of 10	n/a	4 of 4[7]	n/a	n/a	n/a	n/a
Sharmila Nebhrajani OBE	10 of 10	1 of 1[8]	4 of 4	n/a	n/a	n/a	n/a
Alan Rubenstein	10 of 10	2 of 2[9]	3 of 4[10]	5 of 5	n/a	n/a	2 of 2
Arnold Wagner OBE	9 of 10	2 of 2	n/a	n/a	n/a	3 of 3	2 of 2
Baroness Warwick of Undercliffe	10 of 10	1 of 1[11]	4 of 4	n/a	8 of 8	n/a	n/a

* Joined the Board on 7 August 2013.
** Stepped down from the Board on 31 July 2013
*** The Reconsideration Committee forms a panel of non-executive members of the Board without prior involvement in the matter. When a matter is remitted from the Pension Protection Fund Ombudsman the panel cannot be formed from the same members as were previously involved.

Board decisions

A number of decisions that fall within the Board's normal cycle of work were also taken.

These included:

- appointment of a new insolvency risk provider
- approved the communications strategy
- took forward actions recommended by the Board effectiveness review, including establishing a Risk and Audit Committee to replace Audit Committee
- approved the 2013 valuation assumptions, and
- approved the target levy collection of £695 million for 2014/15.

[1] Lady Judge attended two meetings of the Remuneration Committee in her capacity as chairman
[2] Dick Barfield attended one meeting of the Remuneration Committee in his capacity as a chair of the Investment Committee
[3] Ann Berresford attended one meeting of the Investment Committee in her capacity as chair of the Audit Committee
[4] Martin Clarke attended four meetings of the Audit Committee in his capacity as an executive director
[5] David Heslop attended three meetings of the Audit Committee in his capacity as an executive director
[6] Tom Joy attended one meeting of the Remuneration Committee in his capacity as a non-executive director
[7] Andy McKinnon attended four meetings of the Audit Committee in his capacity as an executive director
[8] Sharmila Nebhrajani attended one meeting of the Remuneration Committee in her capacity as chair of the Audit Committee
[9] Alan Rubenstein attended two meetings of the Remuneration Committee in his capacity as Chief Executive
[10] Alan Rubenstein attended three meetings of the Audit Committee in his capacity as Chief Executive
[11] Baroness Warwick of Undercliffe attended one meeting of the Remuneration Committee in her capacity as chair of the Reconsideration Committee

Governance statement continued

Appendix 3 - Highlights of reports

Audit Committee

The Audit Committee is chaired by Sharmila Nebhrajani OBE. The Committee met four times during the year. The agenda continued to be busy, including monitoring compliance with the Board's risk appetite. Six internal audit reports and three 'deep dives' on operational risks and controls (HR Operations, Retirement Income Services and Procurement and Supplier Management) were presented.

As part of its normal cycle of work, the Committee reviewed the risk management policy, the governance statement and the internal audit reports including the Board's corporate governance arrangements. The Committee also reviewed and recommended the Annual Report and Accounts 2012/13 for approval by the Board.

Grant Thornton LLP, PPF's current internal auditors, continued to provide the internal audit service.

The Chair of the former Audit Committee took forward the recommendations set out in the Board effectiveness review and established a revised Committee entitled Risk and Audit Committee.

Remuneration Committee

The Remuneration Committee is chaired by Arnold Wagner OBE. The Committee met twice during the year and agreed objectives for executive directors in 2013/14. They also undertook yearly and half-yearly performance reviews of executive directors and recommended bonus payments for them.

Investment Committee

The Investment Committee is chaired by Dick Barfield. The Committee met five times during the year and the Committee agreed a number of key proposals including the Manager of Managers project to control the enlarged portfolio of investment managers as the Fund grows, the Pensions Infrastructure Platform selection and appointment of managers, and the HAIL project (capturing the premia and hedging properties of illiquid assets) allowing greater allocation to illiquid investment opportunities within the Fund.

As part of its normal cycle of work, the Investment Committee reviewed:

- four investment update reports
- four reports from the investment advisor (Mercer)
- four reports summarising the activity of the Asset and Liability Committee
- two reports on the markets and investment strategy
- four risk policy deep dive reports: credit spread, hedging, counterparty and alternative assets
- two asset class reviews: private equity and public equity
- strategic investment risks and illiquidity risks
- a report on responsible investment
- the risk and return assumptions
- the Statement of Investment Principles, and
- the Investment Committee Governance Framework Compliance Report.

The Board approved the reappointment of Mike O'Brien as the co-opted specialist member of the Investment Committee for a second three year term in 2013, to ensure that there was sufficient independent investment knowledge and experience on the Committee.

Governance statement continued

Decision Committee

The Decision Committee is chaired by John Bevington. The Committee met twice during the year.

The Decision Committee takes decisions on matters which are normally delegated to the Chief Executive which he refers back to the Committee, as well as any specific cases assigned to it by the Board. This may be due to the particular circumstance of the issue where additional Board member input is thought valuable or where it is judged necessary in the light of the possibility of future review or complaint.

Reconsideration Committee

The Reconsideration Committee is chaired by Baroness Warwick of Undercliffe who took over from Sir Anthony Holland on 18 September 2013. The Committee co-opted two specialist members who had an appropriate level of experience to ensure robust decision making. The Committee met on eight occasions during the year and considered, and issued decisions relating to, 12 cases where levy payers challenged their levy. Of these 12, nine were referred to the Pension Protection Fund Ombudsman.

The Committee also considered three non-levy review cases relating to compensation payments, one in relation to the Fraud Compensation Fund and two maladministration complaints.

Nomination Committee

The Nomination Committee met three times during the year. These meetings were chaired by Lady Judge CBE. The Nomination Committee recommended the appointment of Alan Jenkins and Tom Joy to the Board as non-executive members and they both joined the Board on 7 August 2013.

Board appointments

The Secretary of State for Work and Pensions is responsible for appointing the Chairman of the PPF and as a ministerial appointment this is governed by the guidance set by the Office for the Commissioner of Public Appointments. All other Board appointments are made by the Board on the recommendation of the Nomination Committee. However, the Secretary of State must approve the remuneration and terms and conditions for the Chief Executive and the remuneration for other executive Board members. The Secretary of State also determines the fee for non-executive members.

The appointment of 'ordinary' members to the Board is governed by regulations under which the Board must include an independent member as part of its appointment panel.

Governance statement continued

Appendix 4 - Account of Corporate Governance

As stated, the Board is committed to adhering to high standards of corporate governance and reviews its compliance against the UK Corporate Governance Code and the HM Treasury/ Cabinet Office Corporate Governance in central government departments: Code of good practice annually.

The principal areas of compliance are met as follows:

Parliamentary accountability

The Chairman and Chief Executive meet regularly with Ministers and Senior Officials from the Department for Work and Pensions (DWP) in addition to quarterly accountability review meetings. The Department approves the Board's Strategic Plan and the Board delivers its Annual Report and Accounts to Parliament through the Secretary of State.

The Chief Executive of the PPF is also its Accounting Officer. Compliance with Accounting Officer responsibilities are supported through the Board's risk management procedures and through a shared objective for senior management to support the Accounting Officer in fulfilling his responsibilities.

The Board and Board composition

The structure of the Board is underpinned by the framework set out in the Pensions Act 2004 as well as developing governance and operational requirements. Committees have been established to serve these needs. The composition of the Board is determined by the skills, experience and diversity needed to deliver the PPF's statutory functions and is supported by its members' financial, investment, legal, risk management, operational and member representation knowledge.

The Board focuses on strategic issues, supporting the PPF's performance against its strategic objectives, risk management and ensuring that these all support the long-term success of the organisation.

The Board recognises that effective behaviours and culture support organisational delivery and risk management. The Board operates in accordance with its Board Manual which identifies how meetings should be conducted. Individual members also adhere to the code of conduct, guidance on dealing with potential conflicts of interest, and expenses and hospitality.

Board effectiveness

The Board has an operational framework in place and has determined its behavioural values. The actual operation of this framework and these values as well Board balance is reviewed through annual Board effectiveness evaluations. These evaluations are conducted internally with facilitation by external consultants every three years.

The Board has regulations in place for the appointment of 'ordinary' Board members and both the Board and its Nomination Committee consider the current and future needs of the Board in order to facilitate the Board appointment process. New Board members receive induction training and ongoing briefings are provided to support non-executive members' understanding of the organisation's operations and key risks. Board and Committee papers are dispatched a week in advance and the Board is supported by a dedicated secretariat.

Risk management

The Board has set its risk appetite which it reviews at least annually. The Board is supported in its risk management role by its Audit and Risk Committee, its internal and external auditors and its Investment Committee. Regular reports are received from the Executive which has established a Risk Management Committee and an Asset and Liability Committee to ensure effective day-to-day oversight of operational and financial risks. Information on risks and risk management processes is provided in Appendix 5.

Governance statement continued

Appendix 5 – The risk and control environment

Our system of internal control is designed to manage risk to a reasonable level rather than to eliminate all risk of failure to achieve policies, aims and objectives. It can therefore only provide reasonable, and not absolute, assurance of effectiveness.

The system of internal control is based on an ongoing process designed to identify and prioritise the risks to the achievement of the Board of the PPF's policies, aims and objectives. This process is also designed to evaluate the likelihood of those risks being realised and their impact should they be realised and to manage them efficiently, effectively and economically.

The system of internal control has been in place within the Board of the PPF for the year ending 31 March 2014 and up to the date of signing of these accounts, and accords with Treasury guidance.

Internal audit services are provided on an outsourced basis in accordance with 'Government Internal Audit Standards'. Audits are undertaken in accordance with an internal audit plan approved by the Audit Committee. Grant Thornton LLP, PPF's internal auditors, continue to provide internal audit services.

The risk and control environment

As stated, our approach to risk management follows the guidelines provided by HM Treasury in their document 'Orange Book: Management of Risk – Principles and Concepts.'

This is complemented by risk reviews at both a team and process level, with identified risks and controls captured in risk registers and monitored regularly.

Risk processes are embedded throughout the organisation and individuals' responsibilities are communicated annually.

During 2013/14, we have delivered a number of improvements to managing risk, including:

- enhanced risk appetite statement enabling further clarity of the risks the Board wishes to take
- improved risk oversight through the development of a Risk and Audit Committee with greater clarity on responsibilities
- developed the control framework for end user computer solutions
- extended and improving our performance reporting and associated metrics
- implemented an enhanced liquidity risk framework
- extended regular risk reporting to expand on currency, basis, tactical and valuation risks
- carried out further deep dives of our fund managers and action where required
- documented formalisation of the responsibilities of risk owners and providing training on this, and
- mitigated key person risk by enhancing the documentation that describes the sources of risk data and the underlying risk calculations.

We undertake deep dives of particular risk types with risk owners at Board and executive committees to ensure that we are managing all the risks we face and that the controls we have in place are appropriate.

We have identified three business-critical models. These are the Long-term risk model (LTRM), the actuarial liability model, and ACT. LTRM is a stochastic model used to assess the long-term changes in the PPF's funding position and that of eligible schemes, based on a range of economic and insolvency scenarios. The actuarial liability model is used to calculate our liabilities in relation to compensation payments. ACT is an in-house system which rolls forward actuarial liabilities and assets. We can confirm that an appropriate quality assurance framework (as defined in the Macpherson report of March 2013) is in place for these models. The quality assurance framework for these models includes, but is not limited to, external audit, internal and external peer review, governance structures for review and challenge of model assumptions and outputs, developer testing and consideration of the relevant actuarial standards.

The breadth and volume of data that we deal with is a significant responsibility. We therefore operate in accordance with the Security Policy Framework and related Data Security guidance issued by the UK Government. To help achieve this we gained certification to the ISO27001 Information Security standard in 2009 (successfully recertified in 2012) and carry out annual ISO27001 surveillance audits to ensure we maintain compliance with the standard.

Remuneration report

Remuneration and bonuses

Executive directors receive a salary which is reviewed annually by the Remuneration Committee.

Their contracts allow for the payment of an annual performance related bonus of up to 20 per cent of their base salary.

The Chairman was paid a fixed fee and was contracted to work for the PPF for two days a week. All other non-executive directors received a fixed fee, based on working 26 days a year. This salary was not performance-related and there was no provision for compensation if a contract was terminated.

Contracts

Executive directors are employed on a fixed term contract and non-executive directors are appointed for a fixed term of office.

Name	Contract type	Start date	End date
Lady Judge CBE	Term of office (second)	01 July 2013	30 June 2016
Alan Rubenstein	Fixed Term Contract (second)	01 July 2012	30 June 2015
Martin Clarke	Fixed Term Contract (third)	17 May 2013	16 May 2016
David Heslop	Fixed Term Contract (second)	01 July 2012	30 June 2015
Andy McKinnon	Fixed Term Contract (first)	02 January 2013	01 January 2016
John Bevington	Term of office (second)	19 October 2012	18 October 2015
Dick Barfield	Term of office (second)	01 October 2012	30 September 2015
Ann Berresford	Term of office (second)	01 August 2010	31 July 2013
Sir Anthony Holland	Term of office (second)	01 August 2010	31 July 2013
Alan Jenkins	Term of office (first)	07 August 2013	06 August 2016
Tom Joy	Term of office (first)	07 August 2013	06 August 2016
Arnold Wagner OBE	Term of office (second)	04 January 2014	03 January 2017
Baroness Warwick of Undercliffe	Term of office (second)	07 March 2014	06 March 2017
Sharmila Nebhrajani OBE	Term of office (first)	27 June 2012	26 June 2015

Notice periods

The Chief Executive, Executive Director of Financial Risk, Chief Financial Officer and the Chief Operating Officer have notice periods of six months. Non-executive directors' appointments can be terminated with one month's notice by either the Board or the individual member. The Chairman's appointment is subject to a six month notice period by either the Secretary of State for Work and Pensions or by the postholder. This can be waived by either party and the postholder can accept payment in lieu of notice.

Executive directors – outside appointments

We recognise the benefits to the individual, and to the organisation, of executive directors of the PPF serving as non-executive directors of other organisations and companies. These roles are undertaken outside of PPF working hours through a combination of paid and unpaid leave. Fees, where applicable, are retained by the executive director for current appointments. External non-executive appointments held by executive directors during the year were:

Alan Rubenstein, non-executive member of the Supervisory Board of Robeco, a Netherlands asset manager. Investment advisor to the British Coal Staff Superannuation Scheme.

Martin Clarke, Chair of the UK Sustainable Investment & Finance Association. Trustee of the LankellyChase Foundation.

Pensions

Pension benefits are provided through the Civil Service pension arrangements. Further details can be found on the Civil Service website **www.civilservice.gov.uk/pensions/**.

Statutory Reports

Remuneration continued

Cash equivalent transfer values

This is the actuarially-assessed capitalised value of the pension scheme benefits accrued by a member at a particular point in time. The benefits valued are the member's accrued benefits and any contingent spouse's pension payable from the scheme.

CETVs are calculated within the guidelines and framework prescribed by the Institute and Faculty of Actuaries and do not take account of any actual or potential reduction to benefits resulting from Lifetime Allowance Tax which may be due when pension benefits are taken.

Salary and pension entitlements (subject to audit - see auditor's report pages 55-56)

	Salary (in bands of £5,000)				Pensions				
	Year ending 31 March 2014		Year ending 31 March 2013		Real increase in pension and related lump sum	Total accrued pension at pension age at 31/3/2014	Cash equivalent transfer vaule at 31/3/2014	Cash equivalent transfer value at 31/3/2013	Real increase in CETV
	Salary £'000	Bonus £'000	Salary £'000	Bonus £'000	£'000	£'000	£'000	£'000	£'000
Lady Judge CBE Chairman	55-60	N/A	55-60	N/A	N/A[1]	N/A	N/A	N/A	N/A
Alan Rubenstein Chief Executive	195-200	35-40[3]	195-200	35-40[2]	0	15-20	214	205	0
Martin Clarke Director of Financial Risk	165-170	20-25[3]	165-170	20-25[2]	0-5	0-5	51	0	38
David Heslop Chief Operating Officer	135-140	20-25[3]	135-140	25-30[2]	0	10-15	129	122	1
Andy McKinnon Chief Financial Officer (from 2 January 2013)	150-155	15-20[3]	35-40 (Full year equiva-lent: 150-155)	0-5[2]	0-5	0-5	47	9	25
John Bevington Non-executive member	15-20	N/A	15-20	N/A	N/A	N/A	N/A	N/A	N/A
Dick Barfield Non-executive member	15-20	N/A	15-20	N/A	N/A	N/A	N/A	N/A	N/A
Ann Berresford Non-executive member (until 31 July 2013)	5-10 (Full year equiva-lent: 15-20)	N/A	15-20	N/A	N/A	N/A	N/A	N/A	N/A
Sir Anthony Holland Non-executive member (until 31 July 2013)	5-10 (Full year equiva-lent: 15-20)	N/A	15-20	N/A	N/A	N/A	N/A	N/A	N/A
Arnold Wagner OBE Non-executive member	15-20	N/A	15-20	N/A	N/A	N/A	N/A	N/A	N/A
Baroness Warwick of Undercliffe Non-executive member	15-20	N/A	15-20	N/A	N/A	N/A	N/A	N/A	N/A
Sharmila Nebhrajani OBE Non-executive member (from 27 June 2012)	15-20	N/A	10-15 (Full year equiva-lent: 15-20)	N/A	N/A	N/A	N/A	N/A	N/A
Tom Joy Non-executive member (from 7 August 2013)	10-15 (Full year equiva-lent: 15-20)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Alan Jenkins Non-executive member (from 7 August 2013)	10-15 (Full year equiva-lent: 15-20)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A

[1] Lady Judge was not a member of any employer sponsored pension arrangement during the year.

[2] The bonus values disclosed here relate to the executive directors' performance in the 2012/13 year and paid in 2013/14.

[3] The bonus values disclosed here relate to the executive directors' performance in the 2013/14 year and paid in 2014/15.

Two directors have life insurance cover provided by the PPF as in both cases the individuals reached the maximum lifetime allowance so could no longer contribute to the pension scheme. PPF paid £475 for David Heslop and £918 for Alan Rubenstein in respect of this cover.

Remuneration continued

Salary multiples

Reporting bodies are required to disclose the relationship between the remuneration of the highest paid director in their organisation and the median remuneration of the organisation's workforce.

	2013/14	**2012/13**
Band of highest paid director's total remuneration	£235-240k	£235-240k
Median total remuneration	£52k	£50k
Ratio	**4.6**	**4.8**

In 2013/14 one employee (2012/13: none) received remuneration in excess of the highest paid director. Remuneration ranged from £18k to £295-300k (2013: £16k to £235-240k).

Alan Rubenstein
Accounting Officer
10 July 2014

Statement on going concern

In order to comply with the Government Financial Reporting Manual when preparing this annual report and accounts, we have to explain why we have adopted a 'going concern' basis for the organisation. An organisation deems itself a going concern if its management believe that the organisation will continue to operate and there is no intention, nor need, to close down its functions. After reviewing the three funds which we operate, cash flow forecasts and our powers to raise levies and control outgoings, we decided to adopt a going concern basis for the PPF as a whole because we believe we have enough resources to continue operating for the foreseeable future.

Pension Protection Fund

For the PPF, we considered the following factors when making this decision:

- our cash flow forecasts, which indicate that cash and other asset inflows will significantly exceed outflows for the foreseeable future, supported by:
- our levy raising powers – see (**www.pensionprotectionfund.org.uk/levy/aboutlevy/Pages/AbouttheLevy.aspx**) and
- our reserve powers on compensation levels – see (**www.pensionprotectionfund.org.uk/Pages/Compensation.aspx**)

Fraud Compensation Fund

The volume of claims on the FCF remains at relatively low levels so we do not have enough statistics to forecast the level of future claims accurately. We therefore remain vulnerable to an unexpected rise in the volume of claims or unusually large or urgent claims.

However we have reviewed our powers and obligations and decided that the going concern basis remains appropriate for the FCF for the following reasons:

- none of the claims which the FCF has received and which it will probably have to pay out on are from schemes that have immediate cash flow requirements
- claims take some time to investigate and validate, which gives us time to plan how we will settle them
- we have powers to settle claims in instalments in order to ease any strain on the Fund's cash flow
- during the year, the Board maintained its funding strategy for the FCF which is to build up a small surplus in the Fund by raising a levy where necessary.

Administration Fund

In considering the going concern status of the Administration Fund, we took into account the status of the Board as an independent statutory corporation, while also recognising that the Board receives funding from its sponsor department, the Department for Work and Pensions (DWP), in the form of grant-in-aid, to cover all of its expenditure on its functions as FAS scheme manager, and its expenditure on certain PPF administration functions. We also considered the regulations under which DWP finances its payments to the Board on grant-in-aid for PPF administration functions by raising a PPF Administration Levy from eligible pension schemes. We decided that the going concern basis for the Administration Fund remains appropriate because of the robust financial procedures governing:

- the setting of operating budgets, including administration budgets which inform the setting by DWP of the rates of the PPF Administration Levy
- in-year reviews and forecasts of administration expenditure
- controls over applying for grant-in-aid from DWP, and
- the segregation of levy payer-funded PPF activities and Government-funded FAS-related activities.

Audit disclosures

I confirm that I have taken all appropriate steps to make myself aware of any relevant audit information and made sure that the Board's auditors are aware of that information. As far as I am aware, there is no information that the Board's auditors are unaware of. I also confirm that no remuneration for any work other than the statutory audit has been paid to the auditors.

Alan Rubenstein
Accounting Officer
10 July 2014

The certificate and report of the Comptroller and Auditor General to the Houses of Parliament

I certify that I have audited the financial statements of the Board of the Pension Protection Fund for the year ended 31 March 2014 under the Pensions Act 2004. The financial statements comprise: the Consolidated Statements of Comprehensive Net Income, Financial Position, Cash Flows, Changes in Reserves; and the related notes. These financial statements have been prepared under the accounting policies set out within them. I have also audited the information in the Remuneration Report that is described in that report as having been audited.

Respective responsibilities of the Board of the Pension Protection Fund, the Chief Executive and Auditor

As explained more fully in the Statement of Accounting Officer's Responsibilities the Board of the Pension Protection Fund and the Chief Executive, as the Accounting Officer, are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. My responsibility is to audit, certify and report on the financial statements in accordance with the Pensions Act 2004. I conducted my audit in accordance with International Standards on Auditing (UK and Ireland). Those standards require me and my staff to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Board of the Pension Protection Fund's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Board of the Pension Protection Fund; and the overall presentation of the financial statements. In addition I read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by me in the course of performing the audit. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my certificate.

