Pension Protection Fund

The 2019/20 Pension Protection Levy Consultation Document

September 2018

Foreword

This consultation invites comments on the basis on which we should charge our levy for 2019/20, the second year of a three year period where we aim to maintain stable rules.

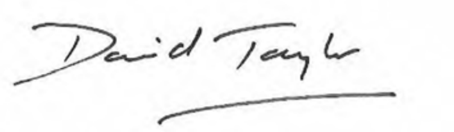
The last few months have seen a challenging environment for the Fund. Last year saw the highest level of claims in our history and claims could well be higher again over the next twelve months. However, while we continue to face significant risks and uncertainty, the PPF's funding position is strong and we're on track to achieve our long-term funding objective. We've therefore been able to leave the levy parameters unchanged for 2019/20 and expect to collect close to £500 million (nearly 10 per cent lower than the 2018/19 levy estimate). We continue to monitor the situation closely and, as we've always made clear, will adjust the levy in future years if necessary to respond to circumstances.

In terms of the rules for calculating individual levies, we have reviewed the changes we made for 2018/19, and concluded that these are operating well. We are, therefore, only proposing some very limited adjustments. However, we are consulting on a new rule to allow us to charge a risk reflective levy for commercial consolidation vehicles.

We are clear that, while consolidation may bring real benefits, a consolidation vehicle may pose different risks from those of 'conventional' schemes. That means it will be essential that there is a robust regulatory framework to protect scheme and PPF members as well as levy payers. We are engaging with the Department for Work and Pensions (DWP) on their work in this area. It will also be essential that we can charge consolidators an appropriate, risk reflective levy not least to ensure there is no cross-subsidy from 'conventional' schemes.

As the new regulatory regime develops, we would expect it to inform our levy methodology, but a consolidation vehicle may well emerge before regulation is in place. We are therefore proposing a new levy methodology now to ensure we can charge an appropriate levy. We will then develop the rule as necessary in future years to reflect wider developments in this area. We would emphasise that although we are putting in place a levy charging methodology, that this cannot be a substitute for an appropriate regulatory regime – and would not protect the Fund, or members, in the absence of one.

Looking to the future, we are exploring how we can better support schemes to plan levy payments. We are also reminding schemes with type A or B contingent assets containing a fixed cap that these will need to be re-executed if they are to be recognised for 2019/20. This is confirmation of the policy that was announced last year to ensure all such agreements are fit for purpose.



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1. Introduction and Executive Summary

1.1. Introduction

1.1.1. This consultation document and the accompanying draft Levy Rules, set out the basis on which we intend to charge the Pension Protection Levy for the 2019/20 Levy Year and seek stakeholder input on those proposals. Alongside our proposals we are also publishing the amount we expect to collect – the Levy Estimate.

1.2. Overview

1.2.1. A key feature of our levy Framework is that we aim to maintain stability in the way in which the levy is calculated, as far as that is possible, over a three year period (or triennium). This objective covers both the parameters for the levy (asset stresses, scaling factor and the like), and rules more broadly. 2019/20 is the mid-year of the third levy triennium (2018/19 to 2020/21).

1.2.2. Although we aim to have this multi-year focus, the formal setting of our Levy Rules and publication of the Levy Estimate for the year remains an annual process (as required by the Pensions Act 2004). We have considered the impact on our funding position of a record year for claims and significant expected claims in the near future, but have concluded that we should not make a change in the parameters we use to set the Levy Estimate – so our 2019/20 Levy Estimate is based upon the third triennium parameters we set last year.

1.2.3. We have also reviewed the performance of our insolvency risk model – in the light of changes made in 2018/19 and the operation of other policy changes. We concluded that these are operating well and there is no need to make changes, beyond very minor clarifications. However we have concluded that there is a case for updating the Levy Rules relating to schemes without a substantive sponsor, and for introducing additional Levy Rules to calculate a levy for consolidation vehicles.

1.2.4. The draft Determination under section 175(5) of the Pensions Act 2004 is published alongside this consultation document. These Levy Rules express the Board's policy in legal form and govern the basis on which we calculate the levy.

1.2.5. The consultation closes at 5pm on 25 October 2018. We will publish our consultation conclusions before the end of 2018.

1.3. Insolvency Risk Measurement

1.3.1. For the third triennium most scheme employers remain assessed for insolvency risk by the PPF-specific model, a bespoke methodology developed with Experian. We jointly rebuilt five scorecards within the PPF-specific model and recalibrated those unaltered taking account of additional insolvency experience since they were developed. To improve assessment for some of the biggest employers in our universe we also introduced the use of credit ratings and the S&P credit model for regulated financial institutions.

1.3.2. For 2019/20 our focus is considering whether the changes introduced in 2018/19 have had the expected results. Our early monitoring does not indicate any areas of concern (though there have been a limited number of insolvencies in the last year against which we can test the model's scores) and we remain satisfied with its performance. We do not therefore, propose any significant changes to the PPF-specific model or the other new scoring methods we introduced.