I am required to obtain evidence sufficient to give reasonable assurance that the expenditure and income reported in the financial statements have been applied to the purposes intended by Parliament and the financial transactions recorded in the financial statements conform to the authorities which govern them.

Opinion on regularity

In my opinion, in all material respects the expenditure and income recorded in the financial statements have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them.

Opinion on financial statements

In my opinion:

- the financial statements give a true and fair view of the state of the Board of the Pension Protection Fund's affairs as at 31 March 2014 and of the net income for the year then ended; and
- the financial statements have been properly prepared in accordance with the Pensions Act 2004 and the Secretary of State's directions issued thereunder.

Opinion on other matters

In my opinion:

- the part of the Remuneration Report to be audited has been properly prepared in accordance with the Secretary of State's directions issued under the Pensions Act 2004; and
- the information given in the Directors' Report, the Strategic Report and the Chief Financial Officer's Review for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which I report by exception:

I have nothing to report in respect of the following matters which I report to you if, in my opinion:

- adequate accounting records have not been kept; or
- the financial statements and the part of the Remuneration Report to be audited are not in agreement with the accounting records or returns; or
- I have not received all of the information and explanations I require for my audit; or
- the Governance Statement does not reflect compliance with HM Treasury's guidance.

Report

I have no observations to make on these financial statements.

Sir Amyas C E Morse
Comptroller and Auditor General

National Audit Office
157-197 Buckingham Palace Road
Victoria
London SW1W 9SP

14 July 2014

The Board of the Pension Protection Fund

Statutory Reports

Chief Financial Officer's Review

Within the financial statements of the Pension Protection Fund we endeavour to provide readers with information presented in the clearest manner possible to understand the Board's financial position.

Over the following pages, I set out an overview of the financial performance of the PPF during the past year. This year has seen the strength of the fund grow once again. It has been a less significant year for claims, both in terms of number and value, even with the UK Coal schemes. Nevertheless, claims exceeded the levy raised. The growth in net assets has been due in part from improved actuarial assumptions and also from the return on the investment portfolio. The investment strategy has been successful in matching the market-driven movement in the liabilities using the LDI portfolio, while continuing to generate a surplus from the growth portfolio.

The claim arising from the UK Coal schemes was the single largest item during the year, as indicated in the contingent liabilities disclosure in last year's annual report. The net deficit on these schemes is included in the provision for schemes in assessment at 31 March 2014.

The financial position of the PPF at 31 March 2014 can be summarised by the funding ratio of 112.5% compared to 109.6% at the same point last year.

All figures in the following overview include the FCF.

Note disclosures and commentary

Alongside the principal financial statements and accompanying notes, we continue to present a commentary to highlight and explain important points in a number of the notes. These are identified by a shaded background and are not audited by the Comptroller and Auditor General, but have been reviewed for consistency. These notes comprise an introductory comment (identified by a shaded background and not subject to audit), a summary of accounting policies specific to individual financial statement items (included in a box) and the disclosures.

The report from the Comptroller and Auditor General on pages 55-56 confirms that there are no matters that need to be brought to readers' attention.

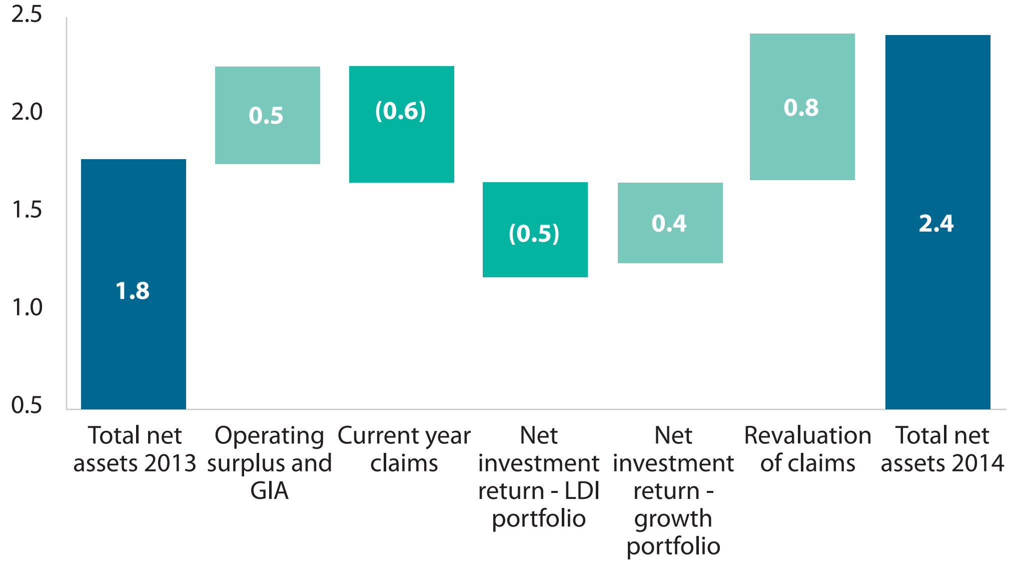
Andy McKinnon
Chief Financial Officer

Chief Financial Officer's review continued

Review of the Consolidated Statement of Comprehensive Net Income

The consolidated statement of comprehensive net income together with the statement of changes in reserves summarise the sources of the change in net assets during the reporting year. These are summarised in the following diagram and further explained in the subsequent commentary.

PPF net asset position movement 2014 (£bn)



Net operating surplus

This is the retained levy income after covering operating expenses. It excludes the effect of the administration levy which is received via DWP as grant-in-aid (GIA) and is required to be accounted for within the statement of changes in reserves.

Levy income of £576.6m shown in the consolidated statement of comprehensive net income was 11% lower (2013: 7% higher) than the prior year figure of £647.7m. £582.8m (2013: £645.6m) is the current year protection levy, with adjustments of prior levy years being £(6.2)m (2013: £2.1m). This was lower than our original published estimate of £630m as a result of the original underfunding and insolvency risk estimates used in the risk-based levy assessment process being higher than had been assumed.

Operating expenses include the expenses of administering the Financial Assistance Scheme (FAS) on behalf of DWP which are recoverable as GIA, again shown separately in the statement of changes in reserves. Other operating expenses (excluding FAS) rose by £2.9m as the operation continued to grow in scale and complexity. Operating expenses have fallen to £105.58 for each of the 452,758 members of the FAS and PPF schemes or in PPF assessment (2013: £109.07) and, as a percentage of year end total assets, PPF costs remained at 0.17% (2013: 0.17%).

After operating expenses, the net operating surplus of £528.8m was sufficient to cover 85% of this year's claims figure of £620.8m or 90% after taking into account the GIA.

Chief Financial Officer's review continued

Net investment return

The net return on investments for the year after investment expenses was an overall negative return of £103.0m (2013: positive return of £1,490.1m). This total is driven by the return on the LDI portfolio, designed to match gains and losses on liabilities of the PPF and those of schemes in assessment. The remainder of the PPF investment assets are managed as a diversified growth portfolio, as set out in the SIP, and have again generated a positive return in excess of target. The LDI portfolio returned £(466.3)m (2013: £798.0m) and the growth portfolio returned a net £363.3m (2013: £692.1m).

Net cost of claims

The net cost of claims was a negative charge of £216.6m (2013: positive charge of £1,424.0m), including claims for the current year of £620.8m (2013: £1,027.9m), the loss on actuarial liabilities and movements in the provision for schemes in assessment. The gain on actuarial liabilities was £525.6m (2013: loss of £703.2m), driven by the effect on the PPF liabilities of falling interest rates, other market movements and changes in actuarial assumptions.

The net movement in the provision for schemes in assessment was a positive figure of £311.8m (2013: £307.1m), the effect of the same market movements and changes in actuarial assumptions being more than offset by the impact of 16 schemes no longer considered probable for entry into the PPF.

The consolidated statement of financial position

The consolidated statement of financial position sets out the details at 31 March 2014 of the assets and liabilities held in all the funds for which the Board is responsible.

For schemes in assessment, although the claim has been recognised, the assets and liabilities remain outside of the PPF and the accounting treatment is simply to include a provision for the net deficit. However, we include the assets and liabilities in full when calculating the funding ratio.

Net assets, including schemes in assessment (SIA), now stand well in excess of £20bn and at 31 March 2014, represented 112.5% (2013: 109.6%) funding of the total liabilities.

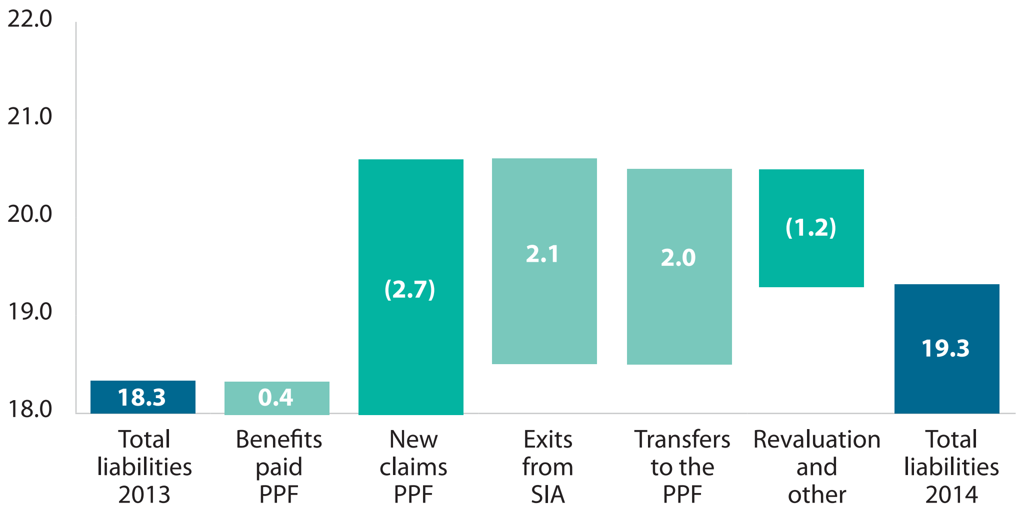
Total net assets at 31 March 2014

	Consolidated Statement of Financial Position £m	Not separately recorded in the Statement of Financial Position £m	Total £m
Assets and liabilities:			
Total assets	23,414.9	5,320.0	28,734.9
Investment and other financial liabilities	(6,969.9)	-	(6,969.9)
Net assets	**16,445.0**	**5,320.0**	**21,765.0**
Actuarial estimate of liabilities	(12,865.9)	(6,468.4)	(19,334.3)
Total net surplus/(deficit)	**3,579.1**	**(1,148.4)**	**2,430.7**

Chief Financial Officer's review continued

The following graph summarises the movements of the actuarial liabilities of the PPF and the claims provisions of FCF from £18,350.4m at the beginning of the year to the closing figure of £19,334.3m. The Actuarial valuation starting on page 93 gives details of how the liabilities have been calculated.

Movement in actuarial liabilities & PPF schemes in assessment (£bn)



The Board of the Pension Protection Fund

CONSOLIDATED STATEMENT OF COMPREHENSIVE NET INCOME

For the year ended 31 March

	Notes	2014 £m	2013 £m
Operating income			
Income from levies	3	576.6	647.7
Total operating income		**576.6**	**647.7**
Operating expenses			
Staff costs	11	(22.3)	(20.3)
Other costs	11	(25.5)	(24.7)
Total operating expenses		**(47.8)**	**(45.0)**
Net operating surplus		**528.8**	**602.7**
Investment activities			
Investment income	5	822.0	336.7
Change in fair value of investments	5	(837.9)	1,239.5
Investment expenses	5	(87.1)	(86.1)
Net investment return		**(103.0)**	**1,490.1**
Claims activities			
Current year claims for compensation	2	(620.8)	(1,027.9)
Revaluation of claims for compensation	2	311.8	307.1
Gains/(losses) on actuarial liabilities	1	525.6	(703.2)
Net cost of claims		**216.6**	**(1,424.0)**
Comprehensive net income for the year		**642.4**	**668.8**

The Board has no comprehensive income or expenditure other than the comprehensive net income disclosed above.
The accounting policies and notes on pages 66 to 91 form part of these financial statements.

The Board of the Pension Protection Fund

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

For the year ended 31 March

	Notes	2014 £m	2013 £m
Assets			
Operational cash		145.4	82.3
Investment assets	4	23,180.9	21,914.2
Levy receivables		44.8	30.7
Transfer-in receivables		30.6	133.2
Other financial assets		4.3	26.3
Property and equipment	12	8.1	0.3
Intangible assets	12	0.8	0.9
Total assets		**23,414.9**	**22,187.9**
Liabilities			
Investment liabilities	4	(6,926.5)	(7,056.6)
Other financial liabilities		(43.4)	(38.7)
Actuarial liabilities	1	(12,859.4)	(11,827.3)
Claims provisions	2	(1,154.9)	(1,503.7)
Total liabilities		**(20,984.2)**	**(20,426.3)**
Total assets less total liabilities		**2,430.7**	**1,761.6**
Represented by **Total levy and tax payer funds**		**2,430.7**	**1,761.6**

The Board of the PPF approved these accounts on 25 June 2014 and authorised the Accounting Officer to sign this Consolidated Statement of Financial Position on the same date.

Alan Rubenstein
Accounting Officer
10 July 2014

The accounting policies and notes on pages 66 to 91 form part of these financial statements.

The Board of the Pension Protection Fund

CONSOLIDATED STATEMENT OF CHANGES IN RESERVES

For the year ended 31 March

	Levy payer funds £m	Tax payer funds £m	Total Reserves £m
Balance at 31 March 2012	**1,065.6**	**(1.0)**	**1,064.6**
Total recognised net income for 2012/13	677.2	(8.4)	668.8
Grant-in-aid received in the year	19.0	9.2	28.2
Balance at 31 March 2013	**1,761.8**	**(0.2)**	**1,761.6**
Total recognised net income for 2013/14	650.9	(8.5)	642.4
Grant-in-aid received in the year	18.8	7.9	26.7
Balance at 31 March 2014	**2,431.5**	**(0.8)**	**2,430.7**

The accounting policies and notes on pages 66 to 91 form part of these financial statements.

The Board of the Pension Protection Fund

CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended 31 March

	2014 £m	2013 £m
Cash flows from operating activities		
Net operating surplus	528.8	602.7
Compensation payments	(445.1)	(331.8)
Assets from schemes transferring into the PPF receivable	373.3	535.6
Items reported in investment return but settled through operating bank accounts	(16.7)	(12.2)
Purchase of intangible assets	(0.4)	(0.9)
Purchase of property and equipment	(8.1)	(0.1)
Depreciation, amortisation and impairment charges	0.8	0.7
Movement in current liabilities	5.8	(4.3)
Movement in receivables	110.0	(98.5)
Net cash inflow from operating activities	**548.4**	**691.2**
Cash flows to investing activities		
Cash transfers to investment managers	(2,071.3)	(1,118.5)
Cash transfers from investment managers	1,559.3	438.8
Net cash outflow to investing activities	**(512.0)**	**(679.7)**
Cash flows from financing activities		
Financing from DWP for PPF activities (levy payer funded)	18.8	19.0
Financing from DWP for FAS activities (tax payer funded)	7.9	9.2
Net cash inflow from financing activities	**26.7**	**28.2**
Net increase in cash and cash equivalents in the year	**63.1**	**39.7**
Cash and cash equivalents at beginning of the year	**82.3**	**42.6**
Cash and cash equivalents at end of the year	**145.4**	**82.3**

The accounting policies and notes on pages 66 to 91 form part of these financial statements.

Statutory Reports

The Board of the Pension Protection Fund

Funds for which the Board is responsible

The Board is a statutory corporation, sponsored by the DWP, incorporated on 6 April 2005 under the Pensions Act 2004. The Act requires the Board to hold and apply statutory funds which constitute the three broad streams in which the financial activities of the Board are accounted for:

- the **Pension Protection Fund** itself
- the **Fraud Compensation Fund**
- the **Administration Funds**.

The **Pension Protection Fund (PPF)** holds substantially all the Board's assets and liabilities, receives protection levy income and incurs much of the Board's costs. Its assets arise from levy income collected, the investment return and assets transferred from schemes for which the PPF has assumed responsibility. The PPF's principal liabilities are to pension scheme members for whom it has assumed responsibility and a provision for the total estimated value of the deficits of schemes where eventual entry to the PPF is judged probable.

The **Fraud Compensation Fund (FCF)** receives fraud compensation levies and holds a fund to compensate schemes which have suffered loss due to acts of dishonesty.

The **Administration Funds** record some of the Board's administrative expense and the related funding. In its role as manager of the Financial Assistance Scheme (FAS) it administers payments to members of certain defined benefit pension schemes which are ineligible for PPF compensation and manages the transition of these schemes to our administrator and the transfer of the schemes' assets to the Government.

Core accounting policies

This section sets out the core accounting policies which apply throughout the financial statements. Accounting policies specific to particular elements of the financial statements are set out in boxes within the relevant note disclosures. The Board's core and specific accounting policies have been consistently applied.

Basis of preparation

These accounts have been prepared in accordance with an Accounts Direction dated 18 February 2010 issued by the Secretary of State for the Department for Work and Pensions, with the approval of the Treasury, in line with the Pensions Act 2004. The Accounts Direction stipulates compliance with the 2013/14 Government Financial Reporting Manual (FReM), which requires accounts to follow, as far as appropriate, private sector practice based on International Financial Reporting Standards (IFRS).

The accounts have been prepared on the going concern basis under the historical cost convention, except for the measurement at fair value through profit and loss of financial instruments and investment property, deposits with banks at amortised cost and the measurement of compensation benefits and associated provisions at the present value of the obligation.

Accounting standards which are particularly relevant to reporting on the Board's responsibilities and activities include:

- IFRS 7 Financial Instruments: Disclosures
- IAS 32 Financial Instruments: Presentation
- IAS 37 Provisions, Contingent Liabilities and Contingent Assets
- IAS 39 Financial Instruments: Recognition and Measurement
- IAS 40 Investment Property

Standards which are likely to affect future financial statements include:

- IFRS 9 Financial Instruments (currently expected to be effective for periods beginning on or after 1 January 2017)
- IFRS 10 Consolidated Financial Statements (effective for the Board for the period beginning 1 April 2014)
- IFRS 12 Disclosure of Interests in Other Entities (effective for the Board for the period beginning 1 April 2014)
- IFRS 13 Fair Value Measurement (currently expected to be effective for the Board for the period beginning 1 April 2015)

These standards are not expected to have a material effect on the Board's financial statements.

Consolidated financial statements

The financial statements consolidate the financial positions and results of the PPF, the FCF and the Administration Funds. The Board holds some investment assets through subsidiaries formed solely for that purpose. The underlying investments, income and gains and losses are recorded in the total investment portfolio. The subsidiaries are listed in note 15.

Segmental reporting

To comply with IFRS 8 Operating Segments, note 14 summarises the financial transactions and balances of the three separate streams of activity described in the introduction above: the PPF, the FCF and the Administration Funds. Further information is available in the notes on provisions for claims, levy income and operating expenses.

Foreign currency translation

These financial statements are presented in sterling, which is the functional currency of the Board.

Transactions denominated in foreign currency are recorded at the exchange rates prevailing on the dates of the transactions. All assets and liabilities denominated in foreign currencies are translated into sterling at the rates prevailing at the year end. Exchange differences arising on settlement and on retranslation are recognised in change in fair value. Forward foreign exchange contracts are valued at rates prevailing at the year end.

Core accounting policies continued

Impact of the Board assuming responsibility for schemes

Before entering the PPF, schemes go through an Assessment Period described at **www.pensionprotectionfund.org.uk/AssessmentPeriod/Pages/AssessmentPeriod.aspx**. Schemes which satisfy the criteria for transfer to the PPF (in particular that they have insufficient assets to meet their liabilities) receive a Transfer Notice under section 160 of the Pensions Act 2004, under which all their property, rights and liabilities are transferred to the Board. At the effective date of the Transfer Notice the scheme's net financial assets are transferred at fair value and its actuarial liabilities are valued using the same policies as apply to the Board's existing actuarial liabilities. Where the net deficit of a transferring-in scheme has been provided for at the end of the previous reporting period, changes in the value of the deficit due to changes in the value of the scheme's assets and liabilities from the previous accounting date up to the effective date of the Transfer Notice are accounted for as revaluation of claims.

Significant estimates and judgements

The preparation of financial statements requires management to make estimates and assumptions. Actual results could differ from estimates. Information about these judgements and estimates is contained in the relevant accounting policies and notes to the accounts. The key areas of estimation uncertainty are:

- actuarial liabilities and gains or losses on actuarial liabilities (note 1)
- claims provisions and contingent liabilities (note 2), and
- techniques for valuing financial instruments for which there is not a quoted price (note 4).

By virtue of the Pension Protection Fund (Tax) Regulations 2006, SI 2006/575, the Board is treated in the same way as UK registered pension schemes. Income from which recoverable withholding tax has been deducted is recorded gross, and the tax recoverable is included in receivables. Where tax withheld cannot be recovered, income is recorded net. The Board does not have to pay tax on its surplus or gains. VAT is normally irrecoverable in the European Union and is recognised as part of the expenditure to which it relates.

Paying compensation

This section describes:

- the PPF's liabilities to pay compensation to members
- provisions and contingent liabilities made for potential claims for schemes to enter the PPF and for schemes to be compensated by the FCF for losses caused by dishonesty.

1 - Liabilities to pay compensation to members

*The consolidated statement of financial position shows that at 31 March 2014 the PPF estimated the value of **existing liabilities to pay compensation to members at £12,859.4m**. During the year **the PPF paid members compensation of £445.1m**. After the actuarial valuation as at March 31 2014 was completed, **a net gain of £525.6m to the income statement** was recognised to decrease estimated liabilities to the amount needed to pay compensation to members.*

The amount of the PPF's liabilities to pay compensation to members (actuarial liabilities) is calculated by the Appointed Actuary – see the Actuarial valuation report starting on page 93.

The value is impacted by changes in actuarial assumptions, discount rates, operating expenses and other relevant factors, including the payment of benefits during the period.

Accounting policy

The Board recognises the full value of the liabilities of the PPF disclosed in the annual Actuarial valuation of the PPF. This includes:

- the present value of the liability to pay compensation to the members, both deferred and retired, of all pension schemes for which the Board has assumed responsibility, valued on the assumptions set out in the Actuary's Report
- an allowance for operating expenses permitted to be charged against the PPF, and
- a provision for the cost of eliminating inequalities caused by Guaranteed Minimum Pensions (GMPs).