1.3.3. In our 2018/19 Policy Statement we said that we would consider whether the S&P credit model should be extended to score other regulated entities. Following a review we have concluded that we should not do so for the reasons set out in Section 4.

1.4. The Levy Estimate

Factors influencing the Levy Estimate

1.4.1. In addition to publishing the rules, we are required to produce a Levy Estimate before we set the rules for each year. We set a Levy Estimate of £550 million for 2018/19.

1.4.2. We have indicated since 2012/13 that we would only propose to intervene to control the change in levy within a triennium in limited circumstances. Although our triennial approach seeks to maintain stability as far as possible within each three-year period it allows us to change the rules if that is deemed appropriate in the circumstances – in particular if there would otherwise be a change in levy of more than 25 per cent or if our funding is adversely challenged to a material degree.

1.4.3. Our 2017/18 accounts reflect a year in which we had a record level of claims and we also reported contingent liabilities in relation to expected insolvencies, of around £1.4 billion. This suggests that claims in 2018/19 are likely to remain at a high level – and could exceed those in 2017/18. We have therefore considered whether this significant increase in claims justified making a change for 2019/20 but concluded it did not - as our funding position remains robust and our probability of meeting our long term funding objective remains high. However, if the level of claims continues to be high, we may need to give careful thought to the position for next year's rules.

1.4.4. We have made assumptions about a number of factors where the actual data we use in the 2019/20 levy invoicing will not be known until the end of March 2019 at the earliest. This has been informed by past experience and soundings we have taken from several consultancies about whether we should expect different outcomes in 2019/20.

1.4.5. This has led to a Levy Estimate of £500 million for 2019/20. The Board is confirming that it does not intend to adjust the Levy Scaling Factor or scheme-based levy multiplier for 2019/20.

1.5. Consolidation Vehicles

1.5.1. The Government's White Paper on DB pensions indicated an intention to bring forward policies to support and encourage the consolidation of DB schemes. This is expected to include bringing forward proposals for a regulatory regime for commercial consolidators – with a further consultation on this expected later this year. We encourage stakeholders, in addition to commenting on this consultation, to engage with the DWP consultation on the regulatory framework when it is launched.

1.5.2. We are also aware of proposals for consolidation vehicles emerging within the existing regulatory framework – in respect of which we may need to charge a levy in 2019/20.

1.5.3. As we have indicated previously (for example in evidence to the Work and Pensions Select Committee), the risks posed by consolidation vehicles differ from those of other schemes – and so we are strongly supportive of an enhanced regulatory regime. In view of the possibility that an arrangement may come in to place which is eligible for PPF protection for Levy Year 2019/20, we have developed our Levy Rules to provide an appropriate basis for calculating a levy.

1.5.4. We propose to base a levy rule for consolidators on our existing methodology for schemes without a substantive sponsor (SWOSS) adjusted to ensure it reflects the particular risks posed by consolidators. We are clear however that the critical long term goal is securing control over risks through effective regulation and that much uncertainty remains over the shape and structure of these vehicles. This means our approach to the levy will need to develop in coming years, and we have flagged some possible areas in section 3 of this document.

1.5.5. Proposed developments from our existing SWOSS methodology are intended to ensure the levy charged to consolidators is in line with commercial pricing and to ensure there is no cross subsidy from existing levy payers. We are proposing to:

- Increase the levy for a consolidator in the (perhaps unlikely) event that there is no requirement for the arrangement to wind up if funding falls below a minimum threshold.
- Implement asset stresses and an end of year recalculation mechanism to reflect respectively the risks of profit extraction and new transfers in.
- Put in place appropriately prudent assumptions for consolidators if they do not provide key information (particularly valuations) at the required frequency.

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

1.6. Contingent Asset Recertification

1.6.1. Section 5 sets out our proposals for contingent asset recognition in 2019/20. In particular it explains the circumstances in which schemes need to re-execute contingent assets using the new standard form agreements and certify them by 31 March 2019 (hard copy documents by 5pm on 29 March 2019), if they are to be recognised in the levy.

1.6.2. The approach we are taking was first set out in our Policy Statement of December 2017 and we contacted schemes with contingent assets in June 2018 to encourage early action on this.

1.6.3. Affected schemes are those with Type A and B contingent assets that include a fixed sum maximum amount element and that have not yet re-executed the agreement on the January 2018 forms.

1.7. Other Third Triennium Changes

1.7.1. We have reviewed how the changes we introduced for the third triennium are working, and are proposing small tweaks to the guidance on certifying deficit reductions and block transfers.