Key judgements and estimates

The calculation of the actuarial liabilities of the PPF relies on assumptions about a number of financial and demographic factors, explained in Annex M2 of the Actuarial valuation.

The change in the total value of actuarial liabilities can be analysed as follows:

	2014 £m	2013 £m
Actuarial liabilities		
Opening value of actuarial liabilities	11,827.3	8,373.3
Actuarial liabilities of schemes which transferred to the PPF during the year	2,001.6	3,080.3
Increase in AVCs to be discharged	1.2	2.3
Actuarial (gains)/losses (see below)	(525.6)	703.2
Benefits paid to members	(445.1)	(331.8)
Total actuarial liabilities	**12,859.4**	**11,827.3**

Actuarial (gains)/losses are the net adjustment required to the outstanding amount of actuarial liabilities after accounting for schemes which have transferred into the PPF and the amount of benefits paid during the year. Actuarial (gains)/losses can be analysed as follows:

	2014 £m	2013 £m
Actuarial (gains)/losses		
Effect of passage of time on discounting	52.6	123.6
Change in assumptions	(698.6)	565.3
Change in experience	(81.6)	(52.0)
Other	88.9	2.3
Revaluation of current year transfers at 31 March	113.1	64.0
Total actuarial (gains)/losses	**(525.6)**	**703.2**

Paying compensation continued

2 – Provisions for claims on the PPF and the FCF

The consolidated statement of financial position shows ***total provisions of £1,154.9m for claims from pension schemes*** *with £1,148.4m being PPF (see page 71) and £6.5m for FCF (see page 72). The consolidated income statement shows* ***net cost of claims valued at a positive value of £216.6m and*** *also showed a benefit in net* ***reductions to the values of claims previously recorded of £311.8m*** *with £311.4m being PPF and £0.4m for FCF.*

The PPF provision relates to schemes in assessment and is calculated by the Appointed Actuary as the present value of estimated future compensation payments to be made by the PPF, less the value of existing assets in such pension schemes. The consolidated statement of comprehensive net income is affected by two elements of claims: the amount of new claims received in the year, and the effect of re-assessing the value of previously reported claims.

The FCF maintains a provision for claims that a pension scheme, with an insolvent sponsor, has lost money through dishonesty.

Accounting policies

The PPF considers all eligible pension schemes whose sponsoring employers have experienced a qualifying insolvency event before the end of the accounting period. Where eventual entry of the scheme into the PPF is judged probable, the Board recognises a provision.

Where the Board believes no qualifying insolvency event has occurred before the end of the accounting period but nonetheless the event could possibly occur and where it has sufficient information, a contingent liability will be disclosed.

The provision or contingent liability is valued at the net deficit impacting the PPF, that is:

- scheme liabilities calculated on the same basis as actuarial liabilities, less
- assets under the trustees' control, including asset recoveries from insolvent employers.

Within the FCF, the Board recognises provisions for claims where it is probable that an eligible pension scheme has suffered a loss due to an act of dishonesty. Where the success of a claim is judged possible, but less than probable, a contingent liability is disclosed.

Key judgements and estimates

The calculation of the costs of claims on both the PPF and the FCF relies on actuarial assumptions for the valuation of scheme liabilities and techniques such as rolling forward asset values as at a prior date to the Board's accounting date using investment indices (see page 97 for the PPF).

Claims on the PPF

Claims provisions, current year claims for compensation, the revaluation of claims for compensation and the total estimate of contingent liabilities relating to the PPF are summarised on the next page.

Paying compensation continued

Claims on the PPF

	Number of schemes	2014 £m	Number of schemes	2013 £m
Claims provisions at start of year	**191**	**1,499.1**	**256**	**1,695.7**
Current year claims for compensation				
Protected liabilities		2,596.9		3,121.8
Scheme assets including recoveries		(1,978.4)		(2,093.9)
Total current year claims for compensation	**107**	**618.5**	**114**	**1,027.9**
Revaluation of claims for compensation				
Release of provision for schemes no longer considered probable for entry	**(16)**	(29.2)	**(37)**	(123.6)
Revaluation of provisions brought forward from previous year end		(264.1)		(92.5)
Change in provisions for schemes transferring into the Protection Fund during the year		(18.1)		(82.1)
Revaluation of claims		**(311.4)**		**(298.2)**
Release of provisions for claims transferred to the PPF	**(122)**	**(657.8)**	**(142)**	**(926.3)**
Claims provisions at end of year	**160**	**1,148.4**	**191**	**1,499.1**

The claims provisions are calculated as the total estimated actuarial liabilities less the total value of assets reported as owned by schemes in assessment at 31 March:

	2014 £m	2013 £m
Total estimated actuarial liabilities for schemes in assessment	(6,468.4)	(6,518.5)
Total assets owned by schemes in assessment	5,320.0	5,019.4
Total net deficits of schemes in assessment	**(1,148.4)**	**(1,499.1)**

Current year claims for compensation on the PPF

Current year claims totalled £618.5m (2013: £1,027.9m) in respect of 107 (2013: 114) schemes. Provisions were made for 102 new schemes (or individual sections of schemes) (2013: 108 schemes) where eventual entry into the PPF is considered probable, and where reliable estimates can be made of the impact on the PPF. Also included are claims in respect of a further 5 schemes (2013: 6 schemes) in assessment estimated to be in surplus at the prior year end but now estimated to be in deficit.

Protected liabilities include provisions for equalisation of GMPs and expenses. The Appointed Actuary's Supplementary Report, in particular Annex S6, gives further information on these provisions.

Revaluation of claims for compensation on the PPF

In the PPF, of the 191 (2013: 256) schemes for which provisions were made as at the end of the previous year:

- 104 (2013: 133) schemes were transferred into the PPF during the year
- 16 (2013: 37) schemes' provisions have been released because the Board no longer considers it probable that the schemes will eventually transfer to the PPF, and
- the remaining 71 schemes, or scheme sections, (2013: 86) are judged likely to enter the PPF. The associated provisions have been retained and revalued.

Paying compensation continued

Release of provisions for claims transferred to the PPF

During the year 122 schemes (2013: 142) transferred into the PPF. Provisions had been created as at 31 March 2013 in respect of 104 of these schemes (2013: 133). A further 18 schemes (2013: 9) completed the assessment process during the year and transferred into the PPF, including 1 (2013: 4) which entered assessment during 2012/13.

Contingent liabilities for possible claims on the PPF

The total value of possible future claims on the PPF at 31 March 2014, net of the value of related scheme assets, was estimated as £776.5m (2013: £2,676.4m). Further analysis is given in Annex S6 of the Actuarial valuation.

Claims on the FCF

Claims provisions, current year claims for compensation, the revaluation of claims for compensation and the total estimate of contingent liabilities relating to the FCF are summarised below. There were three new claims and two claims were settled.

	Number of schemes	2014 £m	Number of schemes	2013 £m
Claims provisions at start of year	**7**	**4.6**	**8**	**13.5**
Current year claims for compensation				
New claims	3	2.3	-	-
Claims paid	(2)	-	(1)	-
Total current year claims for compensation	**1**	**2.3**	**(1)**	**-**
Revaluation of claims for compensation		(0.4)		(8.9)
Claims provisions at end of year	**8**	**6.5**	**7**	**4.6**

Contingent liabilities for possible claims on the FCF

The total value of possible future claims on the FCF at 31 March 2014 was estimated at £8.4m relating to 4 schemes (2013: £1.1m relating to 5 schemes).

Funding compensation – levy income and investment management

This section describes how the PPF and the FCF fund their obligations to pay compensation to members.

The PPF's Statement of Investment Principles (SIP) describes the primary objective as to have sufficient funds to pay compensation to members of eligible pension schemes. The PPF's funding objective, and managing the financial risks associated with it, is designed to achieve a balance between protecting and securing the compensation payments for current and potential members of schemes that come into the PPF while setting a fair and proportionate levy.

The PPF is funded principally from three main sources:

- private sector defined benefit schemes are charged a protection levy
- certain costs are covered by an administration levy, invoiced by the Pensions Regulator to schemes, which funds payments of grant-in-aid by the DWP to the PPF, and
- funds to pay compensation in the future are invested by external fund managers to earn an investment return.

The FCF is mainly funded by the fraud compensation levy and it has its own SIP.

3 - Income from levies

The consolidated statement of comprehensive net income shows that ***total levy income fell by £71.1m to £576.6m, £576.5m for the PPF itself and £0.1m for the FCF****. The PPF levy was £53.5m less than the estimate of £630m mainly because under the risk-based levy assessment process, the original underfunding and insolvency risk estimates turned out to be lower than had been assumed.*

Protection levies are charged to eligible pension schemes incorporating risk-based factors (principally scheme underfunding and employer insolvency risks) and scheme-based factors (principally the value of scheme liabilities). The principles, policies and procedures for levy assessment and invoicing are explained at ***www.pensionprotectionfund.org.uk/levy/Pages/PensionProtectionLevy.aspx****.*

Accounting policy

Protection levy and fraud compensation levy income is recognised on an accrual basis. As required by the FReM, DWP GIA, the mechanism used to receive administration levy funds, is credited directly to the General Reserve as contributions from a controlling party.

Provisions are made for amounts which may have to be credited or repaid following levy payers' appeals. Movements on these provisions are accounted for as adjustments to levy income. Invoiced amounts which cannot be collected from schemes are written off to operating expenses.

The Board did not raise a fraud compensation levy in 2013/14 (2012/13: 25p per eligible pension scheme member). Any levy is collected by the Pensions Regulator on the Board's behalf.

Funding compensation – levy income and investment management continued

Levy income for the year ended 31 March is summarised as follows:

	2014 £m	2013 £m
Risk-based levies in respect of the current year	529.0	573.8
Scheme-based levies in respect of the current year	53.8	71.8
Total protection levies in respect of the current year	**582.8**	**645.6**
Risk-based levies in respect of prior years	(9.3)	(3.4)
Scheme-based levies in respect of prior years	3.0	1.9
Total protection levies in respect of prior years	**(6.3)**	**(1.5)**
Income from protection levies	**576.5**	**644.1**
Income from fraud compensation levy	**0.1**	**3.6**
Total income from levies	**576.6**	**647.7**

Contingent liabilities relating to levy protection income

Some levy income amounts invoiced and paid over a number of years remain subject to the possibility of legal action concerning scheme eligibility. The Board considers, having taken legal advice, these amounts have been fairly invoiced and recognised as income, but it remains possible that the outcome of legal action could be that one or more of these amounts will be written off and money refunded. The total of these amounts is £88.7m (2013: £70.8m).

The above figures exclude DWP GIA funding which is included in movement in reserves. The consolidated statement of changes in reserves shows that the PPF also received administration levy funding through DWP GIA of £18.8m (2013: £19.0m).

4 - Investment assets and liabilities

The consolidated statement of financial position shows that at the year end the PPF and the FCF together had ***gross investment assets valued at £23,180.9m and investment liabilities of £6,926.5m, a net investment portfolio of £16,254.4m****. The consolidated statement of net income shows* ***a net investment loss (income and gains less investment expenses) of £103.0m****.*

The Board's approach to investment is summarised in the Statement of Investment Principles (**www.pensionprotectionfund.org.uk/DocumentLibrary/Documents/SIP_November_2012.pdf**) which summarises investment management governance, objectives, risk management, strategy, fund management and custody. FCF has its own SIP. The day to day fund management of the assets is performed by external fund managers.

The Board holds a wide range of investment assets and liabilities including UK Government bonds, bonds issued by other governments and corporate entities, public equity and alternative investments. To help manage the risks associated with its long-term liabilities to pay compensation to members, the Board has a programme of UK Government bonds sale and repurchase agreement transactions and derivatives (principally interest rate and inflation swaps). The 'Funding for the future' section (page 17) comments on the PPF's investment performance.

Funding compensation – levy income and investment management continued

The change over the year in the PPF's net investment portfolio is summarised as follows:

	2013	Assets transferred from Schemes in Assessment	Net purchases / (sales)	Net gains/ (losses)	Other movements	2014
	£m	£m	£m	£m	£m	£m
Financial assets designated at fair value through profit or loss						
Debt instruments	13,966.8	10.2	2,335.8	(885.6)	(24.2)	15,403.0
Money market funds	936.3	-	132.0	0.7	-	1,069.0
Equity	1,230.3	-	209.2	169.1	(0.6)	1,608.0
Securities funds	1,358.2	788.3	(1,186.9)	(88.6)	(5.9)	865.1
Private equity funds	318.9	60.5	50.9	22.2	(8.5)	444.0
Infrastructure funds	59.3	-	11.1	4.7	(3.2)	71.9
Farm and timberland	-	4.3	5.5	0.7	(0.4)	10.1
Investment property funds	632.4	46.2	(105.3)	10.8	(0.2)	583.9
Investment property held directly	44.7	-	136.0	1.2	-	181.9
Insurance policies	251.3	62.3	-	(29.3)	-	284.3
Other financial assets	8.4	-	-	-	-	8.4
	18,806.6	**971.8**	**1,588.3**	**(794.1)**	**(43.0)**	**20,529.6**
Other investment assets	3,107.6					2,651.3
Total investment assets	**21,914.2**					**23,180.9**
Total investment liabilities	(7,056.6)					(6,926.5)
Net investment portfolio	**14,857.6**					**16,254.4**

Other movements include amortisation and fund manager fees settled through disinvestment.

Assets transferred are in specie movements from schemes coming into the PPF.

Other investment assets and investment liabilities at 31 March comprise:

	2013 £m	2014 £m
Other investment assets		
Foreign exchange contracts	11.0	4.8
Other derivative financial instruments	2,597.5	2,076.7
Investment income receivable	89.6	98.1
Amounts receivable from investments sold	168.3	213.4
Cash at fund managers	241.2	258.3
Total other investment assets	**3,107.6**	**2,651.3**
Other investment liabilities		
Repurchase agreements	(4,277.6)	(4,291.9)
Amounts payable for investments purchases	(380.1)	(446.2)
Derivative financial instruments	(2,398.9)	(2,188.4)
Total investment liabilities	**(7,056.6)**	**(6,926.5)**

Funding compensation – levy income and investment management continued

	2014 £m	2013 £m
Debt instruments form the main element of our portfolio and consist of		
UK Government securities	9,259.2	8,908.2
Other government securities	3,504.5	2,894.6
Total government securities	**12,763.7**	**11,802.8**
UK corporate debt	178.4	173.4
Other corporate debt	890.8	770.2
Other debt instruments	1,570.1	1,220.4
Total debt instruments	**15,403.0**	**13,966.8**

UK Government securities include £4,291.9m (2013: £4,277.6m) sold under agreements to repurchase. Other debt instruments include mortgage-backed securities, alternative credit instruments, asset-backed securities and senior loans.

Financial instruments

Investment assets are all financial instruments except for investment property held directly.

Accounting policies

Classification

Financial instruments are classified at initial recognition as one of:

- Financial assets or liabilities at fair value through profit or loss, separated by:
  (a) those designated at fair value through profit or loss upon initial recognition and
  (b) those classified as held for trading (mainly derivatives - interest rate swaps, inflation rate swaps, options, credit default swaps and forward foreign exchange contracts to support liability driven investment)
- Loans and receivables.

Recognition and derecognition

Financial assets and liabilities at fair value through profit and loss are recognised initially on trade date. Other financial assets and liabilities are recognised on the date they are originated. Financial assets are derecognised when the right to receive cash flows has expired or the Board has transferred substantially all the risks and rewards of ownership or control of the asset. Financial liabilities are derecognised when the obligation to deliver cash or another financial asset is discharged or cancelled, or expires.

Securities sold subject to repurchase agreements remain on the consolidated statement of financial position and a liability is recorded for the consideration received.

Measurement

Financial instruments are measured at fair value, defined as the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

Quoted securities and other exchange-traded assets, including derivative contracts, are valued at closing prices at the end of the reporting period. Prices used are the bid price or last-traded price depending on the convention of the stock exchange or other market on which they are quoted. Pooled investment vehicles are valued at closing bid or single prices as appropriate. Assets for which a recognised investment exchange does not exist are valued at a fair value estimated by the Board's appointed fund managers or other appropriately qualified professional adviser. Where possible, the resulting valuations are validated by the Board's custodian. Derivative contracts which are not exchange-traded (often referred to as over-the-counter contracts) are valued at prices calculated by a pricing agent (and compared to the fund managers' own valuations) using valuation methodologies based on market sources as described below.

Key judgements and estimates

The choice of valuation technique and inputs to the valuation methodology (whether based on observable market data or not) are matters of judgment and involve the use of estimates. The amounts eventually realised from these financial instruments may differ from the estimated values disclosed in these accounts.

Funding compensation – levy income and investment management continued

Financial instruments measured at fair value

The following table analyses the financial instruments in accordance with IFRS 7 to reflect the significance of inputs used in assessing fair value.

Level 1 instruments are valued by reference to quoted prices in active markets for identical assets.

Level 2 instruments are valued using inputs (other than quoted prices taken directly from markets) observable either directly (eg through market information price feeds) or indirectly (ie derived from market rates, prices and other data). Level 2 assets consist mainly of:

- sovereign and corporate debt instruments
- managed funds investing in securities and properties
- derivatives, and
- repurchase agreement liabilities.

Sovereign and corporate debt instruments are valued using prices provided by price aggregation services which source prices from authorised brokers and dealers. These debt instruments are readily realisable.

Holdings of managed funds are normally valued based on unit prices based on current net asset values of the underlying assets. Derivative assets and liabilities are valued using discounted cash flow and options pricing models. These models use as their basis independently sourced market parameters including, for example, interest rate yield curves, inflation rates, option volatilities and currency rates.

The valuation of repurchase agreement liabilities reflects amounts borrowed from counterparties.

Level 3 assets are largely private equity funds and other funds not traded in active markets. These funds are asked to supply audited annual accounts which are mostly presented in accordance with IFRS or US generally accepted accounting principles. Insurance policy assets are valued by the PPF using actuarial models.

	Level 1 £m	Level 2 £m	Level 3 £m	2014 £m
Financial instruments measured at fair value at 31 March				
Debt instruments	462.1	14,940.9	-	15,403.0
Money market funds	1,053.9	-	-	1,053.9
Equity	1,608.0	-	-	1,608.0
Securities funds	-	856.4	8.7	865.1
Private equity funds	-	-	444.0	444.0
Infrastructure funds	-	-	71.9	71.9
Farm and timberland	-	-	10.1	10.1
Investment property funds	-	583.9	-	583.9
Investment property held directly	-	181.9	-	181.9
Insurance policies	-	-	284.3	284.3
Other financial assets	-	-	8.4	8.4
Foreign exchange contracts	4.8	-	-	4.8
Other derivative financial assets	-	2,076.7	-	2,076.7
Investment income receivable	98.1	-	-	98.1
Amounts receivable from investments sold	213.4	-	-	213.4
Cash at fund managers	258.3	-	-	258.3
Repurchase agreements	-	(4,291.9)	-	(4,291.9)
Amounts payable for investments purchased	(446.2)	-	-	(446.2)
Derivative financial liabilities	-	(2,188.4)	-	(2,188.4)
Total	**3,252.4**	**12,159.5**	**827.4**	**16,239.3**

Funding compensation – levy income and investment management continued

	Level 1 £m	Level 2 £m	Level 3 £m	2013 £m
Financial instruments measured at fair value at 31 March				
Debt instruments	495.5	13,413.4	57.9	13,966.8
Money market funds	936.3	-	-	936.3
Equity	1,230.3	-	-	1,230.3
Securities funds	-	1,358.2	-	1,358.2
Private equity funds	-	-	318.9	318.9
Infrastructure funds	-	-	59.3	59.3
Investment property funds	-	632.4	-	632.4
Investment property held directly	-	44.7	-	44.7
Insurance policies	-	-	251.3	251.3
Other financial assets	-	-	8.4	8.4
Foreign exchange contracts	11.0	-	-	11.0
Other derivative financial assets	-	2,597.5	-	2,597.5
Investment income receivable	89.6	-	-	89.6
Amounts receivable from investments sold	168.3	-	-	168.3
Cash at fund managers	241.2	-	-	241.2
Repurchase agreements	.-	(4,277.6)	-	(4,277.6)
Amounts payable for investments purchased	(380.1)	-	.-	(380.1)
Derivative financial liabilities	-	(2,398.9)	-	(2,398.9)
Total	**2,792.1**	**11,369.7**	**695.8**	**14,857.6**

The following table summarises the movement between opening and closing balances of Level 3 financial instruments.

	2014 £m	2013 £m
Financial assets		
Balance at start of year	**695.8**	**488.2**
Gains/(losses) in the statement of comprehensive net income	(7.5)	45.0
Purchases and assets transferred in	402.1	176.0
Sales	(239.4)	(5.8)
Transfers out of Level 3	(23.6)	(7.6)
Balance at end of year	**827.4**	**695.8**

Investment property held directly

Investment property does not include the office accommodation occupied by the Board.

Accounting policies

Investment properties held directly are measured initially at cost, including transaction costs. The PPF follows the fair value model option in IAS 40 Investment Property. Investment properties are valued at their fair value by independent valuers with recognised and relevant qualifications and recent and relevant experience. Gains or losses arising from a change in the fair value are recognised in the consolidated statement of comprehensive net income for the period in which it arises. At 31 March 2013 the Board owned 5 commercial properties in the UK, with a total fair value of £44.7m.

At 31 March 2014 the Board owned 18 (2013: 5) commercial properties in the UK, with a total fair value of £181.9m (2013: £44.7m).

Rental income recognised was £6.5m (2013: £0.7m). Direct operating expenses were not material. There were no restrictions on the realisability of property, income or disposal proceeds. At 31 March 2014 the PPF had exchanged contracts to buy investment properties for £9.6m (2013: £10.2m) subject to approval by the local council.

Funding compensation – levy income and investment management continued

5 - Investment return

Accounting policies

Investment income is accounted for on an accrual basis, that is:

- interest income arising from cash deposits, fixed and variable interest securities and similar investments is accounted for using the effective interest rate method, and
- dividends and distributions are accounted for when the dividend or distribution is declared.

Change in fair value of investments includes:

- gains and losses realised on the disposal of investments
- unrealised gains and losses on investments held at the accounting date, that is the difference between acquisition cost and current fair value, and
- gains and losses arising on the translation of investments (including cash, payables and receivables) denominated in foreign currencies into sterling.

Investment expenses are accounted for on an accrual basis.

	Net investment income 2014 £m	Change in fair value of investment 2014 £m	Total 2014 £m
Financial assets designated at fair value through profit and loss			
Debt instruments	436.4	(885.6)	(449.2)
Money market funds	11.4	0.7	12.1
Equity	24.1	169.1	193.2
Securities funds	0.1	(88.6)	(88.5)
Private equity funds	0.3	22.2	22.5
Infrastructure funds	0.1	4.7	4.8
Farm and timberland	-	0.7	0.7
Investment property funds	23.0	10.8	33.8
Investment property held directly	6.5	1.2	7.7
Insurance policies	20.2	(29.3)	(9.1)
Foreign exchange contracts	-	(6.3)	(6.3)
Interest payable	(29.2)	-	(29.2)
Net gain/(loss) from financial assets designated at fair value through profit and loss	**492.9**	**(800.4)**	**(307.5)**
Deposit interest	**416.2**	**-**	**416.2**
Held for trading			
Derivative financial instruments	**(87.8)**	**(23.3)**	**(111.1)**
Loans and receivables			
Other investment assets	**0.7**	**(14.2)**	**(13.5)**
Total investment return	**822.0**	**(837.9)**	**(15.9)**
Total investment expenses			
Fund management fees			(81.1)
Custody charges			(2.0)
Transactions cost			(4.0)
Total investment expenses			**(87.1)**
Net investment return			**(103.0)**

Funding compensation – levy income and investment management continued

	Net investment income 2013 £m	Change in fair value of investment 2013 £m	Total 2013 £m
Financial assets designated at fair value through profit and loss			
Debt instruments	361.2	656.9	1,018.1
Money market funds	2.8	18.6	21.4
Equity	18.0	211.4	229.4
Securities funds	-	111.1	111.1
Private equity funds	0.4	62.3	62.7
Infrastructure funds	3.3	7.7	11.0
Investment property funds	22.1	3.4	25.5
Investment property held directly	0.7	(2.5)	(1.8)
Insurance policies	16.3	(4.5)	11.8
Foreign exchange contracts	-	(136.0)	(136.0)
Interest payable	(19.2)	-	(19.2)
Net gain from financial assets designated at fair value through profit and loss	**405.6**	**928.4**	**1,334.0**
Deposit interest	**1.2**	**-**	**1.2**
Held for trading			
Derivative financial instruments	**(70.1)**	**314.6**	**244.5**
Loans and receivables			
Other investment assets	**-**	**(3.5)**	**(3.5)**
Total investment return	**336.7**	**1,239.5**	**1,576.2**
Total investment expenses			
Fund management fees			(78.8)
Custody charges			(1.1)
Transactions cost			(6.2)
Total investment expenses			**(86.1)**
Net investment return			**1,490.1**

Certain items previously reported as other investment expenses have been reallocated to the asset type to which they relate.

Statutory Reports

Financial risk management

Managing the payment and funding of member compensation described in the previous sections involves financial risk. The most important categories of financial risk, and the ways in which the Board manages them, are described in Section 4 of the PPF SIP (**www.pensionprotectionfund.org.uk/DocumentLibrary/Documents/SIP_ November_2012.pdf**).

A number of the risks described in the SIP come from holding financial instruments about which further disclosure is given below as required by IFRS 7

- **PPF credit risk** (referred to in the SIP as counterparty risk) – note 6
- **PPF liquidity risk** – note 7
- **PPF market risk** (which includes SIP valuation risk and currency risk) – note 8

These disclosures are followed by notes on:

- **FCF financial risks** – note 9
- **Administration Funds financial risks** – note 10

6 - PPF credit risk

Credit risk is the risk that a counterparty to a financial instrument will cause a financial loss for the PPF by failing to discharge an obligation. The main exposure to credit risk in the PPF's financial instruments arises from investments in sovereign, corporate and other debt instruments (further analysis is given in note 4). The PPF is also exposed to credit risk on derivatives, insurance policies, cash, transfer-in receivables and other receivables.

The principal elements of the PPF's internal policy for managing credit risk include:

- counterparties to derivative contracts should be rated at least A- and are subject to overall exposure limits
- a range of limits applies to counterparties to derivatives contracts and repurchase agreements
- investment management agreements require fund managers to deal with the highest-rated counterparties consistent with best execution, and
- collateral is taken under the terms of the relevant ISDA Master Agreement.

The Board is satisfied that credit exposure is in accordance with the risk appetite described in the SIP.

Financial assets exposed to credit risk at 31 March were:

	2014 £m	2013 £m
Debt instruments	15,403.0	13,966.8
Insurance policies	284.3	251.3
Other derivative financial assets	2,076.7	2,597.5
Amounts receivable from investments sold	213.4	168.3
Cash at fund managers	258.3	241.2
Investment income receivable	98.1	89.6
Operational cash	144.9	81.4
Levy receivables	44.8	30.7
Transfer-in receivables	30.6	133.2
Other receivables	-	2.5
Total	**18,554.1**	**17,562.5**

Levy receivables at 31 March are summarised below. 'Past due' is defined as older than 28 days, the time allowed to levy payers either to pay or to request a review of their levy invoice.

	Up to 3 months past due	3-6 months past due	Over 6 months past due	Total £m
2014	3.2	8.5	33.1	**44.8**
2013	0.1	0.3	30.3	**30.7**

Statutory Reports

Financial risk management continued

7 - PPF liquidity risk

Liquidity risk is the possibility that the PPF has insufficient cash available to:

- settle its financial liabilities when they fall due
- pay compensation to members
- pay for staff and other operating expenses, or
- meet investment commitments to fund managers, for example, capital calls on private equity and infrastructure investments, and purchases of investment property.

Cash requirements and operational cash balances are regularly forecast. Significant amounts of financial instruments could readily be liquidated should the need arise. Additionally, from 2013/14 onwards we have a liquidity risk dashboard and contingency/action plans should we be threatened by liquidity risk issues.

Financial liabilities

Financial liabilities are all due within one year, except for derivative financial instruments, as follows:

	Within 1 year £m	1-5 years £m	5-10 years £m	Over 10 years £m	Total £m
2014	11.3	89.3	134.1	1,953.7	**2,188.4**
2013	223.8	29.9	106.0	2,039.2	**2,398.9**

Paying compensation to members

Payments to members are projected in estimating the actuarial liabilities reported in the consolidated statement of financial position – see note 1 and the Actuarial valuation. Payments to members in the year totalled £445.1m (2013: £331.8m).

Collateral arrangements

At 31 March, the following assets were subject to collateral and similar arrangements with counterparties

	2014 £m	2013 £m
UK Government securities subject to sale and repurchase agreements	5,337.5	5,756.8
Securities lent to market counterparties	352.3	21.5
Total assets provided subject to collateral and similar arrangements with counterparties	**5,689.8**	**5,778.3**
Funds received as collateral for sale and repurchase agreements	4,291.9	4,277.6
Collateral received from counterparties	378.5	25.3
Total assets received subject to collateral and similar arrangements from counterparties	**4,670.4**	**4,302.9**

Capital commitments

Commitments to pay capital calls to fund managers at 31 March totalled:

	2014	2013
Denominated in US dollars	$1,551.1m	$1,198.5m
Denominated in euros	€92.0m	€97 .6m
Denominated in Australian dollars	A$126.8m	-
Denominated in sterling	£42.2m	-

The PPF has also committed capital to pay costs of approximately £0.7m in 2014/15 that relate to the move to new offices.

Statutory Reports

Financial risk management continued

8 - PPF market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate due to changes in market prices, and includes price risk, interest rate risk and currency risk.

Overall exposure to market risk is managed and illustrated in a number of ways. Annex S5 of the Appointed Actuary's Supplementary Report illustrates the sensitivity of the values of the Fund's assets and liabilities to changes in the rates of a wide variety of financial and non-financial factors. The scenarios modelled in this analysis cover changes in interest rates, changes in inflation rates (including where CPI rates diverge from RPI), changes in UK Government bond yields and changes in mortality assumptions and other demographic factors.

We estimate the sensitivity of the Fund's financial position to adverse changes in financial markets using a value at risk analysis as part of calculating the risk-based levy. The approach is described in the document Pension Protection Fund Consultation: Guidance for the Bespoke Investment Risk Calculation (www.pensionprotectionfund.org.uk/DocumentLibrary/Documents/1213_Investment_%20Risk_Guidance.pdf). Investment risk is monitored by reference to the impact of stress scenarios on assets and liabilities. Data on market movements and asset allocations is used to test the sensitivity of funding ratios across our schemes in assessment to changes in these factors. The asset and risk factor stresses applied reflect an immediate one standard deviation fall in funding (or asset value) calibrated over a one year period.

As at 31 March 2014, an immediate combination of the circumstances reflected in this scenario would result in an increase in assets of £1.8 bn (2013: £1.7 bn) and an increase in liabilities of £2.5 bn (2013: £2.4 bn), a net negative impact on the statement of financial position of £0.7 bn (2013: negative £0.7 bn).

Price Risk

Price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from interest rate risk or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting similar financial instruments traded in the market. The PPF's financial instruments are carried at fair value and fair value changes are recognised in the consolidated statement of comprehensive net income, therefore all changes in market conditions will directly affect total investment return.

The Board manages price risk by diversifying its investments across a range of asset types, both within the UK and globally, and sets asset allocation guidelines for the fund managers as per the table below at 31 March.

	2014 £m	**Actual %**	**Tolerance range**
Asset Class			
Global bonds	5,520.8		
UK bonds and cash	6,355.9		
Cash and bonds	**11,876.7**	**74.4%**	**65% - 85%**
Public equity	1,618.3	10.1%	5% - 20%
Alternatives (including property)	2,475.1	15.5%	10% - 25%
Total assets allocated per SIP	**15,970.1**	**100.0%**	

Alongside the strategic allocation, the SIP permits tactical investment views to enhance return or to control risk, within the overall risk appetite set by the Board. The actual investment values disclosed above incorporate tactical positions held at 31 March 2014 but exclude assets and liabilities held solely for hedging purposes.

Statutory Reports

Financial risk management continued

Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

The valuation of the PPF's liabilities is sensitive to interest rates, which is taken into account in setting the PPF's strategic asset allocation. The Board mitigates interest rate risk by using derivatives and repurchase agreements to closely match the sensitivities of liabilities to interest rates.

At the 31 March, PPF financial instruments exposed to interest rate risk were:

	Fixed rate £m	Variable rate £m	Non-interest bearing £m	2014 £m
Debt instruments	12,866.3	2,536.7	-	15,403.0
Money market funds	-	-	1,053.9	1,053.9
Equity	-	-	1,608.0	1,608.0
Securities funds	98.6	163.8	602.7	865.1
Private equity funds	-	-	444.0	444.0
Infrastructure funds	-	-	71.9	71.9
Farm and timberland	-	-	10.1	10.1
Investment property funds	-	-	583.9	583.9
Investment property held directly	-	-	181.9	181.9
Insurance policies	-	-	284.3	284.3
Other financial assets	8.4	-	-	8.4
Foreign exchange contracts	-	-	4.8	4.8
Other derivative financial assets	-	2,076.7	-	2,076.7
Investment income receivable	-	-	98.1	98.1
Amounts receivable from investments sold	-	-	213.4	213.4
Cash at fund managers	-	258.3	-	258.3
Repurchase agreements	(4,291.9)	-	-	(4,291.9)
Amounts payable for investments purchased	-	-	(446.2)	(446.2)
Derivative financial liabilities	-	(2,188.4)	-	(2,188.4)
Total	**8,681.4**	**2,847.1**	**4,710.8**	**16,239.3**

Statutory Reports

Financial risk management continued

	Fixed rate £m	Variable rate £m	Non-interest bearing £m	2013 £m
Debt instruments	13,052.3	914.5	-	13,966.8
Money market funds	-	-	936.3	936.3
Equity	-	-	1,230.3	1,230.3
Securities funds	244.5	973.1	140.6	1,358.2
Private equity funds	-	-	318.9	318.9
Infrastructure funds	-	-	59.3	59.3
Investment property funds	-	-	632.4	632.4
Investment property held directly	-	-	44.7	44.7
Insurance policies	-	-	251.3	251.3
Other financial assets	8.4	-	-	8.4
Foreign exchange contracts	-	-	11.0	11.0
Other derivative financial assets	-	2,597.5	-	2,597.5
Investment income receivable	-	-	89.6	89.6
Amounts receivable from investments sold	-	-	168.3	168.3
Cash at fund managers	-	241.2	-	241.2
Repurchase agreements	(4,277.6)	-	-	(4,277.6)
Amounts payable for investments purchased	-	-	(380.1)	(380.1)
Derivative financial liabilities	-	(2,398.9)	-	(2,398.9)
Total	**9,027.6**	**2,327.4**	**3,502.6**	**14,857.6**

Currency risk

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The PPF's liabilities are in sterling. The PPF's investment policy is to operate a currency management strategy to apply an optimal currency hedging ratio based on the characteristics of the related asset classes. At 31 March the residual un-hedged foreign currency exposure is as follows:

	2014 £m	2014 %	2013 £m	2013 %
Asset Class				
Euro	56.1	6.6%	125.4	10.4%
US dollar	313.3	37.1%	464.0	38.7%
Other currencies	475.4	56.3%	611.4	50.9%
Total	**844.8**	**100.0%**	**1,200.8**	**100.0%**

9 - FCF financial risks

The FCF has £15.1m (2013: £15.1m) of money market funds, and provisions valued at £6.5m (2013: £4.6m). The Board's policy is to build up a small surplus in the Fund by raising levies over a number of years. The FCF is at risk of a large and urgent claim, or a number of such claims occurring closely together. The Board considers this possibility unlikely however, and does not consider it proportionate to build up a large surplus, which would help to mitigate the risk, at the expense of levy payers.

Credit risk – The FCF's funds are principally in units in liquidity funds managed by external fund managers.

Liquidity risk – The FCF is not exposed to significant liquidity risks as assets are readily realisable. Additionally, the time required to assess new claims would allow the FCF to raise any further levy income needed.

Market risk – the FCF's holdings in money market funds are subject to some price risk and interest rate risk. Claims can include variable rate interest for the period between the effective date of loss and the date of compensation.

10 - Administration Funds financial risks

Because of the non-trading nature of the Board of the Pension Protection Fund's administration activities and the way it is financed, the Board is not exposed in this area to the degree of financial risk faced by business entities.

Statutory Reports

Operating the business

This section explains the elements of the consolidated financial statements which relate to operating the PPF's business, including operating expenses and infrastructure, and gives other required disclosures.

11 - Operating expenses

Operating expenses rose by £2.8m to £47.8m. Staff costs rose by £2.0m to £22.3m as staff numbers increased to resource major projects and develop control and management functions, and in response to staff turnover. We have re-presented certain costs between member payroll services and advisory and other professional services as we believe that this better reflects the costs of administering these services. Increased member numbers increased the external cost of running member payroll services by £1.6m to £9.4m. The increasing volume and complexity of member service and investment management have required additional information and processing systems, increasing the cost of IT and telephony by £1.0m to £3.9m. Accommodation costs include a provision of £1.4m for future costs under existing premises lease contracts which will not yield future benefits.

Total operating expenses are allocated to three funds: the PPF itself, the PPF Administration Fund and the FAS Administration Fund. The PPF is charged with the costs of creating and maintaining records of members entitled to PPF compensation, running payrolls to pay compensation and verifying data for the purposes of creating and maintaining data and running payrolls, investment costs and insolvency costs. Other costs are charged, as appropriate, to the PPF Administration Fund or the FAS Administration Fund.

Total operating expenses are summarised as follows:

	Pension Protection Fund £m	PPF Administration Fund £m	FAS Administration Fund £m	2014 £m
Staff Costs				
Wages and salaries	4.6	7.3	2.5	14.4
Social security costs	0.5	0.6	0.2	1.3
Other pension costs	0.9	1.3	0.5	2.7
Short term, seconded and temporary staff	1.6	2.0	0.3	3.9
Total staff costs	**7.6**	**11.2**	**3.5**	**22.3**
Other Costs				
Member payroll services	5.2	0.7	3.5	9.4
Staff related and recruitment	0.3	1.0	-	1.3
Advisory and other professional services	5.0	2.0	0.1	7.1
Statutory audit costs	-	0.1	-	0.1
Accommodation and general office	0.3	1.7	0.8	2.8
IT and telephony	2.6	1.0	0.3	3.9
Depreciation and amortisation charges	-	0.6	0.2	0.8
Write off receivables	0.1	-	-	0.1
Total other operating expenses	**13.5**	**7.1**	**4.9**	**25.5**
Total operating expenses	**21.1**	**18.3**	**8.4**	**47.8**

Statutory audit costs were £133,000 (2012/13: £130,000).

Operating the business continued

	Pension Protection Fund £m	PPF Administration Fund £m	FAS Administration Fund £m	2013 £m
Staff Costs				
Wages and salaries	3.5	6.2	2.6	12.3
Social security costs	0.4	0.6	0.2	1.2
Other pension costs	0.7	1.1	0.4	2.2
Short term, seconded and temporary staff	0.8	3.3	0.5	4.6
Total staff costs	**5.4**	**11.2**	**3.7**	**20.3**
Other Costs				
Member payroll services	4.0	1.0	2.8	7.8
Staff related and recruitment	0.3	1.1	0.1	1.5
Advisory and other professional services	4.4	2.2	0.6	7.2
Statutory audit costs	-	0.1	-	0.1
Accommodation and general office	2.1	1.6	0.8	4.5
IT and telephony	1.4	1.2	0.3	2.9
Depreciation and amortisation charges	-	0.5	0.2	0.7
Write off receivables	-	-	-	-
Total other operating expenses	**12.2**	**7.7**	**4.8**	**24.7**
Total operating expenses	**17.6**	**18.9**	**8.5**	**45.0**

Certain allocations between member administration costs and advisory and other professional services have been restated.

The average number of staff employed, including secondment and temporary staff, was:

	2014	2013
Permanent employees and fixed term contracts	255	227
Short term, seconded and temporary staff	28	35
Total staff	**283**	**262**

Pensions

Employees of the Board of the Pension Protection Fund are eligible for membership of the Principal Civil Service Pension Scheme (PCSPS) and can opt to join the defined benefit section, or to contribute to a stakeholder (defined contribution) arrangement. The PCSPS is an unfunded multi-employer defined benefit salary related scheme but the Board is unable to identify its share of the underlying assets and liabilities. Defined benefit contributions are therefore accounted for by the Board as if they were contributions to a defined contribution scheme. A full actuarial valuation of PCSPS was carried out as at 31 March 2010 and details can be found in the Cabinet Office: Civil Superannuation Resource Accounts (**www.civilservice.gov.uk/pensions**).

During the year to 31 March 2014, employer contributions of £2.6m (2013: £2.2m) were payable to the defined benefit section of the PCSPS at one of four rates in the range 16.7% to 25.8% (2013: 16.7% to 25.8%). The scheme's actuary reviews employer contributions every four years following a full scheme valuation. These contribution rates reflect the benefits as they are accrued, not when the costs are actually incurred, and reflect past experience of the scheme. Employees of the Board can opt to open a partnership pension account, which is a stakeholder pension with an employer contribution. Employer contributions of £39k (2013:£47k) were paid to one or more of a panel of three appointed stakeholder pension providers. Employer contributions were age-related and range from 3% to 12.5% (2013: 3% to 12.5%) of pensionable pay, and employers also match employee contributions up to 3% of pensionable pay. In addition, employer contributions were payable to the PCSPS to cover the cost of the future provision of lump sum benefits on death in service and ill health retirement of these employees. Accrued pension contributions at 31 March 2014 were £239k (2013: £190k) and were paid in April 2014.

Statutory Reports

Operating the business continued

Staff exit packages

Exit package payments agreed to former staff are summarised as follows:

	Number of compulsory redundancies		Number of other departures agreed		Total number of exit packages by cost band	
Exit package cost band	**2014**	**2013**	**2014**	**2013**	**2014**	**2013**
< £10,000	-	-	2	1	2	1
£10,000 - £25,000	1	-	-	1	1	1
£25,000 - £50,000	3	-	-	1	3	1
£50,000 - £100,000	-	-	-	1	-	1
Total number of exit packages	**4**	**-**	**2**	**4**	**6**	**4**
Total cost	**£128,563**	**-**	**£3,083**	**£160,833**	**£131,646**	**£160,833**

12 - Property and equipment and intangible assets

The PPF's property and equipment comprise IT hardware and furniture and fittings. Intangible assets are mainly the value of internally developed software.

Accounting policies

Property and equipment: IT hardware and furniture and fittings are capitalised if the cost of purchase either as a single item or as a group of related items bought for a common purpose exceeds £1,000.

Intangible assets: The costs of major software licences, development and enhancement are capitalised and amortised over their expected useful lives. Software maintenance costs are written off as incurred.

Depreciation: Depreciation is provided at rates calculated to write down the cost (less any estimated residual value) of each asset on a straight line basis over its expected useful life as follows:

Leasehold improvements	5 years
IT hardware	3-4 years
Other assets	3 years

	IT hardware £m	Furniture & fittings £m	Payment on account & assets under construction £m	Total property and equipment £m	Intangible assets £m
Cost					
At 1 April 2013	**4.8**	**1.0**	**0.1**	**5.9**	**4.4**
Additions in the year	-	-	8.5	8.5	-
Disposals in the year	-	-	-	-	-
Assets brought into use	0.1	-	(0.5)	(0.4)	0.4
At 31 March 2014	**4.9**	**1.0**	**8.1**	**14.0**	**4.8**
Depreciation and amortisation					
At 1 April 2013	**(4.7)**	**(0.9)**	**-**	**(5.6)**	**(3.5)**
Charged in the year	(0.2)	(0.1)	-	(0.3)	(0.5)
Disposals in the year	-	-	-	-	-
At 31 March 2014	**(4.9)**	**(1.0)**	**-**	**(5.9)**	**(4.0)**
Net book value at 31 March 2014	**-**	**-**	**8.1**	**8.1**	**0.8**

Operating the business continued

	IT hardware £m	Furniture & fittings £m	Payment on account & assets under construction £m	Total property and equipment £m	Intangible assets £m
Cost					
At 1 April 2012	**4.5**	**1.0**	**0.3**	**5.8**	**3.4**
Additions in the year	-	-	1.0	1.0	0.1
Disposals in the year	-	-	-	-	-
Assets brought into use	0.3	-	(1.2)	(0.9)	0.9
At 31 March 2013	**4.8**	**1.0**	**0.1**	**5.9**	**4.4**
Depreciation and amortisation					
At 1 April 2012	**(4.3)**	**(0.8)**	**-**	**(5.1)**	**(3.3)**
Charged in the year	(0.4)	(0.1)	-	(0.5)	(0.2)
Disposals in the year	-	-	-	-	-
At 31 March 2013	**(4.7)**	**(0.9)**	**-**	**(5.6)**	**(3.5)**
Net book value at 31 March 2013	**0.1**	**0.1**	**0.1**	**0.3**	**0.9**

In April 2014 the Board took occupancy of new business premises as described in note 13. As a result of this relocation, a number of substantially and fully depreciated items of property and equipment were written off. Additionally, new IT hardware was purchased that is estimated to have a useful economic life of 4 years.