1.8. Longer Term Changes

1.8.1. The next point at which we expect to consider substantive policy changes in our approach will be for our fourth triennium which begins in Levy Year 2021/22. Consideration of potential issues for the fourth triennium is expected to commence in the next year and we would be interested in any initial views on areas we should consider. Our existing contract for insolvency risk services (with Experian) ends in 2020/21 and we have begun the compulsory tendering process for the period starting from 2021/22, which will coincide with the new triennium.

1.8.2. We also ask, in section 6.4, for views on how we might improve our customer service, including payment services. This will inform the ongoing development of our services over fourth triennium. We would in particular value views on potential improvements that would be valuable to levy payers to help them plan for and pay the levy.

2. The Levy Estimate and Parameters

2.1. Introduction - Third Triennium

2.1.1. Our levy Framework seeks to provide stability of methodology through establishing rules that remain substantially unchanged for a three year period (“triennium”). 2019/20 is the second year of our third triennium.

2.1.2. We indicated it was our intention for the Levy Scaling Factor and scheme-based levy multiplier that are used in the levy calculation to remain constant for the triennium unless this would result in setting a Levy Estimate outside an acceptable range (see paragraph 2.2.1 below).

2.2. The Triggers for Changing Parameters

2.2.1. Our levy Framework sets a formula for the levy, including the associated levy parameters. Other than in specific limited circumstances, we intend to keep the levy parameters unchanged for the current triennium, ie, up to and including 2020/21. The circumstances we specified for changing the parameters are where their retention would cause:

- the Levy Estimate to exceed the levy ceiling, or,
- the scheme-based Levy Estimate to exceed the statutory maximum of 20 per cent of the total Levy Estimate, or,
- the Levy Estimate to vary by more than 25 per cent from the preceding year’s estimate; in 2018/19 our published estimate was £550 million.

2.2.2. We have previously explained that we would also have to consider a revision of the parameters should exceptionally adverse scheme risk and economic conditions challenge our funding position to an unacceptable degree. We reserve the right to vary the parameters should such extreme circumstances materialise.

2.2.3. Our 2017/18 accounts reflect a year in which we had a record level of claims (driven by a small number of very large claims) and we also reported contingent liabilities in relation to expected insolvencies, of around £1.4 billion. This suggests that claims in 2018/19 are likely to remain at a high level – and could exceed those in 2017/18. We have therefore considered whether this significant increase in claims justified making a change for 2019/20. We concluded it did not - as our funding position remains robust and our probability of meeting our long term funding objective remains high. However, if the level of claims continues to be high, we may need to give careful thought to the position for next year’s rules.

2.2.4. Over 2019/20 we expect to see an overall improvement in underfunding risk compared to 2018/19 as employers pay deficit-reduction contributions and scheme funding levels improve, though this will be partially offset by the impact of recent market conditions (in particular, low gilt yields) on smoothed funding levels (our levy formula smooths funding over a five year period to reduce volatility).

2.2.5. Notwithstanding that we may see some further large claims, we expect to see a modest improvement in insolvency scores on average, which reduces the Levy Estimate. Using these and other assumptions (summarised below) together with unchanged levy parameters produces a Levy Estimate of £500 million for 2019/20. This is a nine per cent decrease compared to the Levy Estimate of £550 million for 2018/19.

2.3. Our Assumptions for the 2019/20 Levy Estimate

2.3.1. Assumptions are needed because we produce the estimate well in advance of having all the data that will be used in levy invoice calculations. Much of the data we use will be provided up to the end of March 2019 (scheme return data, contingent asset certifications/re-certifications and monthly insolvency risk scores); other information (about DRCs and block transfers) can be provided up to the end of April and June 2019.

2.3.2. In setting our assumptions we have looked at trends in recent years, market data and also sought the views of a number of firms of actuaries on expected scheme behaviour in the run up to 2019/20. It is always difficult to judge the setting of individual assumptions, particularly those which depend on scheme behaviour, but taken together we consider that these assumptions provide a balanced view of the factors that may affect the total levy.

2.3.3. Existing scheme data, together with our assumptions, is used to estimate the impact on levy invoices of various factors, the most material of which being scheme funding and insolvency risk. Our assumptions for each of these areas are set out in more detail below.

Scheme Funding

2.3.4. Each year the funding risk of schemes will change as a result of market movements, new accrual and payments to reduce deficits (certified as DRCs). The assumptions for market movements - which are used when we roll forward and smooth scheme return data for invoicing - are particularly critical as these include the gilt yields used to discount liabilities, as well as the indices used to value assets.

2.3.5. To reduce volatility in levies arising from market movements, the calculation of the underfunding risk smooths market conditions over a period of five years up to the Measurement Time, which for 2019/20 is 31 March 2019. As a result assumptions are required regarding market yields and indices over the period from the date on which the Levy Estimate is calculated up to 31 March 2019.

2.3.6. We derive our future yield and index values from the Economic Scenario Generator (ESG). This is a stochastic tool provided by a third-party (Moody's Analytics) and adapted for use by the PPF to generate a range of economic scenarios over a number of years, for example as an input to our Funding Strategy.

2.3.7. In addition, we also reflect our experience that when new valuations are submitted, that these are more likely to show improved funding (relative to the previous valuation transformed to the new date), than to show a fall in funding.

2.3.8. We have assumed schemes that certified Deficit Reduction Contributions (DRCs) for 2018/19 will continue to do so at a similar level for 2019/20, following our policy change last year to simplify calculation and certification requirements.

Changes in Insolvency Risk

2.3.9. We need to make assumptions about how the Pension Protection Scores that we use to measure insolvency risk will change over the year to March 2019 and indeed afterwards due to any appeals. To do this we have looked at the most recent year's data showing how scores have changed and used this, along with market information, to create the assumption.

Contingent Assets

2.3.10. We introduced various changes to the Contingent Asset (CA) certification regime for 2018/19, some of which were expected to increase certifications and others to reduce certifications. Our experience in 2018/19 has been that the number of new CAs is slightly lower than 2017/18 but that they have a significantly larger levy impact due to a handful of new CAs resulting in large levy reduction. Non-recertifications of CAs in 2018/19 had an even lower impact than in the previous year. We have assumed that the impact of new CA certifications and non-recertifications for 2019/20 will be similar to the observed impact for 2018/19.

2.4. Our Levy Parameters and Levy Estimate for 2019/20

2.4.1. After taking account of our assumptions and the levy Framework we are setting the Levy Estimate for 2019/20 at £500 million, with the Levy Scaling Factor and scheme-based levy multiplier remaining at 0.48 and 0.000021 respectively.

2.4.2. We have reviewed the other levy parameters (for example, the risk-based levy cap, investment risk stress factors and levy rates) as we do annually. We have concluded that these remain appropriate, in the context of our desire to maintain stable rules for the third levy triennium. We are not therefore proposing any changes to the levy parameters. We are also retaining the existing threshold for requiring a bespoke investment risk stress test – of £1.5 billion s179 liabilities. The exception to this is that we expect any scheme which is a SWOSS or commercial consolidation vehicle, (as defined in rules C5 and C6 of the Levy Rules) to carry out a bespoke test regardless of size.

2.4.3. Stakeholders may be aware that a new version of the s179 valuation assumptions guidance – A9 - has been released for consultation. The consultation period closes on 21 September and it is envisaged that the finalised guidance will come into force before the start of Levy Year 2019/20.

2.4.4. Consistent with our normal policy of keeping the output basis the same throughout a triennium, we will retain version A8 as the output basis for Levy Year 2019/20. Any s179 valuations prepared under version A9 and submitted by the Measurement Time for 2019/20 will be transformed back to the A8 assumptions.

2.4.5. As A9 is still subject to consultation, we have not documented the corresponding assumptions in the draft Transformation Appendix. Paragraph 4.3.3 of the draft Transformation Appendix covers the situation where a submitted s179 valuation has been prepared on a later version of the assumptions guidance than A8, and provides for the use of the appropriate assumptions in determining the s179 input basis.

2.4.6. The Court of Justice of the European Union recently ruled that PPF members should receive at least 50 per cent of the value of their accrued old age pension in the event of employer insolvency. The vast majority of members already receive compensation in excess of 50 per cent of their accrued old age benefits and we expect the number of members affected by this ruling to be very small. We will be considering the ruling carefully, including what action we can take prior to legislative change, and/or the conclusion of UK court proceedings. Once the implementation approach is clear we will consider whether any changes to s179 valuation guidance is needed and consult appropriately.

3. Scheme Consolidation and Schemes Without a Substantive Sponsor

3.1. Context

3.1.1. The Government's White Paper on DB Pensions (published on 19 March 2018) set out its three priorities for DB schemes, one of which is supporting and encouraging consolidation. There are a range of measures the Government is proposing, including accreditation for DB master trusts, but perhaps the most significant is the Government's plan to enable the introduction of so-called "superfund" consolidators – where commercial entities set up vehicles designed to bring together and manage the liabilities of previously unassociated schemes with third party investment included to provide additional funding.

3.1.2. It is envisaged that these schemes will be operated as occupational pension schemes – with a company established purely to fulfil the legal obligation to have an employer. As a result, such consolidators would be eligible for PPF protection.

3.1.3. Consolidators are expected to be structured with buffer funds, held outside the scheme (and, therefore, generally not scheme assets), which may become available to the scheme in specified circumstances – or alternately will provide a return to the investors supplying funds to the vehicle.

3.1.4. This fixed buffer replaces the covenant of the employer whose scheme has transferred members to the consolidator so that the success or otherwise of the consolidation vehicle – and the payment of member benefits - will depend upon managing the assets of the fund and the buffer fund.