13 - Operating lease commitments

In April 2014 the Board took occupancy of new business premises under a commercial lease, comprising rent, property service charges and the installation of certain fixtures and fittings. The lease has a period of 15 years from March 2014 with a rent review due after 5 years.

Additionally, at 31 March 2014 the Board continued to lease existing premises under a number of Memoranda of Terms of Occupancy (MOTO) with DWP under which a bundled facilities price comprising rent, rates and property service charges was payable to DWP Estates. A provision of £1.4m has been made for the amounts estimated to be payable to DWP for early termination of the MOTO and certain dilapidations and refurbishments of the premises. The Board permanently vacated these premises after the year end as part of a planned notice period.

Accounting policy

The commercial lease and the MOTO with DWP are treated as operating leases as defined in IAS 17 Leases. Payments under these leases are charged to the Statement of Comprehensive Net Income on the basis of amounts payable in the year.

As at the year end the total future minimum payments under these arrangements were:

	2014 £m	2013 £m
Not later than one year	1.3	1.6
Later than one year and not later than five years	4.7	-
Later than five years	10.7	-
Total	**16.7**	**1.6**

Statutory Reports

Operating the business continued

14 - Segmental analysis

As indicated earlier, the Board accounts for its financial activities in the following funds:

- The Pension Protection Fund itself
- The Fraud Compensation Fund, and
- The Administration Funds.

The elements of the consolidated financial statements attributable to each segment are summarised in the tables below. Additional information relating to each activity can be found in the following notes:

- Provisions for claims (note 2)
- Levy income (note 3)
- Operating expenses (note 11).

Consolidated statement of comprehensive net income

For the year ended 31 March	2014 £m	2013 £m
Pension Protection Fund		
Net operating surplus	555.4	626.5
Net investment return	(103.0)	1,490.0
Net cost of claims	218.5	(1,432.9)
Net comprehensive income	**670.9**	**683.6**
Fraud Compensation Fund		
Net comprehensive income	**(1.8)**	**12.6**
Administration Funds		
Operating expenses	**(26.7)**	**(27.4)**
Consolidated net comprehensive income	**642.4**	**668.8**

Consolidated statement of financial position

For the year ended 31 March	2014 £m	2013 £m
Total assets less total liabilities		
Pension Protection Fund	2,423.6	1,752.5
Fraud Compensation Fund	8.7	10.5
Administration Funds	(1.6)	(1.4)
Consolidated statement of financial position	**2,430.7**	**1,761.6**

Statutory Reports

Operating the business continued

15 - Subsidiaries

The Board holds a small proportion of its investment portfolio through subsidiaries. As at 31 March 2014 these were:

PPF Nominee 1 B. V. (a company registered in the Netherlands)

PPF Nominee 2 B. V. (a company registered in the Netherlands)

Crown Secondary Placement Plc (a company registered in Ireland).

The subsidiaries do not operate separately from the PPF's overall investment management processes, and the relevant assets, liabilities, income and expense are recorded with the appropriate asset classes in the PPF's accounting records. All subsidiaries are 100% owned by the Board and have a 31 March year end.

16 - Related party transactions

Accommodation costs totalling £1.9m (2013: £1.8m) were payable to the Estates Division of DWP under the arrangements described in note 13, Operating lease commitments. DWP is the sponsoring department. In addition to the accommodation costs in the year £26.7m (2013: £28.2m) was received from DWP in GIA. There are no other related party transactions to disclose.

17 - Events after the reporting period

On 8 April 2014 the House of Lords agreed a House of Commons amendment to the Pensions Bill 2013 – 14. These amendments will change the way PPF compensation cap operates. The changes will not come into force before April 2015 and will be incorporated into secondary legislation through the Pensions Act 2014. The amendments involve a change to the maximum level of compensation payable by the PPF. The amendments mean that members of schemes entering assessment after the Bill becomes an Act of Parliament will have an increased level of entitlement for each full year beyond 20 years service in their scheme. Additionally, members of schemes that have already transferred to the PPF will have their compensation increased prospectively. We estimate the likely impact on the consolidated statement of financial position, taking account of transferred schemes and schemes in assessment (current pensioners and non-pensioners expected to be capped in future), will be an increase of approximately 0.4% in the actuarial liability.

The accounts were authorised for issue on 14 July 2014, the date the Comptroller & Auditor General certified them. The accounts do not reflect events after this date.

Summary of Principal Findings of the Two Actuarial Valuation Reports

Since the previous valuation as at 31 March 2013:

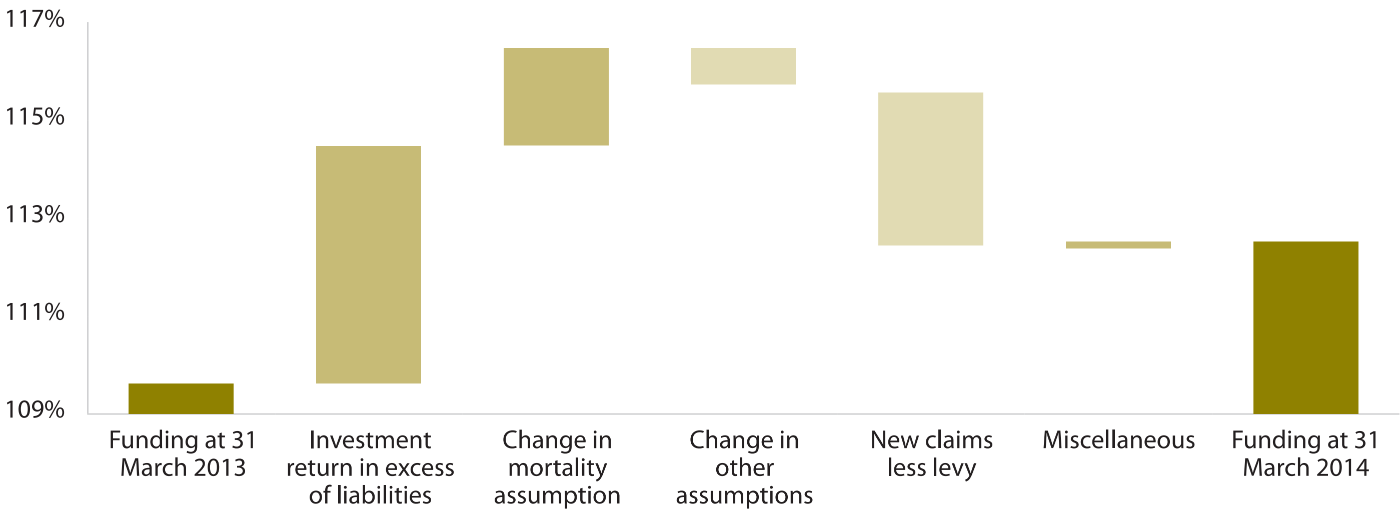
- 122 schemes have transferred into the PPF, bringing the total number of schemes which have transferred into the PPF as at 31 March 2014 to 694
- as at 31 January 2014, the number of members receiving compensation from the PPF has grown from 80,665 to 95,599 and the number of future retirees who will receive compensation from the PPF has increased from 91,353 to 100,070
- the excess of assets over liabilities in respect of those schemes already transferred into the PPF has increased from £3,252 million to £3,572 million, corresponding to an increase in the funding ratio from 127 per cent to 128 per cent for schemes already transferred
- the number of schemes in the assessment process which contribute to the provisions figure (schemes considered likely to transfer) has decreased from 187 to 158 as at 31 March 2014, and
- the excess of liabilities over assets in respect of those schemes forming the provisions has decreased from £1,499 million to £1,148 million.

The combined assets in respect of those schemes already transferred into the PPF and those schemes which are considered likely to transfer into the PPF exceeds the combined liabilities, resulting in an overall surplus of £2,424 million as at 31 March 2014, as summarised below:

	Assets £m	Liabilities £m
Schemes already transferred into the PPF	16,431.4	12,859.4
Estimated provisions in respect of schemes likely to be transferred	5,320.0	6,468.4
Total	**21,751.4**	**19,327.8**
Excess of assets over liabilities	**2,423.6**	
Funding Ratio (assets / liabilities)	**112.5%**	

This compares to a funding ratio of 109.6 per cent as at 31 March 2013.

The following chart shows the key factors that have contributed to the change in funding since last year:



Actuarial valuation

Actuarial valuation of the Pension Protection Fund

To: The Board of the Pension Protection Fund
From: Stephen Rice, Appointed Actuary
The actuarial valuation of the Pension Protection Fund as at 31 March 2014

1. Introduction

The Board of the Pension Protection Fund ('the Board') is required by paragraph 22 of schedule 5 to the Pensions Act 2004 to prepare a statement of accounts in respect of each financial year. Each statement of accounts must contain an actuarial valuation of the assets and liabilities of the Pension Protection Fund prepared and signed by the Appointed Actuary.

This is the ninth actuarial valuation of the Pension Protection Fund. The effective date of this valuation is 31 March 2014. The previous actuarial valuation was as at 31 March 2013, and the report on that valuation was dated 11 October 2013.

At its meeting on 26 April 2006, the Board appointed me to prepare the annual actuarial valuation of the assets and liabilities of the Pension Protection Fund. I intend my report to help the Board prepare the annual report and accounts as at 31 March 2014 and so I see the Board as the user of this report. As required by paragraph 22(5) of Schedule 5 to the Pensions Act 2004, the Board will be sending a copy of this report, as part of the statement of accounts, to the Secretary of State and also to the Comptroller and Auditor General. No party, apart from the Board, the Secretary of State and the Comptroller and Auditor General, should rely on any part of this report.

This report does not contain advice on the funding of compensation payable from the Pension Protection Fund. In particular, the results of this valuation are not used in the determination of the levy. All the results in this report are outcomes of a valuation exercise involving the quantification of amounts for recording in the annual report and accounts.

In my view, while the Actuaries' Code issued by the actuarial profession applies to the preparation of this report, there are no professional practice standards which directly apply. I have, however, prepared this report having regard to the principles in three Technical Actuarial Standards, namely TAS R (Reporting Actuarial Information), TAS D (Data) and TAS M (Modelling). This report should be considered alongside my supplementary report dated 9 July 2014. As my reports are prepared solely for the purpose of the PPF's annual report and accounts, I have not produced any projections of future accounting positions in either this or my supplementary report because the Board does not require them for its accounting disclosures.

The data and methodology used for the valuation as at 31 March 2014 differs slightly from previous valuations. These changes have been made to accommodate a revised timetable to provide the annual report and accounts earlier than in previous years. Liabilities were initially calculated based on market conditions as at 28 February 2014. These figures are then adjusted to reflect market conditions as at 31 March 2014. I believe that adopting this approach does not materially affect the accuracy of the results that would otherwise have been provided.

2. Membership data

As at 31 March 2014 694 schemes had transferred to the PPF. Compensation payments due in respect of the members of these schemes form the liabilities reported on in this report. Data in respect of the 694 transferred schemes has been received from four sources:

- For the 654 schemes where responsibility for the administration transferred to the PPF on or before 31 January 2014 and for four material schemes that transferred during February 2014, individual member data has been provided by the PPF's administrators, Capita. The effective date of the data was 31 January 2014 (or 11 February 2014 for the four material schemes that transferred on this date).
- For one scheme which had formally transferred to the PPF, but for whom as at 31 January 2014 the administration had yet to pass to Capita, individual member data has been provided by the administrator who was administering the scheme during the assessment period. The effective date of the data was 10 January 2014.
- In addition, member data grouped by age and gender was provided by the administrator who was administering the scheme during the assessment period for a further four schemes with material liabilities which transferred in February or March 2014 (not including the four schemes referred to in the first bullet point). Each scheme's effective date of the data was between October 2007 and December 2011.
- Finally, for the remaining 31 schemes (smaller schemes which transferred in February or March 2014), liabilities were determined from the latest section 143 or 179 valuation provided as part of the scheme returns submitted on to the Exchange database maintained by the Pensions Regulator. Liabilities calculated in this way account for about 1.5 per cent of the total liabilities transferred to the PPF.

Due to the accelerated timescale for providing valuation results, it was necessary to receive extracts of data at an earlier date than for previous years. Adjustments have been applied to ensure the data is consistent with the valuation date and that the accuracy of the valuation results is not materially affected.

I have carried out some overall checks on this data for general reasonableness and to ensure that it is consistent with that used in the actuarial valuation at 31 March 2013 and have no material concerns relating to the accuracy of the data provided.

A summary of the individual member data is as follows (figures in brackets are as at 31 March 2013):

Deferred pensioners

Sex	Number	Average age	Total accrued pension revalued to 31 January 2014 (uncapped) £000s pa
Male	67,309 (60,892)	50.8 (50.1)	266,341 (238,469)
Female	32,761 (30,461)	49.1 (48.5)	69,423 (64,025)
Total	**100,070 (91,353)**	**50.2 (49.6)**	**335,764 (302,494)**

Pensioners

Status	Sex	Number	Average age	Total Compensation at 31 January 2014 (capped where applicable) £000s pa
Members	Male	57,314 (48,107)	69.7 (68.9)	302,951 (250,795)
	Female	23,481 (20,493)	69.5 (68.8)	48,061 (41,414)
Dependants (excluding children)	Male	1,375 (1,146)	72.1 (71.3)	1,908 (1,631)
	Female	13,117 (10,640)	75.0 (74.4)	37,513 (29,541)
Children	Male	152 (134)	15.1 (15.9)	221 (174)
	Female	160 (145)	15.6 (15.5)	229 (201)
Total		**95,599 (80,665)**	**70.2 (69.4)**	**390,883 (323,756)**

Individuals who are receiving one tranche of compensation as well as being entitled to a further tranche of compensation, beginning after 31 January 2014, are included in both tables.

A summary of the data used for the 35 schemes where individual data was not available is as follows:

	Number of members	Average age	Estimated pension as at 31 March 2014 £000s pa
Deferred Pensioners	3,724	49.3	11,065
Pensioners	2,094	69.8	15,719

3. Compensation

Compensation for PPF members has been determined in accordance with the provisions of Schedule 7 to the Pensions Act 2004 and consequent regulations. A summary of the compensation provisions is shown in Annex M1.

4. Method

The approach to placing a value on the liabilities depends on whether individual membership data is available or not.

Method where individual or grouped membership data is available.

The expected compensation cash flows have been estimated for PPF members for whom individual or grouped data was provided by Capita or the administrator. In estimating each yearly compensation cash flow for each member, account is taken of:

- the initial amount of compensation or accrued pension
- mortality
- the normal pension age for deferred members
- compensation increases
- the PPF compensation cap, and
- the probability of survivors' compensation being paid.

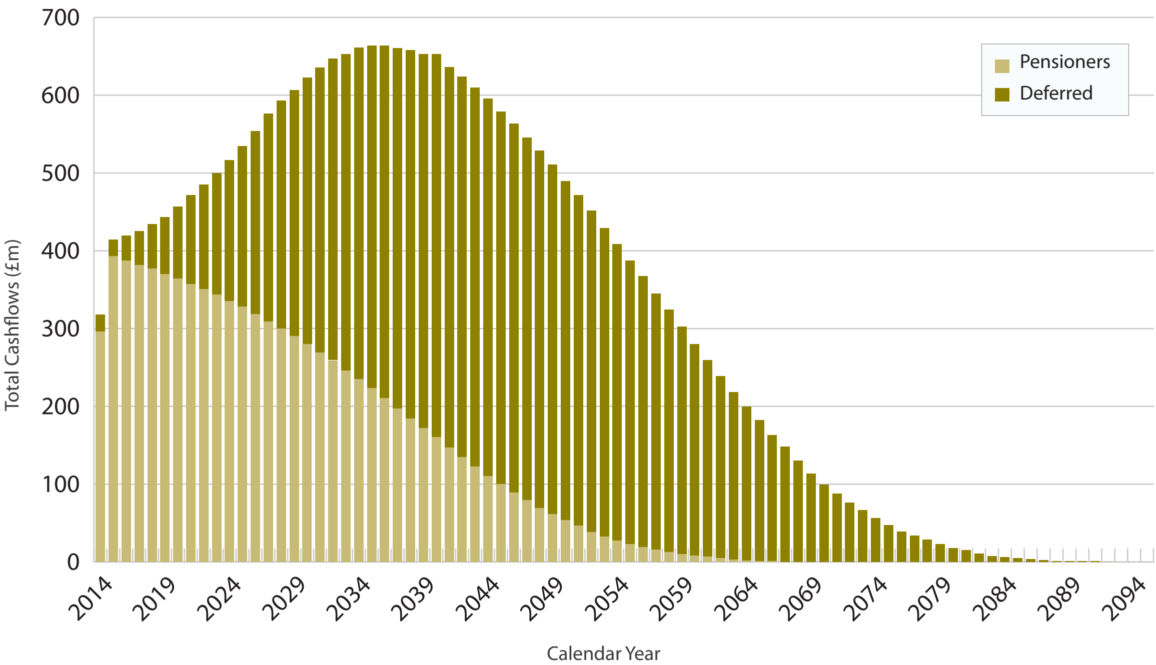
Total Cashflows

The resulting yearly compensation cash flows are discounted back to a present value and summed to obtain the actuarial present value of each member's liability.

Initially liabilities were calculated as at 28 February 2014 and based on assumptions derived from market conditions as at 28 February 2014. A loading was subsequently applied to this initial calculation of the liabilities to allow for the change in market conditions as at 31 March 2014 and the change in calulation date to 31 March 2014. The loading was calculated as the percentage difference in the present value of the projected cashflows calculated as at 28 February 2014 using assumptions as at 31 March 2014 and the present value of the projected cashflows as at 28 February 2014 using assumptions as at 28 February 2014, plus an allowance for the time value of moving the valuation forward to 31 March 2014.

The financial and demographic assumptions employed are described briefly in the next section of this report and set out more fully in Annex M2.

The total expected cash flows for all schemes that transferred to the PPF as at 31 March 2014 are shown in the following chart (ignoring early and late retirement and commutation of annual compensation for a lump sum).



Method where individual or grouped membership data is not available

Where individual or grouped data is not available, the section 179 value of the liabilities was rolled forward to 31 March 2014 based on market conditions at that date.

Where individual data is not available, the section 143 or 179 value of the liabilities was rolled forward to 31 March 2014 based on market conditions at that date.

The methodology used to roll the section 143 or 179 liabilities forward to 31 March 2014, at the same time changing the valuation assumptions to those described in Annex M2, is consistent with that to be applied for the calculation of levy in the financial year 1 April 2014 to 31 March 2015 (ignoring smoothing and stressing of assets and liabilities). The 14/15 methodology is available in the Pension Protection Levy section of the Pension Protection Fund web-site at: **www.pensionprotectionfund.org.uk/DocumentLibrary/Documents/1415_transformation_appendix.pdf**

A further adjustment has been applied to the liabilities for the expected cost of GMP equalisation. Further details on the adjustment applied can be found in Annexes M1 and M2.

An adjustment was also made for the payment of benefits from the effective date of the section 143 or section 179 valuation up to the valuation date.

Actuarial valuation

5. Assumptions

The approach to deriving the assumptions also depends on the availability of individual membership data. Where individual data is available, term-dependent financial assumptions can be adopted and cash flows can be generated; also, mortality rates can relate to the circumstances of an individual, for example taking into account their gender, postcode and amount of compensation. Where individual data was not available, average assumptions were used. Annex M2 describes both approaches to deriving the assumptions in more detail.

In order to estimate future compensation cash flows in respect of PPF members I have needed to make assumptions about:

- annual increases in payment to that element of their compensation which accrued after 5 April 1997
- revaluation of compensation in deferment for those whose compensation does not begin to be paid until after the valuation date, 31 March 2014
- their future mortality and other demographic features, and
- whether the Secretary of State exercises his power under paragraph 30 of Schedule 7 of the Pensions Act 2004 to vary the 100 per cent level of compensation for those members in category 1 of Annex M1 and the 90 per cent level of compensation for those members in category 2 of Annex M1.

In order to determine the present value of the liabilities, I have needed to discount the compensation cash flows, estimated as described above, back to the valuation date, 31 March 2014.

The Appointed Actuary has responsibility for the assumptions used in the statutory valuation of the assets of the PPF and the transferred liabilities, which are the subject of this report. The Board has responsibility for the assumptions used to value the assets and liabilities for schemes forming the provisions, as well as contingent liabilities, which are the subject of my supplementary report. Since there is a large overlap in the two sets of assumptions, past practice has been to adopt the same assumptions, as far as possible, for both purposes, which are agreed by the Board.

In proposing the assumptions for the 2014 actuarial valuation, I have taken note of the Accounts Direction which is given by the Secretary of State for Work and Pensions with the approval of HM Treasury in accordance with Schedule 5, Part 4 of the Pensions Act 2004.

Under this direction, the Board is required to prepare accounts in compliance with:

- the accounting principles and disclosure requirements of the current edition of the Government Financial Reporting Manual (the 'FReM') issued by HM Treasury which is in force for the financial year for which the accounts are being prepared
- other guidance issued by HM Treasury in respect of accounts which are required to give a true and fair view, and
- the Framework document agreed with the PPF Board.

The existing Accounts Direction also states that the discount rate used to discount future cash flows and liabilities should be that advised by the PPF's actuary (in accordance with Schedule 5 Part 4 section 22(4)(b) of the Pensions Act 2004 and the PPF valuation regulations 2005 and 2006).

None of the above provides direction on the choice of assumptions made for the valuation. However, in taking account of these documents and the Accounts Direction, the Board is required to place a value on the provisions which is the best estimate, ie is equally likely to overstate as to understate the actual value.

This follows from IAS 37, which the Board is required to take into account in accordance with the FReM. As the same choices of assumptions are made as far as possible for this report as for valuing the provisions, the value placed on liabilities of the PPF is also best estimate. I have chosen to do this using market pricing where possible.

A full description of the assumptions made can be found in Annex M2.

I have also carried out a sensitivity analysis in which the effect on the assets and liabilities is shown of changes in certain key assumptions. The results of this analysis may be seen in the supplementary report which I have prepared concerning provisions in respect of the PPF as at 31 March 2014.

6. Value of assets

The value of the PPF assets is determined in accordance with regulations 2, 4 and 5 of the Pension Protection Fund (Valuation of the Assets and Liabilities of the Pension Protection Fund) Regulations 2006 (SI 2006 / 597).

I have adopted the value of the PPF assets as stated in the relevant accounts prepared by the Board for the financial period ending on 31 March 2014. I have not adopted either of the adjustments made available by regulations 4 and 5 as I considered that it was not appropriate to do so.

Accordingly, I have taken the value of the PPF assets as at 31 March 2014 as £16,431,400,000. This includes £3,650,000 in respect of AVC assets that match AVC liabilities yet to be discharged.

This compares with £15,078,900,000 as at 31 March 2013.

An analysis of the change in the value of the assets of the Fund between 31 March 2013 and 31 March 2014 is as follows:

	£000s
Value of assets at the start of the year (31 March 2013)	**15,078,900**
Assets for schemes entering the PPF during the year to 31 March 2014 (measured at their transfer dates)	1,334,100
Assets received in respect of schemes transferred in prior years	9,700
Income from Pension Protection Levies	576,500
Compensation paid	(445,100)
Change in current assets (AVCs to be discharged)	1,200
Change in value of interest rate swaps and inflation swaps	(325,200)
Change in value of repurchase agreements	(80,400)
Change in value of invested assets on account of changes in bond yields	(50,600)
Change in value of invested assets on account of other changes (excluding bond yields, interest rate swaps, inflation swaps and repurchase agreements) net of investment management expenses.	440,300
Investment expenses	(87,100)
Staff and other costs	(21,100)
Miscellaneous	200
Value of assets at the end of the year (31 March 2014)	**16,431,400**

7. Value of liabilities

The value of the PPF liabilities is determined in accordance with regulation 3 of the Pension Protection Fund (Valuation of the Assets and Liabilities of the Pension Protection Fund) Regulations 2006 (SI 2006 / 597). This requires that:

- the liabilities of the Pension Protection Fund shall be any sums or properties falling to be paid or transferred out of the Fund required to meet liabilities listed in section 173(3) of the Pensions Act 2004, and
- the value of a liability shall be the present value of that liability at the valuation date.

The actuarial liabilities in respect of PPF members on the assumptions described in section 5 and Annex M2, are summarised in the table below:

Type of member	**£000s**
Deferred pensioners	6,125,400
Pensioners	6,381,300
Administration expenses to be met from the Fund	349,100
Current liabilities (AVCs to be discharged)	3,600
Total	**12,859,400**

Accordingly I have taken the value of the liabilities of the Pension Protection Fund as at 31 March 2014 as £12,859,400,000.

This compares with £11,827,300,000 as at 31 March 2013.

An analysis of the change in the actuarial liabilities between 31 March 2013 and 31 March 2014 is as follows:

	£000s
Actuarial liabilities at the start of the year (31 March 2013)	**11,827,300**
Effect of passage of time on discounting	52,600
Compensation paid	(445,100)
Actuarial (gain)/loss due to experience being different from what was assumed	(81,600)
Liabilities for schemes entering the PPF during the year to 31 March 2014 (measured at schemes' transfer dates)	2,001,600
Revaluation between transfer date and 31 March 2014 for schemes that entered the PPF during the year	113,100
Actuarial (gain)/loss due to changes in financial assumptions	(562,900)
Actuarial (gain)/loss due to changes in mortality assumptions	(135,700)
Change in GMP equalisation allowance	47,400
Change in expense allowance	41,500
Change in current liabilities (AVCs to be discharged)	1,200
Actuarial liabilities at the end of the year (31 March 2014)	**12,859,400**

8. Conclusion

As at 31 March 2014, the value of the PPF's assets was £16,431,400,000 and the value of the liabilities was £12,859,400,000. These values have been determined in accordance with the Pension Protection Fund (Valuation of the Assets and Liabilities of the Pension Protection Fund) Regulations 2006 (SI 2006 / 597).

The excess of assets over liabilities was £3,572,000,000 as at 31 March 2014, which corresponds to a funding ratio of 128 per cent.

This excess of assets over liabilities needs to be understood in the context of additional pension schemes that had entered into an assessment period, as defined in section 132 of the Pensions Act 2004, with effect from a date on or before 31 March 2014.

Therefore, in addition to this formal report on the assets and liabilities, I have estimated provisions in respect of the assets, potential recoveries and liabilities of those schemes which, in the Board's judgement, are likely to be transferred into the PPF. These provisions are shown in my supplementary report to the Board dated 9 July 2014 and will be shown in the statement of accounts being prepared by the Board for the financial period ending on 31 March 2014.

I have also estimated contingent liabilities as at 31 March 2014, in respect of other pension schemes which, in the Board's judgement, may possibly be transferred into the PPF in the near future. These contingent liabilities are shown in my supplementary report to the Board dated 9 July 2014 and will be disclosed in footnotes to the statement of accounts prepared by the Board for the financial period ending on 31 March 2014.

Signed: Stephen Rice

Date: 9 July 2014

Name: Stephen Rice, Appointed Actuary

Job Title: Chief Actuary

Qualification: Fellow of the Institute and Faculty of Actuaries

Employer: The Board of the Pension Protection Fund

Annex M1 Summary of compensation provided by the Pension Protection Fund

Broadly speaking, the PPF provides two levels of compensation:

1. For individuals who have reached their scheme's normal pension age before the assessment date or, irrespective of age, are in receipt of either a survivor's pension or a pension on the grounds of ill health, the PPF pays a compensation level of **100 per cent**.

   In broad terms and in normal circumstances, this means a starting level of compensation that equates to 100 per cent of the pension in payment immediately before the start of the assessment period, as defined in section 132 of the Pensions Act 2004. This is subject to a review of the rules of the scheme by the Board.

2. For most people aged below their scheme's normal pension age on the assessment date, the PPF pays a compensation level of **90 per cent**.

   In broad terms and in normal circumstances, this means 90 per cent of the pension an individual had accrued immediately before the assessment date (subject to a review of the rules of the scheme by the Board).

   Compensation is revalued in line with the increase in the RPI between the assessment date and March 2011, and the increase in the CPI between March 2011 and the commencement of compensation payments. This is subject to a floor of 0 per cent over the whole period, and to a maximum increase of 5 per cent a year for the whole period (2.5 per cent a year for pension accrued on or after 6 April 2009). Compensation is subject to an overall cap, which from 1 April 2014 equates to £36,401.19 a year at age 65 (the cap is adjusted according to the age at which compensation comes into payment).

   On 25 June 2013 the Pensions Minister announced his intention to introduce a service-related compensation cap. The new legislation was not in force on 31 March 2014 and so I have made no allowance for it in this valuation.

For both categories of members, once compensation is in payment, the part that derives from pensionable service on or after 6 April 1997 is increased on 1 January each year in line with:

- for years 2011 and earlier, the increase in the RPI capped at 2.5 per cent and with a floor of 0 per cent, and
- for years 2012 and later, the increase in the CPI capped at 2.5 per cent and with a floor of 0 per cent.

Also, after a member's death, compensation is paid to any children who are under 18 years old, or under 23 if they are in full-time education or have a disability. Generally compensation will be paid to any legal spouse, civil partner or other relevant partner. However, individual circumstances may differ in this regard depending on the rules of the former pension scheme.

Under the Pensions Act 2004, the Board has a duty to pay compensation on a basis that is no more or less favourable to a woman (or man) than it would be to a comparable man (or woman) in respect of pensionable service on or after 17 May 1990. In meeting this requirement, the Board must take into account any differences in scheme benefits that have arisen owing to differences in the calculation of Guaranteed Minimum Pensions (GMPs) for males and females. Accordingly, all schemes for which the Board assumes responsibility on or after 1 June 2013 are required to equalise members' compensation prior to transfer, and the Board is undertaking work to adjust compensation for members of unequalised schemes which have already transferred to the PPF.

Annex M2 sets out the assumed loading for GMP equalisation which has been applied to the liabilities of unequalised schemes.

Under paragraphs 29 and 30 of Schedule 7 of the Pensions Act 2004, the Board:

- has the power to alter the rates of revaluation and indexation, and
- can recommend to the Secretary of State for Work and Pensions that the percentage of benefits paid as compensation is varied.

It is expected that such provisions would only be used in exceptional circumstances, as the Board has other powers it could use if the financial position did deteriorate, for example the ability to amend the amount of levy it collects. I have therefore assumed that the Board does not exercise this discretion.

Annex M2 Assumptions

Assumptions in respect of schemes for which the Board assumed responsibility on or before 31 March 2014 will be either the same as, or derived in the same way as, those derived for the valuation as at 31 March 2013, unless stated otherwise.

a) Compensation levels

As for previous valuations of the Pension Protection Fund, I have continued to assume that the Secretary of State will not exercise his power under paragraph 30 of Schedule 7 of the Pensions Act 2004 to vary the 100 per cent level of compensation for those members in category 1 of Annex M1 and the 90 per cent level of compensation for those members in category 2 of Annex M1.

The new legislation introducing a service-related compensation cap was not in force on 31 March 2014 and, as such, I have made no allowance for it in this valuation.

b) Financial assumptions

Financial assumptions where individual membership data is available

For the liabilities in respect of transferred schemes where individual data is available, I have applied the same rationale in setting the financial assumptions as I did in my report as at 31 March 2013. I consider that it is still appropriate for the financial assumptions to vary according to the term of the particular cash flow being estimated and discounted.

i) Discount rates

I consider that a notional portfolio of assets consisting of cash plus appropriate zero-coupon interest rate swaps contracts and inflation swaps contracts plus gilt strips (or notional gilt strips) provides the best match to the PPF liability cash flows. Calculating the liabilities in this way represents a low-risk approach to the setting of the financial assumptions, in the sense that there should be a low risk of the notional assets being inadequate to pay the PPF members as at the valuation date their full compensation.

Under the terms of a zero-coupon interest rate swap contract with notional principal P and tenor (=duration) N, the PPF would at time N pay interest to the counterparty on P of the London Interbank Offered Rate (Libor) while the counterparty would at the same time pay to the PPF a fixed interest rate specified in the contract.

Since around August 2008, zero-coupon interest rate swap yields for longer tenors have been lower than the gilts strip yields at the same duration. It is therefore considered reasonable to construct a notional portfolio so that it contains gilts strips (or more often notional gilts strips) at longer durations and cash and swaps contracts at shorter durations.

Because it is difficult to earn close to Libor interest on cash, a deduction is made from the zero-coupon interest rate swap yields of 15 basis points at each term.

The discount rate for each term is therefore taken as the higher of the zero-coupon interest rate swaps yield less 15 basis points and the gilts strip yield. In practice, at the valuation date this broadly leads to the use of swaps rate less 15 basis points for terms up to five years and gilts strip yields thereafter.

A zero-coupon interest rate swaps yield curve as at 31 March 2014 was obtained from Insight Investment who constructed the curve by seeking indicative prices from investment banks.

A gilts strip yield curve as at 31 March 2014 was obtained from Insight Investment, which was derived from information available from the UK Debt Management Office. This curve shows gilt strips yields at terms from one year to 50 years inclusive. Yields at each of these terms are in respect of bonds with the closest nominal maturity to the indicated term. As the zero-coupon swaps curve and gilt strips curve both extend only as far as term 50, I have assumed that the forward rate applying in each year after year 50 is the same as that applying at year 50.

In my opinion, the PPF's Statement of Investment Principles is consistent with this discount rate derivation, despite the fact that the PPF takes some extra investment risk in the expectation of outperformance.

ii) Revaluation rates

I have assumed that the PPF will not exercise its power under paragraph 29 of Schedule 7 of the Pensions Act 2004 to amend the maximum revaluation rate of 5 per cent a year (2.5 per cent a year in respect of compensation which derives from service after 5 April 2009).

Future revaluations of deferred compensation are linked to increases in the CPI. In considering what assumption would be appropriate for future CPI increases, I have noted that at present there is almost no market in CPI swaps or indeed any other instruments from which CPI prices can reasonably be inferred. Such limited current market pricing information as is available from insurance companies would suggest an assumption of CPI increases being 0.4 per cent a year less than RPI increases. I have therefore assumed the same. I have further assumed that the rate of future RPI increases, for the period from the valuation date to normal pension age, is determined from the RPI inflation swap curve (supplied as at 31 March 2014 by Insight Investment).

I am aware that there are other methods of deriving a CPI assumption and these include, for example, deducing a best estimate of the future gap between RPI and CPI from the market implied measure of RPI. I do not feel that this method is consistent with the setting of the other financial assumptions. Should a deeper market develop, I expect that the implied gap between RPI and CPI will further increase; although the actual gap that would apply in these circumstances is very uncertain. I have shown the sensitivity of the balance sheet to there being a gap of 0.9 per cent (compared to 0.4 per cent in the main results). This may be seen in the supplementary report which I have prepared concerning the provisions of the PPF as at 31 March 2014.

The revaluation rate is assumed to be equal to the assumed CPI spot rate except where the spot rate exceeds the maximum revaluation rate. The maximum revaluation rate of 5 per cent a year does not apply at any term, for compensation deriving from service before 6 April 2009. The maximum revaluation rate of 2.5 per cent a year applies for all terms greater than two years, for compensation deriving from service after 5 April 2009.

iii) Pension increase rates

I have assumed that the PPF will not exercise its power under paragraph 29 of Schedule 7 of the Pensions Act 2004 to amend the maximum annual increase rate of 2.5 per cent a year, for compensation accrued after 5 April 1997.

For this compensation increase, therefore, I need an assumption, for each term, for the increase in the CPI capped at 2.5 per cent and with a floor of 0 per cent (call this CPI[0, 2.5 per cent]). If there was a market in CPI[0, 2.5 per cent] inflation swaps then a curve of prices for each term would be derivable directly. However such a market does not exist. Furthermore, the market for the equivalent swaps based on RPI capped at 2.5 per cent, which does exist, is very small and hence the derived curve can be unsatisfactorily affected by a small amount of data. Therefore, this year I have used a CPI[0, 2.5 per cent] curve derived using the SABR model calibrated on market price data from securities that are uncapped and those which are capped at 3 per cent. This curve was supplied by Insight Investment.

For each year beyond 50 years, I have assumed that the pension increase assumption applying is the same as that at term 50.

The table below shows the annualised average term-dependent rates of discount, inflation and increases to pensions in payment as at 31 March 2014 that I have assumed over the given term. The rates are presented as spot rates. Figures shown in brackets are as at 31 March 2013.

Term	Discount rate pa	CPI revaluation rate pa	Post 1997 pension increase rate pa
1	0.551% (0.453%)	2.380% (3.025%)	2.069% (2.262%)
2	0.911% (0.461%)	2.475% (3.069%)	2.062% (2.227%)
3	1.317% (0.525%)	2.578% (3.038%)	2.074% (2.179%)
4	1.654% (0.647%)	2.652% (3.011%)	2.078% (2.146%)
5	1.921% (0.821%)	2.700% (3.006%)	2.069% (2.142%)
10	2.912% (1.918%)	2.890% (3.118%)	2.081% (2.143%)
15	3.396% (2.671%)	3.089% (3.222%)	2.106% (2.149%)
20	3.621% (3.134%)	3.204% (3.280%)	2.125% (2.152%)
30	3.724% (3.545%)	3.265% (3.328%)	2.146% (2.154%)
40	3.613% (3.616%)	3.245% (3.333%)	2.146% (2.151%)
50	3.557% (3.504%)	3.266% (3.361%)	2.154% (2.152%)

Source: Insight Investment

Financial assumptions where individual membership data is not available

It is not possible to use term-dependent rates as we do not have individual member data to be able to project cash flows. We have therefore made assumptions about the following:

- discount rate in deferment net of revaluation increases in deferment – see Annex M1 for a description of these increases
- discount rate in payment for non-increasing compensation for current pensioners
- discount rate in payment for non-increasing compensation for future pensioners
- discount rate in payment for increasing compensation for current pensioners net of increases in payment – see Annex M1 for a description of these increases, and
- discount rate in payment for increasing compensation for future pensioners net of increases in payment – see Annex M1 for a description of these increases.

These financial assumptions have been derived from the term-dependent rates described earlier, ie from those rates used to value the liabilities of transferred schemes where individual membership data is available. This has been done by assuming that cash flows for schemes where individual data is not available will follow the same shape as cash flows for those schemes where individual data is available.

Single rates of discount, inflation and pension increases were determined so that the present values placed on the cash flows for both the pensioners and the deferred pensioners were equal to the present value determined using term-dependent rates. These single rates of discount, inflation and pension increase were then used to determine the net discount rates as set out in the following table. The figures in brackets are those as at 31 March 2013.

Net discount rate	% pa
In deferment for compensation accrued before April 2009	0.5 (0.1)
In deferment for compensation accrued after April 2009	1.1 (0.9)
In payment for non-increasing compensation for current pensioners	3.2 (2.6)
In payment for non-increasing compensation for deferred pensioners	3.6 (3.3)
In payment for increasing compensation for current pensioners	1.1 (0.5)
In payment for increasing compensation for deferred pensioners	1.4 (1.1)

c) Demographic assumptions

i) Mortality

The assumption for mortality is in two parts. The first part is the assumption about baseline mortality. This reflects the rate at which people have been dying in the recent past. The second part of the assumption is an estimate of how mortality rates will change over time. Taken together, these assumptions reflect my best estimate of the mortality that will be experienced by members of the PPF, ie it is my view that the assumption is equally likely to overstate as to understate actual experience.

- **Baseline mortality**

For the valuation as at 31 March 2013, a mortality analyst, Club Vita, provided us with 240 different mortality curves to apply to individual members based on:

- member status, ie deferred pensioner, pensioner, or dependant
- sex
- lifestyle (based on postcode)
- amount of compensation, and
- applicable period (pre-retirement or post-retirement).

Club Vita has updated their experience dataset since the previous valuation and so has provided us with more up-to-date mortality curves to use this year. A total of 239 different mortality curves have been used for the valuation as at 31 March 2014.

These curves have been derived by analysing a large amount of data from Club Vita's members (including the PPF). These curves are based on mortality experienced over the period 2009-2011.

Where individual membership data is not available Club Vita provided us with mortality curves which reflect average mortality across the whole PPF membership. Because the liabilities of these schemes without individual membership data are calculated by rolling forward the results of an earlier section 143 or 179 valuation, it is not possible to use the chosen assumptions precisely. Instead, ratios of annuity values based on male members and female spouses are used in the transformation of the valuation result. This straightforward and tractable approach is fit for purpose since men comprise the majority of pension scheme liabilities.

- **Allowance for changes in mortality over time**

For the valuation as at 31 March 2013, I adopted the CMI-2012 mortality projection model. This model was adopted in its core form, without advanced parameterisation, with a long-term improvement rate of 1.5 per cent a year for both men and women.

I have seen no evidence to suggest that the long-term improvement rate should be changed from my assumption adopted last year. However, since the previous valuation, the CMI has updated the CMI-2012 model to take account of more up-to-date data.

For this valuation, I have therefore adopted the CMI-2013 mortality projection model in its core form, without advanced parameterisation, with a long-term improvement rate of 1.5 per cent a year for both men and women. In standard notation, my assumption for men is denoted CMI_2013_M [1.5 per cent] and for women is denoted CMI_2013_F [1.5 per cent].

It should be recognised that there is a substantial element of subjectivity about mortality assumptions and that different actuaries will come to different conclusions. The appropriate mortality assumption for future valuations will be kept under review and I have shown the sensitivity of the balance sheet to the assumed long-term rate of improvement. This may be seen in the supplementary report which I have prepared concerning the provisions of the PPF as at 31 March 2014.

- **Life expectancies implied by the mortality assumptions**

The following table illustrates the range of cohort life expectancies of pensioners aged 65 on 31 March 2014 and, for non-pensioners, the range of cohort life expectancies once they reach age 65 (based on the mortality assumptions being used for this valuation). The non-pensioners are assumed to be aged 40 currently. Cohort life expectancies are based on the age-specific mortality rates allowing for projected changes in mortality. The figures in brackets show the cohort life expectancies based on the assumptions adopted in my valuation as at 31 March 2013. Without the change made to mortality assumptions, we would see life expectancy increase over time due to an allowance for future mortality improvements.

Men

Membership group	Minimum life expectancy in years	Maximum life expectancy in years	Range of life expectancies, in years, within which 75% of all accrued compensation lies	Average life expectancy in years (weighted by annual compensation)
Pensioners:				
- Members	17.8 (17.7)	23.6 (25.3)	20.1-23.6 (20.3-24.1)	22.1 (22.3)
- Dependants	15.3 (18.2)	21.0 (21.1)	18.9-20.9 (18.2-21.1)	19.7 (20.0)
Non-pensioners:				
- Members	20.9 (20.8)	26.5 (28.0)	23.1-25.9 (23.3-25.6)	24.7 (25.1)
- Dependants	18.3 (21.2)	24.1 (24.1)	22.0-24.1 (21.2-24.1)	22.9 (23.0)

Women

Membership group	Minimum life expectancy in years	Maximum life expectancy in years	Range of life expectancies, in years, within which 75% of all accrued compensation lies	Average life expectancy in years (weighted by annual compensation)
Pensioners:				
- Members	21.4 (21.2)	26.1 (27.4)	23.1-25.5 (23.1-25.1)	24.7 (24.2)
- Dependants	19.7 (19.9)	26.8 (27.8)	22.3-25.3 (22.8-26.5)	23.0 (24.5)
Non-pensioners:				
- Members	24.6 (24.3)	29.1 (30.4)	26.2-28.4 (26.6-27.8)	27.7 (27.3)
- Dependants	23.2 (23.4)	29.5 (30.5)	25.5-27.3 (26.9-27.6)	26.2 (27.5)

Note that the minimum life expectancy is the life expectancy of the member in the particular category given with the shortest life expectancy which is determined by Club Vita using sex, postcode and pension amount. The maximum life expectancy is determined in a corresponding way.

ii) Commutation, early retirement and late retirement

No allowance is made for commutation of compensation, early retirement or late retirement (the latter became an option to members on 30 April 2013). Even though estimated cash flows would be affected by making allowances, nonetheless these member options are roughly cost-neutral in that the value of the liabilities is roughly the same whether or not a member exercises the option. The factors used to determine the amount of compensation given up for cash, early retirement compensation or late retirement compensation are assumed to change over time (being reviewed at least annually) in order to maintain this broadly cost-neutral position.

iii) Proportion married

For pensioners:

Where there is provision for survivor pensions for relevant partners an assumption consistent with 90 per cent (males) or 80 per cent (females) at normal pension age.