3.1.5. Our expectation is that the Government will bring forward detailed proposals, including on a regulatory approach, later this year. An enhanced regulatory regime is required because the nature of the risks involved for consolidators, and the appropriate approaches to managing those risks, are different to those for schemes with a substantive sponsor. In particular, because of the lack of a substantive sponsor, a failure of the investment strategy of the consolidator would trigger a claim on the PPF – which ultimately is a cost to all "conventional" schemes paying a PPF Levy.

3.1.6. Our views on these risks and our priorities for the new legislative regime were set out in our letter to the Work and Pensions Select Committee[1]. In summary we consider the new regime must:

- Limit the impact of consolidator failure by imposing wind up triggers that require a consolidator to cease operating as soon as the risk of a claim on the PPF becomes too high.

[1] The letter (together with our oral evidence and an earlier note) are available on the website of the Work and Pensions Select Committee. The letter is at: http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/work-and-pensions-committee/defined-benefit-pensions-white-paper/written/85745.html

- Ensure any consolidator is financially robust by requiring them to conduct modelling that shows they can – for example – pay benefits in full in the required percentage of scenarios.
- Ensure transfers provide greater security for members, by requiring a robust assessment that transfers increase security over that offered by the scheme with its current employer(s).

3.1.7. In terms of the absence of a continuing substantive employer and the reliance upon investment returns to secure benefits, these schemes will resemble the schemes without a substantive employer (SWOSS) for which we developed a levy rule in 2017/18[2].

3.1.8. We propose to base our levy for commercial consolidators on the methodology we established for SWOSS schemes. The nature of the risk a consolidator would pose to us is broadly similar in nature to that posed by a SWOSS – in that it is the risk of investment failure and there is no substantive sponsor. Our SWOSS methodology uses the Black-Scholes formula – a well-known approach to calculating option pricing. We use it for calculating a price (ie, levy) for underwriting the risk of a scheme's funding position falling to the extent that the scheme would be expected to claim on us with a deficit that would cause a cost to us. We do this by setting the "strike price" for the option calculation slightly below 100 per cent on a section 179 basis. The levy charged under this methodology is highly sensitive to the scheme's funding position and level of investment risk.

3.1.9. However, although the fundamental nature of the risk posed to us by consolidators and SWOSS are comparable, there are clearly some critical differences including the potential for a scheme to grow in size during the Levy Year, and the possibility of profit withdrawal and concerns over scale. On the other hand, consolidators may also offer security not available in a SWOSS, through the establishment of buffer funds.

3.1.10. We have therefore considered whether these differences in risk (and other issues) require changes to the current SWOSS methodology either now or at a later date. In doing so, we are mindful that there remain considerable unknowns (e.g. on the final structure of any propositions that do emerge and the shape of the new regulatory regime). This means the levy rule we establish for 2019/20 will almost certainly need to be developed further in subsequent years as matters become clearer. Our focus for 2019/20 is establishing a workable rule but also to flag areas we may look to incorporate in future.

3.1.11. Ensuring that a special rule fully prices the risks of a consolidation vehicle is critical so there is no in-built expectation of other levy payers having to subsidise consolidators. This is particularly important, as other levy payers do not have a choice about whether to pay the levy and it extends the risks that

[2] The levy rule was developed to reflect the potential emergence of a SWOSS and was used for levy years 2017/18 and 2018/19. More detail on the development and rule in our special consultation of February 2017 can be found at: https://www.pensionprotectionfund.org.uk/DocumentLibrary/Documents/SPV%20condoc%20and%20appendix%2020022017%20FINAL%20w%20Cover.pdf

they are covering. We have also aimed for transparency, setting out the basis on which we have developed our proposal. This is designed to ensure that the likely cost of the levy can be factored in to thinking on the design of consolidators, and so we are not placing undue barriers in the way of those seeking to develop propositions which could be of genuine benefit.

3.2. How Will We Define a Consolidation Vehicle?

3.2.1. In order to specify which schemes will fall within scope of this appendix we have drafted an “entry rule”. This is difficult to draft in the absence of regulations, or indeed examples of consolidators already in operation (and from our initial contact with parties considering the establishments of commercial consolidation vehicles it is clear that propositions may differ in material ways). The approach we have taken, is to set a rule at C6.1 of the main Levy Rules so that for levy purposes a commercial consolidator is:

> …a Scheme that the Board has confirmed as meeting both of the following criteria at any time:
>
> (a) It is a Scheme where one of the purposes of its establishment and/or the nature of the ongoing operation of the Scheme and/or of its surrounding arrangements is, in the opinion of the Board, to effect consolidation of Schemes’ liabilities and/or to enable a return to be payable otherwise than to Members; and
>
> (b) It is a Scheme in respect of which the nature of the scheme and/or the risk posed to the Board is such that in the opinion of the Board it is more appropriate for the Levy Rules applicable to (1)(a) above to apply than the Levy Rules that would otherwise apply.