Where there is no provision for survivor pensions for relevant partners other than legal spouses an assumption consistent with 80 per cent (males) or 70 per cent (females) at normal pension age.

For deferred pensioners:

Where there is provision for survivor pensions for relevant partners an assumption, at the assumed date of retirement or earlier death, of 90 per cent (males) or 80 per cent (females).

Where there is no provision for survivor pensions for relevant partners other than legal spouses an assumption, at the assumed date of retirement or earlier death, of 80 per cent (males) or 70 per cent (females).

These are standard assumptions normally considered reasonable by actuaries measuring liabilities of UK pension funds.

iv) Age difference between member and dependant

Females assumed to be three years younger than males.

This is a standard assumption normally considered reasonable by actuaries measuring liabilities of UK pension funds and is consistent with the recent experience of the fund.

v) Children's pensions

No specific additional allowance is included for prospective children's pensions. Children's pensions already in payment are assumed to cease in accordance with the compensation entitlement with no allowance for mortality prior to cessation.

vi) Expenses

Certain administration expenses are met from the Pension Protection Fund rather than from the Administration Fund.

An allowance equal to 2.7 per cent of the value of the liabilities in respect of members who transferred into the Pension Protection Fund before 1 April 2014 has been made in respect of the expected future cost of these expenses. This has been derived from a calculation of the present value of the expected future expenses that will be incurred in respect of these members. This calculation was based on the budgeted expenses to be incurred by the PPF in respect of running a notional portfolio in the three years following the valuation date. This compares to an allowance of 2.4 per cent in the previous year's valuation.

vii) GMP equalisation

Schemes for which the Board assumes responsibility on or after 1 June 2013 are required to equalise members' compensation prior to transfer. For these schemes therefore, data provided by Capita includes compensation amounts that have already been adjusted for any inequalities on account of GMP.

For former members of all other schemes where the Board is undertaking work to adjust compensation that is unequal (between men and women) on account of inequalities in GMPs, an allowance for the expected cost has been made.

The cost included is 1.3 per cent of the actuarial liabilities in respect of unequalised transferred schemes. This allowance has increased from that used in the valuation as at 31 March 2013 (0.9 per cent). The change reflects changes to our membership profile as a result of schemes transferring to the PPF since 31 March 2013 but before 1 June 2013. This has resulted in a decrease in the proportion of benefits payable from age 60 which acts to increase the impact of equalisation.

A number of assumptions have gone into the calculation of this provision and some sensitivities to the result have been carried out. By looking at a number of extreme scenarios, I conclude that the impact of equalising compensation for GMPs should be between 0.6 per cent and 4.3 per cent of liabilities and provisions.

Actuary's supplementary report as at 31 March 2014

To: The Board of the Pension Protection Fund
From: Stephen Rice, Chief Actuary to the Board of the Pension Protection Fund
Actuarial liabilities, provisions and contingent liabilities of the Pension Protection Fund as at 31 March 2014

1. Introduction

The Board of the Pension Protection Fund ('the Board') is required by paragraph 22 of schedule 5 to the Pensions Act 2004 to prepare a statement of accounts in respect of each financial year. Each statement of accounts must contain an actuarial valuation of the assets and liabilities of the PPF. This actuarial valuation is set out in my report to the Board dated 9 July 2014.

The statement of accounts also contains provisions and discloses contingent liabilities that require actuarial estimation. This supplementary report contains these estimates. This supplementary report also contains actuarial balance sheets for the PPF showing actuarial liabilities and provisions in comparison with the corresponding assets.

The Board is responsible for the accounting policies, and this report has been prepared within the framework which it has determined. Although I have not been explicitly commissioned to provide this report, I have, nevertheless, prepared it for the Board and I intend my report to assist the Board with the preparation of the annual report and accounts as at 31 March 2014. I therefore see the Board as the user of this report and no other party should rely on any part of this report.

This report does not contain advice on the funding of compensation payable by the PPF. In particular, the results of this valuation are not used in the determination of the levy. All the results in this report are outcomes of a valuation exercise involving the quantification of amounts for recording in the annual report and accounts.

In my view, while the Actuaries' Code issued by the actuarial profession applies to the preparation of this report, there are no professional practice standards which directly apply. I have, however, prepared this report having regard to the principles in three Technical Actuarial Standards, namely TAS R (Reporting Actuarial Information), TAS D (Data) and TAS M (Modelling). This report should be considered alongside my report to the Board dated 9 July 2014. As my reports are prepared solely for the purpose of the PPF Annual Report and Accounts, I have not produced any projections of future accounting positions in this report because the Board does not require them for its accounting disclosures.

2. Provisions

Under IAS 37 of the International Accounting Standards Board a provision should be recognised when:

- an entity has a present obligation (legal or constructive) as a result of a past event
- it is probable that a transfer of economic benefits will be required to settle the obligation, and
- a reliable estimate can be made of the amount of the obligation.

The application of this requirement in the accounting standard to the Board's statement of accounts as at 31 March 2014 is set out in Annex S1.

3. Contingent liabilities

Under IAS 37, a contingent liability is not recognised as a liability because it is either:

- a possible obligation (it has not yet been confirmed whether there is an obligation that could lead to a transfer of economic benefits), or
- a present obligation that does not meet the recognition criteria in IAS 37, ie it is not probable that a transfer of economic benefits will be required to settle the obligation, or a sufficiently reliable estimate of the amount of the obligation cannot be made.

A contingent liability should, however, be disclosed if the possibility of an outflow of economic benefit to settle an obligation is more than remote. The application of this requirement in the accounting standard to the Board's statement of accounts for the financial period ending on 31 March 2014 is set out in Annex S2.

The definitions of contingent liabilities are specified by the Board and I have calculated the values accordingly. However, it should be noted that claims arising after 31 March 2014 could arise from sources other than those described in the definitions for the contingent liabilities. For the avoidance of doubt, the contingent liabilities are not meant to represent the expected claims in the coming year.

4. Data

The data used for this valuation is summarised in Annex S3.

5. Compensation provided by the Pension Protection Fund

The compensation provided by the Pension Protection Fund is summarised in Annex M1 of my report to the Board dated 9 July 2014.

6. Assumptions

The assumptions used to calculate the actuarial liabilities are set out in full in Annex M2 of my report to the Board dated 9 July 2014.

The set of assumptions used in order to calculate the provisions and contingent liabilities as at 31 March 2014 are in most respects the same as those used to calculate the actuarial liabilities. The differences are shown in Annex S4.

I have performed a sensitivity analysis by amending the valuation basis in key areas. The assumptions adopted for the sensitivity analysis are shown in Annex S5.

7. Method to calculate the assets, actuarial liabilities, provisions and contingent liabilities

a) Actuarial liabilities

The method of calculating the actuarial liabilities is set out in my report to the Board dated 9 July 2014.

b) Provisions

To determine whether a provision is required for a scheme it is necessary to determine whether as at the insolvency date the value of the assets was less than the amount of Protected Liabilities (see Annex S1). This is determined in the first instance from consideration of any notice issued in respect of the scheme under section 144 or 145 of the Pensions Act 2004. Where no such notice has been issued, consideration is then given to any internal reports indicating the likely funded status of the scheme at the insolvency date. Finally, for all schemes not already categorised under the two preceding steps, assumptions to determine the funded status at the insolvency date are derived from market conditions as at the insolvency date following the published guidance on undertaking a valuation in accordance with section 179 of the Pensions Act 2004 (version as in force as at the insolvency date). This guidance is available on the Pension Protection Fund web-site **www.pensionprotectionfund.org.uk/TechnicalGuidance/Pages/ValuationGuidance.aspx**

The method of calculating the provisions varied according to the data that the Board was holding about the relevant schemes as at 31 March 2014.

1. Updated asset value information and recent membership data

This information was obtained from certain schemes classified as 'material schemes'. These are schemes which:

(i) satisfy the definition of a provision as set out in Annex S1

(ii) are sufficiently large (broadly those having liabilities of approximately £75 million or more), and

(iii) actually did provide individual membership data and updated asset information.

Some schemes with liabilities less than £75 million were also classified as 'material' schemes where the membership data could conveniently be collected.

For the majority of the material schemes, membership data and updated asset information were provided as at 31 October 2013.

For all material schemes, the asset value at 31 March 2014 was determined by rolling forward the updated asset value and making an adjustment for benefits paid between the effective date of the assets and 31 March 2014.

Similarly as for transferred schemes, initially liabilities were calculated as at 28 February 2014 and based on assumptions derived from market conditions as at 28 February 2014. A loading was subsequently applied to this initial calculation of the liabilities to allow for the change in market conditions as at 31 March 2014 and the change in calculation date to 31 March 2014. The loading was calculated as the percentage difference in the present value of the projected cashflows calculated as at 28 February 2014 using assumptions as at 31 March 2014 and the present value of the projected cashflows as at 28 February 2014 using assumptions as at 28 February 2014, plus an allowance for the time value moving the valuation forward to 31 March 2014.

No allowance was made for membership movements between the effective date of the membership and 31 March 2014 as the majority of data was provided at effective dates close to 31 March 2014.

Material schemes in assessment and schemes which have already transferred to the PPF (excluding those valued by rolling forward a section 143 or 179 valuation) account for 89 per cent of the total liabilities and provisions.

2. A section 143 valuation or a section 179 valuation, but not updated assets and membership data

- If the scheme was to be included in the provisions, the section 143 or 179 valuation was rolled forward to 31 March 2014 on the valuation basis.

The methodology used to roll the s143 / s179 valuation results forward to 31 March 2014, at the same time changing the valuation assumptions to those described in Annex S4, is consistent with that to be applied for the calculation of levy in the financial year 1 April 2014 to 31 March 2015 (ignoring smoothing and stressing of assets and liabilities). The 14/15 methodology is available in the Pension Protection Levy section of the Pension Protection Fund web-site at: **www.pensionprotectionfund.org.uk/DocumentLibrary/Documents/1415_transformation_appendix.pdf**

3. A Minimum Funding Requirement (MFR) valuation, but not updated assets and membership data, nor a section 143 valuation nor a section 179 valuation

The MFR valuation was initially transformed to a section 179 valuation (guidance version G3/A3) at the MFR valuation date using a methodology consistent with that available in the Pension Protection Levy section of the Pension Protection Fund website at: **www.pensionprotectionfund.org.uk/DocumentLibrary/Documents/1415_transformation_appendix.pdf**

In practice very few schemes (less than 0.5 per cent of the liabilities) are assessed based on an MFR valuation and in all cases the transformed section 179 valuation has been used for the purpose of the calculations.

- The resulting section 179 valuation was rolled forward to the insolvency date and used as a proxy for a section 143 valuation to determine whether the scheme was in deficit at the insolvency date and hence whether it should be included in the provisions.
- If the scheme was to be included in the provisions, the resulting section 179 valuation was then rolled forward to 31 March 2014 on the valuation basis using the same methodology.

4. Schemes withdrawn from assessment (as overfunded on a section 143 valuation) and operating or anticipated to operate as a closed fund

For schemes currently operating as a closed fund where it is considered probable that they will ultimately transfer to the PPF, an allowance has been made based on a roll forward of the section 143 assets and liabilities, with an adjustment where necessary to reflect the expectation that such schemes will be close to 100 per cent funded at the point of transfer.

No allowance has been made for schemes that may operate as a closed fund in the future and which may then transfer to the PPF.

5. No updated assets and membership information, nor a section 143 valuation, nor a section 179 valuation, nor a MFR valuation

It was assumed that the scheme was in deficit at the insolvency date. The scheme's provision was estimated as the median provision for schemes where data was available. In total three schemes have been valued in this way.

Where information relating to income and outgo was forthcoming, this information was used to provide a more precise estimate of the scheme assets and liabilities as at 31 March 2014 than was available solely using the roll-forward methodology.

In a similar way as for schemes that have transferred to the PPF, a provision has been included for the cost of equalising compensation that is unequal on account of inequalities in GMPs accrued between 17 May 1990 and 5 April 1997. This provision is to cover the cost of equalisation on the liabilities of schemes which contribute to the provisions.

A single loading was applied to the liabilities forming the provisions, equal to the loading applied to the transferred schemes ie 1.3 per cent of liabilities. This assumption is discussed further in Annex M2.

c) Contingent liabilities

The method adopted for contingent liabilities was identical to that for provisions where the Board was in possession of a section 179 valuation. This was the same method as adopted last year. Additionally a loading for schemes which have not equalised for GMPs was applied to the liabilities forming the contingent liabilities. This loading was equal to the loading applied to the transferred schemes ie 1.3 per cent of liabilities.

8. Results of the calculations

The results of the calculations of the actuarial liabilities, provisions and contingent liabilities are set out in Annex S6. I also show the results as at 31 March 2013 using the assumptions set out in the Report and Accounts as at 31 March 2013.

It is my opinion that the data collection processes and calculation methods described in Section 7 have resulted in calculations that represent a reasonable estimate of provisions and contingent liabilities in aggregate for the Pension Protection Fund. I recognise that the use of summary data and roll-forward methodologies inevitably introduce approximations into the calculations, but I consider they remain appropriate for calculating aggregate provisions and contingent liabilities for the purposes of this supplementary report.

9. Actuarial balance sheets

Annex S7 sets out the actuarial balance sheets for the Pension Protection Fund as at 31 March 2014, including the liabilities of the schemes forming the provisions. For this purpose the liabilities are taken to be:

(a) the present value of the liabilities of the Pension Protection Fund to pay sums or transfer property, as required under section 173(3) of the Pensions Act 2004. This includes the liabilities in respect of compensation to members of schemes for which the Board has assumed responsibility and the cost of equalising compensation for GMPs on these liabilities. The total value is taken as £12,859,400,000, the same figure as was used in my actuarial valuation report of 9 July 2014, and

(b) my estimate of the present value of the liabilities of the schemes forming the provisions, as set out in Annex S6 of this report, which amounts to £6,468,400,000.

Accordingly I have taken the total liabilities including provisions of the Pension Protection Fund as at 31 March 2014 as £19,327,800,000.

In the actuarial balance sheets for the Pension Protection Fund as at 31 March 2014, the assets are:

(a) the value of the Pension Protection Fund assets determined in accordance with regulations 2, 4 and 5 of the Pension Protection Fund (Valuation of the Assets and Liabilities of the Pension Protection Fund) Regulations 2006 (SI 2006/597) - this value is taken as £16,431,400,000, the same figure as was used in my actuarial valuation report of 9 July 2014, and

(b) the sum of the estimated values of the assets in the schemes that generated the provisions described in section 2 of this report, plus any anticipated recoveries estimated on a prudent basis (£400,500,000) - this figure amounts to £5,320,000,000.

Accordingly I have taken the value of the assets of the Pension Protection Fund as at 31 March 2014 as £21,751,400,000.

10. Reconciliation of the change in the funding position

Annex S8 shows a reconciliation of the opening and closing net funding position in the actuarial balance sheet for the Pension Protection Fund, including the schemes that generate the provisions.

Signed: Stephen Rice

Date: 9 July 2014

Name: Stephen Rice, Appointed Actuary

Job Title: Chief Actuary

Qualification: Fellow of the Institute and Faculty of Actuaries

Employer: The Board of the Pension Protection Fund

Annex S1 Provisions in the Statement of Accounts for the financial period ending on 31 March 2014

The Statement of Accounts as at 31 March 2014 contains provisions in respect of eligible schemes as defined in section 126 of the Pensions Act 2004 in relation to which:

- an insolvency event notice under section 120 of the Pensions Act 2004 had been received by the Board from an insolvency practitioner on or before 31 March 2014
- the Board had not stated on or before 31 March 2014 that the insolvency event was not a qualifying insolvency event
- the insolvency date was on or before 31 March 2014
- a withdrawal notice under section 122(2)(b) of the Pensions Act 2004 had not been received on or before 31 March 2014 (and, in the Board's judgement, is unlikely to be received) from the insolvency practitioner
- as at the insolvency date, the value of the assets was, in the Board's judgement, likely to have been less than the amount of the Protected Liabilities as defined in section 131 of the Pensions Act 2004 (determined on the section 179 basis as at the insolvency date), and
- transfer to the PPF had not taken place on or before 31 March 2014.

Schemes which had, in the Board's judgement, a surplus of assets over the value of the protected liabilities at the insolvency date, but which may ultimately enter the PPF have been considered. A provision might be appropriate if there are a significant number of schemes in this position. Based on an analysis of our recent experience, I do not consider that this is so.

In addition, the position of schemes which, as a result of the valuation process set out in Annex S3, have a surplus of assets over the estimated value of the protected liabilities at the valuation date, and therefore contribute a negative amount to the provisions, has also been considered. It might be appropriate to offset some of this negative provision if there are a significant number of schemes in this position because some of these schemes may not ultimately enter the PPF. Again, I do not consider that this is so.

In addition to the above provisions I considered those schemes where a section 143 valuation had been completed by the trustees and this showed an excess of assets over Protected Liabilities. These schemes did not, therefore, transfer into the PPF. There is a possibility that some of them will return to the PPF within six months of the section 143 valuation being signed off (for instance if the trustees obtained a buy-out quote that showed a deficit of assets compared with the protected liabilities). They have, however, been ignored in the provisions calculation because there is uncertainty over whether these schemes will return to the PPF and because they are expected to have a small surplus which is not material.

Schemes which have completed the assessment period and have been operating as a closed fund have also been considered. There is a possibility that some of these schemes will return to the PPF (for instance if the trustees can demonstrate that there are now insufficient assets to provide PPF levels of compensation). It was considered probable that seven of these schemes will ultimately transfer to the PPF and a provision has therefore been included for these cases. Information relating to them is limited and out of date. An allowance has been made for these schemes based on a roll forward of the section 143 assets and liabilities to 31 March 2014, with an adjustment where necessary to reflect the expectation that such schemes will be close to 100 per cent funded at the point of transfer.

Additionally, an allowance for insolvency events that occurred on or before 31 March 2014 that have yet to be reported has also been made. This takes the form of an 'IBNR reserve' (Incurred But Not Reported reserve) which is determined by estimating the number of schemes where a claim has been incurred but not reported. This is calculated as a percentage addition to the number of schemes which have been reported and included as provisions. This percentage has been determined from an analysis of the average time lag between insolvency event occurrence and notification of such an event to the Board (via a section 120 notice) with consideration of the proportion of events resulting in a claim, as shown in the following table:

Number of months between insolvency event and Board receipt of S120 notice	Cumulative proportion of notifications received by each point in time
0	60%
1	89%
2	93%
3	95%
4	96%
5	97%
10	99%
15	99%
16	100%

For this estimated number of schemes where a claim is yet to be reported, the provision is based on the median provision of schemes where a claim has been reported.

Annex S2 Contingent liabilities in the Statement of Accounts for the financial period ending on 31 March 2014

Three types of contingent liabilities are disclosed in footnotes to the statement of accounts. The definitions of the three categories are given below.

1. Type 1 contingent liabilities are in respect of eligible schemes in relation to which:

- an insolvency event notice under section 120 of the Pensions Act 2004 was received by the Board from an insolvency practitioner on or before 31 March 2014
- the Board had stated on or before 31 March 2014 that the insolvency event was NOT a qualifying insolvency event
- in the Board's judgement, a subsequent insolvency event which will be a qualifying insolvency event is likely
- the Board has sufficient data about the scheme to be able to make an estimate of a contingent liability, and
- as at 28 February 2014, the value of the assets was, in the Board's judgement, likely to have been less than the amount of the Protected Liabilities, as defined in section 131 of the Pensions Act 2004.

2. Type 2 contingent liabilities are in respect of eligible schemes in relation to which:

- in the Board's judgement, as at 31 March 2014, no insolvency event has taken place, but the Board is nonetheless expecting to receive an insolvency event notice under section 120 of the Pensions Act 2004 from an insolvency practitioner in the future
- the Board has sufficient data about the scheme to be able to make an estimate of a contingent liability, and
- as at 28 February 2014, the value of the assets was, in the Board's judgement, likely to have been less than the amount of the Protected Liabilities, as defined in section 131 of the Pensions Act 2004.

3. Type 3 contingent liabilities are in respect of schemes where:

- the Dun & Bradstreet failure scores are available to the Board and, based on the data available as at 28 February 2014, the score corresponding to the weighted insolvency probability of the scheme's participating employers was less than 10 (which means the probability of insolvency over the next year was greater than 4.68 per cent)
- the Board has sufficient data about the scheme to be able to make an estimate of a contingent liability, and
- as at 28 February 2014, the value of the assets was, in the Board's judgement, likely to have been less than the amount of the Protected Liabilities as defined in section 131 of the Pensions Act 2004.

Out of a population of around 6,500 schemes considered, 214 had a failure score of less than 10 associated with them. Of these 214 schemes, 147 were in deficit.

There is the potential to have a slight overlap with the IBNR reserve referred to in Annex S1. In the context of the total contingent liabilities I would expect the overlap to be trivial.

Type 3 contingent liabilities exclude any scheme already within the provisions or other categories of contingent liabilities.

It should be noted that in practice the schemes contributing to the Type 3 contingent liabilities often change considerably from one year to the next.

Annex S3 Data

a) Data in respect of PPF members

This data was shown in my report to the Board dated 9 July 2014.

b) Data in respect of provisions and contingent liabilities

There are 158 schemes which contribute to the provisions figure in the statement of accounts for the financial period ending on 31 March 2014 (and a further two schemes included via the IBNR estimate). Liabilities in respect of another 24 schemes have not been recognised, ie not included in the provisions, because the value of their assets was, in the Board's judgement, likely to have exceeded the amount of the protected liabilities at their insolvency date. For Type 1, Type 2 and Type 3 contingent liabilities the recognition test assessment was undertaken at 28 February 2014 since a qualifying insolvency event had not occurred.

A database is maintained for schemes forming the provisions. Data used to identify these schemes is obtained from information sent to the PPF on an employer's insolvency. This data is updated when new information arises. For instance, when a claim is rejected by the PPF, the database is updated to reflect this information and the scheme is no longer included in the provisions calculations.

For material schemes (broadly schemes with liabilities in excess of £75 million), the PPF actively seeks from trustees up-to-date individual member data and current asset values. For all other schemes the latest section 143 or 179 valuation provided for levy purposes is used to assess asset and liability values. The section 179 valuation used will be that held on Exchange at the 31 March preceding insolvency.

For contingent liabilities we make use of information that the PPF has gathered from sources such as Dun & Bradstreet, negotiations with companies and information submitted by the Pensions Regulator. The data used to place a value on these liabilities is taken from the information we hold for levy invoicing purposes. A database is not maintained over time for these schemes. A separate identification of contingent liabilities is made each year for the annual report and accounts and the latest data available is used in the valuation.

The numbers of schemes contributing to the various types of provisions and contingent liabilities are given in the table below. Figures in brackets relate to the total number of schemes considered for inclusion, ie it includes schemes where the value of their assets was, in the Board's judgement, likely to have exceeded the amount of the protected liabilities at their insolvency date for provisions and the calculation date for contingent liabilities. In all of the figures we have sought to recognise all segregated parts of schemes as separate schemes. This is the same treatment as was adopted at 31 March 2013.

Liability		Number of schemes recognised	Number of pensioners *	Number of deferred pensioners *
Provision	2014	158 (182 in total)	42,748	48,261
	2013	187 (223 in total)	41,070	69,617
Provision - IBNR	2014	2 (2 in total)	n/a	n/a
	2013	4 (4 in total)	n/a	n/a
Type 1 contingent liability	2014	0 (0 in total)	0	0
	2013	0 (0 in total)	0	0
Type 2 contingent liability	2014	5 (7 in total)	1,076	1,083
	2013	17 (17 in total)	5,234	8,648
Type 3 contingent liability	2014	147 (214 in total)	16,258	36,120
	2013	152 (187 in total)	39,532	70,361

* Data in respect of recognised schemes only

The valuation of the liabilities of material schemes forming the provisions has been undertaken using individual membership data. The valuation of the liabilities of all other schemes forming the provisions and contingent liabilities has not been undertaken using member-by-member data as we do not hold this data. Instead the historic valuation results available for the schemes have been used and rolled forward. As such the valuation will not be as accurate as one undertaken using individual membership data for each scheme. This approach, while perhaps inappropriate for valuation purposes for some schemes on an individual basis, in aggregate is, in my opinion, acceptable for estimating provisions and contingent liabilities. Generally there is no reason to doubt the quality of the information provided within a particular scheme's valuation report. It is important, however, to note that any errors contained within the original scheme valuation will carry through to this valuation.

Because of the lack of uniformity of data summaries in individual schemes' valuation reports, it has not been possible to provide any other summary data about schemes in the various liability categories.

As we do not hold member-by-member data for all the schemes forming the provisions, we have not been able to indicate the incidence of cash flows relating to the schemes forming the provisions. However, when collecting data for material schemes we obtained information relating to the individual pensioners in payment and deferred pensioners and this indicated that the shape of the cash flows for schemes forming the provisions is not dissimilar to that for transferred schemes.

Annex S4 Assumptions

All assumptions will be either the same as, or derived in the same way as, those derived for the valuation as at 31 March 2013, unless stated otherwise.

a) Actuarial liabilities

The assumptions adopted were described in my report to the Board dated 9 July 2014.

b) Basis adopted for Provisions and Contingent Liabilities

1. Discount, inflation and pension increase rates

For the provisions represented by material schemes we have used the term-dependent rates as described in Annex M2. For the provisions represented by non-material schemes and contingent liabilities it is not possible to use term-dependent rates as we do not have individual member data to be able to project cash flows. We have therefore made assumptions about the following:

- discount rate in deferment (net of revaluation increases in deferment – see Annex M1 for a description of these increases)
- discount rate in payment for non-increasing compensation for current pensioners
- discount rate in payment for non-increasing compensation for future pensioners
- discount rate in payment for increasing compensation for current pensioners (net of increases in payment – see Annex M1 for a description of these increases), and
- discount rate in payment for increasing compensation for future pensioners (net of increases in payment – see Annex M1 for a description of these increases).

These financial assumptions have been derived from the term-dependent rates shown in Annex M2. This has been done by assuming that cash flows for provisions will follow the same shape as cash flows for the Pension Protection Fund liabilities.

Single rates of discount, inflation and pension increases were determined so that the present values placed on each of the cash flows for pensioners and deferred pensioners corresponding to the Pension Protection Fund liabilites were equal to the present value determined using term-dependent rates. These single rates of discount, inflation and pension increase were then used to determine the net discount rates as set out in the following table. The figures in brackets are those as at 31 March 2013.

Net discount rate	% pa
In deferment for compensation accrued before April 2009	0.5 (0.1)
In deferment for compensation accrued after April 2009	1.1 (0.9)
In payment for non-increasing compensation for current pensioners	3.2 (2.6)
In payment for non-increasing compensation for deferred pensioners	3.6 (3.3)
In payment for increasing compensation for current pensioners	1.1 (0.5)
In payment for increasing compensation for deferred pensioners	1.4 (1.1)

2. Mortality

My previous report used base member mortality of S1PMA (men) and S1PFA (women), with base dependant mortality of S1DFA (female dependants) and S1PMA (male dependants). All these baseline tables were issued by the CMI. For this year I have adopted base mortality assumptions provided by the mortality analyst Club Vita. I now consider, following recent analysis, that the new assumptions provide greater consistency between the liabilities forming the provisions and those in respect of transferred schemes, as well as ensuring a more bespoke assessment of mortality reflective of the actual members and schemes forming the provisions.

For material schemes, Club Vita provided us with 239 different mortality curves to apply to individual members based on:

- member status, ie deferred pensioner, pensioner, or dependant
- sex
- lifestyle (based on postcode)
- amount of compensation, and
- applicable period (pre-retirement or post-retirement) .

This is the same approach used for schemes which had transferred to the PPF on or before 31 March 2014, as described in Annex M2 of my report to the Board dated 9 July 2014.

For non-material schemes (where individual membership data is not available), Club Vita provided us with mortality curves which reflect average mortality across the whole membership. There were ten average mortality curves, which varied according to membership status (pensioner member / pensioner contingent life / deferred member / deferred contingent life), sex and applicable period (pre / post retirement).

There is no evidence to suggest that my assumption for long-term mortality improvement used in my previous report should change, other than to adopt the latest update to the CMI model to allow for more recent data. I have therefore adopted the CMI-2013 mortality projection model in its core form, without advanced parameterisation, with a long-term improvement rate of 1.5 per cent a year for both men and women for this valuation, ie CMI_2013_M [1.5 per cent] for men and CMI_2013_F [1.5 per cent] for women. These future projections have been issued by the CMI.

Because the liabilities of non-material schemes' provisions and contingent liabilities are calculated by rolling forward the results of an earlier valuation, it is not possible to use the chosen assumptions precisely. Instead, all members of non-material schemes are assumed to be male and their dependants assumed to be female. Ratios of annuity values using male mortality are therefore used in the transformation of the valuation result. This straightforward and tractable approach is fit for purpose since men comprise the majority of pension scheme liabilities.

3. Proportion Married

80 per cent of members are assumed to be married or to have a relevant partner. Again, because the liabilities (other than for material schemes) are calculated by rolling forward the results of an earlier valuation it is not possible to use sex-specific proportions married.

4. Age difference between member and dependant

Females assumed to be three years younger than males.

5. Children's pensions

No specific allowance.

6. Expenses

Allowance has been made for expenses incurred by the trustees prior to transfer into the Pension Protection Fund. I have assumed that these will be the same as the wind-up expenses calculated in accordance with the section 179 methodology. Schemes are assumed to be, on average, midway through the assessment period. So allowance is made only for 50 per cent of the full section 179 wind up expense cost; and, for schemes where the asset value is based on a roll forward of a valuation that pre-dates the insolvency, 50 per cent of the full section 179 wind up cost is deducted from the asset value. In addition allowance has been made for costs incurred by the Pension Protection Fund of transitioning members across to the Pension Protection Fund. This has been calculated based on our current estimate of these costs. Allowance has also been made for certain expenses incurred after transfer to the Pension Protection Fund, in respect of schemes which are likely to transfer to the Pension Protection Fund (see Annex M2 of my report to the Board dated 9 July 2014 for an explanation of the expenses that are to be met from the Fund after a scheme transfers to the PPF). The same allowance is used as for transferred schemes (2.7 per cent). Expressed as a percentage of the provisions, the aggregate allowance for expenses incurred during the assessment process, during transition to the PPF and then after transfer, is 3.6 per cent. The equivalent figure from last year is 3.9 per cent.

Annex S5 Sensitivity analysis

Results have been calculated on the basis described in Annex S4. However, the future is never certain, and a wide range of factors could affect the future finances of the PPF. It is possible to capture some measure of how different possible outcomes for these factors affect the PPF by showing different valuation results using different values for the assumptions set out in Annexes M2 and S4. For instance, if recipients of PPF compensation were to live longer than expected, the cash flows out of the PPF would rise, other things being equal. The risks that such a change pose to the PPF can be investigated by showing the results of the PPF valuation modified to reflect different assumptions about mortality rates and longevity.

I have considered nine scenarios covering the main uncertainties.

Scenario 1: Assumptions based purely on the swaps curve at 31 March 2014 but with a deduction of 15 basis points at each term.

Scenario 2: Assumptions based purely on the gilts curve at 31 March 2014.

Under scenarios 1 and 2 the effect of the basis change is on the actuarial liabilities and on the liabilities forming the provisions.

Scenario 3: Nominal yields are assumed to increase by 0.5 per cent per annum.

Scenario 4: Inflation is assumed to increase by 0.5 per cent per annum at each term.

In scenarios 3 and 4, I have looked at the effect on the invested assets and assets in respect of schemes forming the provisions as well as the effect on the liabilities. The result of a decrease in the above yields of the same magnitude has not been shown. This is because the PPF aims to adopt a fully hedged position with regards to interest and inflation. As a result, our funding position is relatively insensitive to changes in these rates. This is illustrated by the results of scenario 3 and 4 shown in Annex S7.

Scenario 5: Increases in the CPI are assumed to be 0.9 per cent lower than increases in the RPI, ie assuming that a market had developed in CPI and that it was priced at 0.9 per cent below RPI.

Scenario 6: The probability of death in each year of age is assumed to be 90 per cent of that used in the main basis.

Scenario 7: The long-term projection of mortality improvements is assumed to be increased by 0.5 per cent to 2.0 per cent a year.

Scenario 8: The value of non-LDI type assets is assumed to decrease by 10 per cent at 31 March 2014. The asset value would be expected to change by a similar order of magnitude in the opposite direction if instead these assets are assumed to increase by 10 per cent.

Scenario 9: Assumptions based on section 143 entry valuation basis (effective from 1 April 2011).

A summary of the assumptions is shown overleaf:

	Main Basis	Scenario 1	Scenario 2	Scenario 3	Scenario 4	Scenario 5	Scenario 6	Scenario 7	Scenario 8	Scenario 9
Discount rate in deferment for compensation accrued before April 2009	0.51%	0.12%	0.51%	1.00%	-0.02%	1.00%	0.51%	0.51%	0.51%	(0.33)%
Discount rate in deferment for compensation accrued after April 2009	1.09%	0.68%	1.09%	1.58%	1.09%	1.13%	1.09%	1.09%	1.09%	0.78%
Discount rate in payment for non-increasing compensation for current pensioners	3.20%	2.92%	3.19%	3.67%	3.20%	3.20%	3.20%	3.20%	3.20%	3.60%
Discount rate in payment for non-increasing compensation for future pensioners	3.57%	3.18%	3.57%	4.07%	3.57%	3.57%	3.57%	3.57%	3.57%	3.60%
Discount rate in payment for increasing compensation for current pensioners	1.06%	0.79%	1.05%	1.52%	0.96%	1.18%	1.06%	1.06%	1.06%	1.10%
Discount rate in payment for increasing compensation for future pensioners	1.38%	0.99%	1.38%	1.86%	1.30%	1.46%	1.38%	1.38%	1.38%	1.10%
Non LDI assets	Market value	Market value	Market value	Market value	Market value	Market value	Market value	Market value	Fall by 10%	Market value
Proportion married	As in Annexes S4 and M2	As in Annexes S4 and M2	As in Annexes S4 and M2	As in Annexes S4 and M2	As in Annexes S4 and M2	As in Annexes S4 and M2	As in Annexes S4 and M2	As in Annexes S4 and M2	As in Annexes S4 and M2	As in s143 guidance (B5)
Mortality	As in Annexes S4 and M2	As in Annexes S4 and M2	As in Annexes S4 and M2	As in Annexes S4 and M2	As in Annexes S4 and M2	As in Annexes S4 and M2	As in Annexes S4 and M2 but with 10% reduction in death rates	As in Annexes S4 and M2 but with 2.0% long-term mortality improve-ment	As in Annexes S4 and M2	As in s143 guidance (B5)

Annex S6 Calculation results

a) Calculation of actuarial liabilities for members who have transferred into the Pension Protection Fund

The actuarial liabilities in respect of former members of schemes for which the Board assumed responsibility on or before 31 March 2014 plus the cost of equalising compensation for GMPs on those liabilities plus a sum required to meet the remaining liabilities under Regulation 3 of the Pension Protection Fund (Valuation of the Assets and Liabilities of the Pension Protection Fund) Regulations 2006 amount to £12,859,400,000.

b) Calculation of provisions

160 schemes were included in the provisions in the statement of accounts for the financial period ending on 31 March 2014. The table below shows the estimated assets held at 31 March 2014 in the 160 schemes forming the provisions. It also shows the outstanding anticipated recoveries, the resulting total assets and estimated funding position in respect of those 160 schemes. A comparison is shown with the equivalent figures from the 2012/13 Annual Report and Accounts using the assumptions described in that report):

	31 March 2014 £000s	31 March 2013 £000s
Assets excluding anticipated recoveries	4,919,500	4,640,100
Anticipated recoveries	400,500	379,000
Total assets	**5,320,000**	**5,019,400**
Provisions	**6,468,400**	**6,518,500**
Excess of liabilities over assets	**1,148,400**	**1,499,100**

The liabilities recognised as provisions are the present value of the liabilities calculated at each valuation date on the relevant basis.

The provision assets have increased by £301 million and this can be reconciled as follows:

	£m	£m
Assets as at 31 March 2013		**5,019**
Change in schemes' assets due to benefits paid out	(214)	
Actuarial and assumed investment returns	37	
Data changes (including updated valuation information and changes in recoveries)	(76)	
Claims no longer considered probable (exits or schemes estimated to be in surplus at their assessment date)	(81)	
Claims now considered probable (includes schemes that were not considered probable in 2013 but which subsequently transferred to the PPF)	96	
New schemes entering assessment	1,904	
Schemes accepted into the PPF (assets as at transfer date)	(1,334)	
Change in allowance for expenses incurred to date whilst in assessment period	(31)	
Assets as at 31 March 2014		**5,320**

The provision liabilities have decreased by £51 million and this can be reconciled as follows:

	£m	£m
Provision liabilities at 31 March 2013		**6,519**
Change in schemes' liabilities due to benefits paid out	(214)	
Effect of passage of time on discounting	73	
Data changes (including updated valuation information)	(123)	
Claims no longer considered probable (exits or schemes estimated to be in surplus at their assessment date)	(111)	
Claims now considered probable (includes schemes that were not considered probable in 2013 but which subsequently transferred to the PPF)	107	
New schemes entering assessment	2,703	
Schemes accepted into the PPF (liabilities as at transfer date)	(2,002)	
Change in schemes' liabilities on account of change in allowance for cost of GMP equalisation	25	
Change in schemes' liabilities on account of change in allowance for expenses over the assessment period and on-going administration post transfer	(18)	
Change in schemes' liabilities on account of change in mortality assumptions	(168)	
Change in schemes' liabilities on account of change in financial assumptions	(323)	
Provision liabilities at 31 March 2014		**6,468**

c) Calculation of contingent liabilities

The estimated amounts for the various types of contingent liabilities were as follows (a comparison is shown with the equivalent figures from the 2012/13 Annual Report and Accounts under the Main Assumptions basis as described in that report):

Type of contingent liability	Estimated scheme funding positions as at 31 March 2014 £000s	Estimated scheme funding positions as at 31 March 2013 £000s
1	0	0
2	39,300	547,400
3	737,200	2,129,000
Total	**776,500**	**2,676,400**

The liabilities recognised as contingent liabilities are the present value of the deficit calculated at each valuation date on the relevant basis.

Shown below are the total assets and total liabilities that correspond to the above deficits (contingent liabilities). A comparison is shown with the equivalent figures from the 2012/13 Annual Report and Accounts under the Main Assumptions basis.

Type of contingent liability	31 March 2014 Assets £000s	31 March 2014 Liabilities £000s	31 March 2013 Assets £000s	31 March 2013 Liabilities £000s
1	0	0	0	0
2	92,500	131,800	947,300	1,494,700
3	3,743,700	4,480,900	7,763,500	9,892,500
Total	**3,836,200**	**4,612,700**	**8,710,800**	**11,387,200**

At this stage it is too early to assess whether any recovery is available for any type of contingent liability so none has been assumed.

Annex S7 Actuarial balance sheet

On the main 31 March 2014 basis the Pension Protection Fund actuarial balance sheet is as follows:

Assets	£000s	Liabilities	£000s
The value of the Pension Protection Fund assets determined in accordance with the Pension Protection Fund (Valuation of the Assets and Liabilities of the Pension Protection Fund) Regulations 2006	16,431,400*	The present value of the liabilities of the Pension Protection Fund to pay sums or transfer property as required under section 173(3) of the Pensions Act 2004	12,859,400*
The sum of the estimated values of the assets in the schemes that generated the provisions, plus any anticipated recoveries**	5,320,000***	The present value of the liabilities of the schemes forming the provisions **	6,468,400
Total assets	**21,751,400**	**Total liabilities**	**19,327,800**
Excess of assets over liabilities			**2,423,600**
Funding Ratio (assets / liabilities)			**112.5%**

* Inclusive of £3,650,000 in respect of AVC assets that match AVC liabilities yet to be discharged
** Inclusive of an allowance for IBNR (scheme assets of £10,845,000 and liabilities of £12,074,000)
*** Inclusive of anticipated recoveries of £400,500,000

I have also calculated the actuarial liabilities and the liabilities of the schemes forming the provisions using the bases set out in Annex S5.

The balance sheet on the various scenarios (as described in the section on sensitivity analysis in Annex S5) is as follows. None of these scenarios should be interpreted as upper or lower bounds of the range of reasonable estimates which might be made.

	Main Basis	Scenario 1 2014 Swaps less 15 basis points	Scenario 2 2014 gilts	Scenario 3 Nominal plus 0.5%	Scenario 4 Inflation plus 0.5%	Scenario 5 CPI is 0.9% lower than RPI	Scenario 6 10% reduction in death rates	Scenario 7 Long-term mortality improvement plus 0.5%	Scenario 8 Non LDI assets fall by 10%	Scenario 9 S143 Basis
Assets	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
The value of the Pension Protection Fund assets	16,431	16,431	16,431	14,862	17,068	16,431	16,431	16,431	15,331	16,431
The values of the assets in the schemes that generated the provisions	5,320	5,320	5,320	5,099	5,458	5,320	5,320	5,320	5,046	5,320
Total assets	**21,751**	**21,751**	**21,751**	**19,961**	**22,526**	**21,751**	**21,751**	**21,751**	**20,376**	**21,751**
Liabilities										
The present value of the liabilities of the Pension Protection Fund	12,859	13,744	12,930	11,863	13,381	12,495	13,304	13,250	12,859	14,161
The present value of the liabilities of the schemes forming the provisions	6,469	6,911	6,478	5,947	6,713	6,250	6,660	6,660	6,469	7,086
Total liabilities	**19,328**	**20,655**	**19,408**	**17,810**	**20,094**	**18,745**	**19,964**	**19,910**	**19,328**	**21,247**
Excess of assets over liabilities	**2,423**	**1,096**	**2,343**	**2,151**	**2,432**	**3,006**	**1,787**	**1,841**	**1,048**	**504**
Funding Ratio (assets / liabilities)	**113%**	**105%**	**112%**	**112%**	**112%**	**116%**	**109%**	**109%**	**105%**	**102%**

Annex S8 Comparison with the funding position as at 31 March 2013

Under IAS 37 a reconciliation is required of the opening and closing net funding position on the actuarial balance sheet, including schemes that generate the provisions. I show this as a table below:

Reconciling item	**£m**
Excess of assets over liabilities on the actuarial balance sheet at 31 March 2013	1,752
Change in actuarial liabilities (this is further broken down in section 7 of my report on the actuarial valuation of the Pension Protection Fund)	(1,032)
Change in liabilities for schemes forming the Provisions (this is further broken down in Annex S6)	51
Change in Pension Protection Fund assets (this is further broken down in section 6 of my report on the actuarial valuation of the Pension Protection Fund)	1,352
Change in assets for schemes forming the provisions (this is further broken down in Annex S6)	301
Excess of assets over liabilities on the actuarial balance sheet at 31 March 2014	**2,424**

Commonly abbreviated terms

ALCO – Asset and Liability Committee

AVC – additional voluntary contribution

CETV – cash equivalent transfer value

CMI – Continuous Mortality Investigation

CPI – Consumer Prices Index

DWP – Department for Work and Pensions

FAS – Financial Assistance Scheme

FCF – Fraud Compensation Fund

FReM – Government Financial Reporting Manual

GIA – grant-in-aid

GMP – Guaranteed Minimum Pension

GTAA – Global Tactical Asset Allocation

IAS – International Accounting Standard

IBNR – incurred but not reported

IFRS – International Financial Reporting Standard

ISDA – International Swaps and Derivatives Association

ISO – International Organization for Standardization

IT - information technology

LDI – liability driven investment

Libor - London Interbank Offered Rate

MFR – Minimum Funding Requirement

ORSA – Own Risks and Solvency Assessment

PPF – Pension Protection Fund

RPI – Retail Prices Index

SIA - schemes in assessment

SIP - Statement of Investment Principles

TAS – Technical Actuarial Standard

Pension
Protection
Fund

Renaissance, 12 Dingwall Road,
Croydon CR0 2NA

T: 0845 600 2541
F: 020 8633 4903

www.pensionprotectionfund.org.uk

ISBN 978-1-4741-0857-7

9 781474 108577

140040 - Designed by Croydon Design