The scheme would then be charged a levy based on rules set out in the new Commercial Consolidator Appendix

3.2.2. Our intent in drafting the entry rule is that Part (a) of the rule might be expected to identify consolidation vehicles but may also capture some schemes that are beyond our intended scope. Part (b) therefore restricts the scope to any arrangement which in terms of the risks posed or nature of activity looks as if it should come within our definition allowing us to exclude arrangements such as DB master trusts where the link with the original employer is not broken.

3.2.3. It will be seen that the entry rule has a “subjective” component in that it is framed as indicating that a scheme is a consolidation vehicle if it appears to be one in the opinion of the Board, having regard to features expected to occur in a consolidator. We think this provides more flexibility than a wholly “objective” rule – so we can avoid including schemes we wouldn’t wish to, or excluding a scheme that is in economic substance operating as a consolidator. This is particularly important in the initial stages of policy development and commercial innovation.

3.2.4. The rule considers two features of potential vehicles: having a purpose for the scheme, or surrounding arrangements, to consolidate liabilities, and generating a return other than for members. We would interpret the former as covering both a scheme that pools liabilities in a single fund, and one where the liabilities of each precursor scheme are held in a separate section (since "the surrounding arrangements" would still be shared). In addition, the rule allows schemes to fall within scope due to earning a return other than for members – which allows both for designs that envisage immediate returns for investors and those where returns follow the securing of liabilities.

3.2.5. The rule identifying a commercial consolidator can be applied in respect of any point in time when a consolidator is identified (e.g. if a scheme were initially being invoiced as a "standard" scheme before it became clear it was a consolidation vehicle).

3.2.6. We expect that the Department for Work and Pensions will in due course legislate to put in place an authorisation regime for schemes operating as consolidation vehicles. It is likely we could use this, once operational, to identify schemes to which the consolidator Levy Rules should apply. In the meantime, we believe it will be possible to identify consolidators as it is in the nature of the propositions that there is extensive communication about the establishment of, and transfers in to, a consolidation vehicle.

Consultation question: do you think the proposed definition will adequately identify those schemes that ought to be levied as a consolidation vehicle?

3.3. The Black-Scholes Formula

3.3.1. Our starting point for the levy is the existing SWOSS methodology based on the Black-Scholes formula (used in option pricing). This is because the risk presented by consolidators is essentially the same as that posed by other SWOSSs: the risk of scheme funding falling sufficiently to trigger a claim on the PPF.

3.3.2. The use of Black-Scholes effectively provides a commercial price for that risk by treating a claim as a put option and establishing how much - in financial markets - it would cost to underwrite the risk of scheme funding falling below the strike price.

3.3.3. In the current methodology we have set the strike price as the cost to us of paying compensation to members (calculated on our accounting basis). However, we do not consider we can simply "pick up and drop" the existing methodology. In order to meet our objectives we propose to make changes to the SWOSS methodology to:

- Reflect the different nature of risk posed by consolidators. This includes the risk presented by profit extraction and writing new business, but also the risk of consolidators operating without a wind up trigger.
- Address limitations within the SWOSS methodology, in order to prevent any undercharging or cross subsidy from standard schemes. These changes would apply to other SWOSS schemes as well as consolidators.

3.4. Reflecting Differences in Risk From Other SWOSS Schemes: Profit and in-year transfers

3.4.1. A key difference in risk between consolidators and other SWOSSs is that some consolidation structures may provide for profit extraction while member liabilities remain with the consolidator and also for the possibility of growth in liabilities as the consolidator writes new business. The current levy methodology calculates the levy for a year using data collected at the end of the preceding financial year. This means that if profit is extracted over the course of the year or if the consolidator writes new business the levy would not take this into account but they *could* have a significant impact on the risk the PPF is exposed to.

3.4.2. In order to allow for potential profit extraction we intend to use the Black-Scholes formula to assess the potential for funding to exceed the level at which extraction can occur – in the same way we already use it to measure the potential for a claim. We would then remove the expected profit at the start of the year from the assets used in the levy calculation. Where profit extraction isn't possible either because profits are only taken after buyout of liabilities, or due to the timing of the arrangements for profit extraction (e.g. so that information supplied to us is net of any profit that can be taken for the following year) then no adjustment would be needed.

3.4.3. We do not think it is possible to anticipate the effect of transfers in to a consolidator over the year – the impact of transfers obviously depends on the relative size of the consolidator and would need to reflect the possibility of varying levels of new business growth in the early years (much as the level of buyouts varies from year to year). An upfront adjustment would also present challenges in regard to any levy already paid by transferring schemes (leading to double-charging).

3.4.4. We therefore propose to introduce an end year reconciliation process – recalculating the levy to allow for the effect of any new transfers that occurred over the course of the year. The impact of transfers would be backdated to the point they occurred. We propose to construct this rule as a discretionary power for the Board allowing us to choose not to act if the impact of changes is insufficiently significant.

3.4.5. Recognising that the transferring scheme may have paid a levy, we would only expect to charge a consolidator any extra levy that would be due as a consequence of a transfer (i.e. only that part of any increase in excess of any levy already paid by the transferring scheme in respect of those liabilities).

Inability to impose requirements – wind up triggers and provision of information

3.4.6. A further distinction between consolidators and other SWOSS schemes is that our SWOSS methodology assumes we and TPR can - as a condition of approving the RAA or other transaction - require certain conditions be met. Chief amongst these is the imposition of a wind up trigger that automatically triggers an insolvency and assessment period if scheme funding falls below the trigger point.

3.4.7. Our engagement with DWP suggests that such protection can be expected to feature in the regulatory framework they envisage, and we anticipate those setting up vehicles prior to the introduction of a framework will choose to include a wind-up trigger for good governance and /or to protect members from losing benefits. However, the possibility of a consolidator coming into being without a wind up trigger – or one which is not framed in a way that will definitely trigger an assessment period if funding falls below the trigger - presents a significant risk since the funding position of the consolidator could deteriorate significantly before claiming on us. As such, we think it is right that this increased risk is reflected in the levy. Doing so should also provide a strong incentive for consolidators to put a wind up trigger in place.

3.4.8. There are two potential solutions to achieve this. Our preferred option is to achieve this by adjusting the strike price used in the Black-Scholes formula. Currently the strike price is the cost of meeting compensation payments to scheme members calculated on an adjusted s179 basis (in line with our accounting basis). For consolidators with no suitable wind up trigger in place we propose to raise the strike price to the level of funding below which the most likely outcome is that the consolidator will fail. We expect this to be at least 100 per cent of s179 liabilities[3]. This will mean that the levy is accurately pricing the risk of the consolidator making a claim on the PPF, with a significant increase in levies as funding approaches unsustainable levels.

3.4.9. There is a case for the higher strike price to be used in all circumstances. However, we think where wind up triggers are present it is reasonable to charge a lower levy as they provide a safeguard for us.

3.4.10. An alternative mechanism would be to charge a different, and substantially higher scheme-based levy to a consolidator that has not identified to us that it has a wind-up trigger e.g. 0.25 per cent of assets.

3.4.11. Using a scheme-based approach would provide a more consistent incentive – but would increase costs for a well-funded scheme without a trigger. By comparison, the proposed method only imposes a substantial cost if scheme funding falls.

3.4.12. A further concern is that without the ability to impose governance arrangements, we cannot require consolidators to provide us with the information we need to calculate the levy (legislation only requires provision of valuation information every three years). To ensure we get the necessary information we propose to build appropriately prudent assumptions into the rules –that can be expected not to underestimate the risk - and which will apply unless information is provided to the level and frequency we need (most critically the provision of annual valuations). For example, we will be seeking information about expected increases in liabilities for existing members (sometimes referred to as “scheme drift”) and in the absence of information will assume a level of increase at the top end of current experience of 2 per cent increase in liabilities a year (this and other assumptions are shown as

[3] Our draft rules do not currently make explicit provision for a consolidator with a suitable wind-up trigger. Our intention is to use the same strike price as would apply for a SWOSS, and Rule C6.7 in the Levy Rules allows this. We may extend the rules to make this more explicit in December.

default values in the appendix, which might be expected to reduce if information is supplied).

3.4.13. This is similar to the approach we have used elsewhere – the Levy Rules already include provisions to apply prudent assumptions (known as the poor data methodology) following block transfers of liabilities. Information on transfers over the year could be required - if not provided voluntarily - under our s191 powers or taken from annual accounts.

Consultation question: to incentivise consolidators to have appropriate wind-up-triggers, do you think it better to adjust the strike price or set a higher scheme-based levy?

Consultation question: do you agree that we should make prudent assumptions in the event information is not forthcoming?

The presence of a buffer fund

3.4.14. One aspect of the consolidation proposals that may offer an enhanced level of security, relative to SWOSS schemes, is the presence of a buffer fund. Because this is not a scheme asset, this would not automatically be taken account of in assessing the underfunding risk of the scheme.

3.4.15. Provided that a buffer fund can be demonstrated to offer sufficient guarantees of availability (etc) we think it is reasonable for it to be recognised in the levy. Accordingly we will recognise buffer funds where they meet our existing requirements for contingent assets (we expect type B contingent assets to be the most appropriate) or for ABCs. We have considered whether there should be additional flexibility to recognise structures outside our existing framework of risk reduction measures – but do not think this proportionate (in terms of the number of parties involved) or appropriate (in providing more flexibility to consolidators than to conventional schemes).

Consultation question: do you have comments on the approach proposed in relation to buffer funds?

3.5. Addressing Limitations in the SWOSS Methodology

3.5.1. We also intend to strengthen the SWOSS methodology to reduce any risk the levy might charge too little for the risk. These changes would apply both to SWOSSs and commercial consolidators.

3.5.2. Firstly, we propose to build in an allowance for expected growth in PPF liabilities for existing members over the 12 month period to 31 March 2020. This reflects that a wind-up could occur at any point in the year – and that liabilities might have grown by that time. We will do this by applying prudent assumptions to liabilities but also allow consolidators or SWOSSs/consolidators to provide their own calculations if they wish to do so.

3.5.3. Secondly, we will implement an iterative approach to the calculation of the levy. The current SWOSS levy undercharges because it does not reflect the impact of the levy itself on scheme assets. For consolidators and SWOSSs we propose to address this by introducing an iterative methodology - effectively calculating the levy, deducting the charge from assets, and then recalculating repeatedly until the level of increase between calculation steps becomes negligible.

3.5.4. This is likely to have little impact on levies for schemes that are well funded, but would become material if funding weakened. Indeed, at a point close to the strike price, calculating a levy through an iterative process means the levy simply increases more with each iteration (without ever converging on a finite figure). In essence this indicates that no levy adequately reflects the risk of the scheme, if that levy comes from existing resources (either resources of the scheme or the associated buffer fund). In such a situation the levy would be limited to the assets of the scheme. In practice we consider it extremely unlikely that such a situation would arise as a wind-up trigger would be set at a higher level than this.

3.5.5. In addition, we intend on making a small adjustment to our formula which reflects a consultation response to our original consultation on the SWOSS levy: using an exchange pricing variant of the Black-Scholes formula (referred to as the Garman-Kohlhagen formula). This means that the formula models liabilities and assets separately, rather than modelling funding. We agree this is a more theoretically appropriate approach, but practical effects are very limited, and so we delayed until wider changes were being made.

3.5.6. A characteristic of the current methodology, which may result in underestimation of risk, is that it contains an assumption of assets outperforming liabilities over the year. Moving to the Garman-Kohlhagen version of the formula has broadly the same effect as setting the risk-free rate to zero (since each of the assets and liabilities are modelled with the same risk free rate) – which would otherwise have required an adjustment to the existing formula.

3.5.7. As noted in section 3.1, the strike price that is used to calculate the levy for SWOSS and consolidation schemes, is adjusted from the section 179 basis, using factors to reflect the potential cost to the PPF of providing compensation for pensioner and deferred members (based on our accounting basis). The factors we use will be updated for any changes in s179 assumptions (we are currently consulting on a new version of s179 assumptions[4]) and our valuation basis[5] in time for publication of the rules in December.

Consultation question: do you have comments on the adjustments we are making to the SWOSS methodology (and which will also apply in the commercial consolidator methodology)?

3.6. Information We Will Need From Consolidation Vehicles

3.6.1. As noted above, in order to calculate the proposed levy accurately it will be desirable to have a range of information from the scheme on an annual basis.

[4] https://www.pensionprotectionfund.org.uk/DocumentLibrary/Documents/S143%20condoc%20Aug%202018.pdf

[5] Our valuation basis is described in Annex M2 of our annual report and accounts (page 143 on) - https://www.pensionprotectionfund.org.uk/DocumentLibrary/Documents/Annual%20Report%202017-2018.pdf

While we recognise that such information would be disproportionate for the average scheme, our expectation is that these schemes will employ extremely sophisticated information systems. This will allow them, for example to track member liabilities on an individual basis, rendering the information we are seeking easier to produce. Similarly we would expect a consolidator to have a sophisticated investment strategy, and be able to procure the bespoke investment risk calculations we expect from schemes with s179 liabilities above £1.5 billion.

3.6.2. A table setting out the expected information requirements can be found in Appendix B.

Consultation question: are the information requirements that we propose ones that consolidators can reasonably comply with?

Consultation question: if not are there simplifying assumptions that we should use?

3.7. Impact of the Consolidator Rules

3.7.1. As with other schemes without a substantive sponsor, the levy calculation would be very sensitive to changes in the funding level. We have set out an example calculation for the levy for differing levels of funding – based on a relatively low risk investment strategy and a substantially lower risk strategy at Appendix A. It is notable that, at the levels of funding we understand those promoting commercial propositions intend to operate at, that the levy would be relatively low. However, if the funding position falls then the levy would rise rapidly.

3.8. Future Development of a Consolidator Levy

3.8.1. The development of consolidation models may have significance for the risk the PPF faces, if they become widespread, since their risks can be expected to be more positively correlated than for conventional schemes. This may be the case both because investment strategies are likely to be similar and because in the absence of substantive sponsors the timing of failures is likely to be correlated.

3.8.2. For 2019/20 it is not anticipated that consolidation schemes will have significant scale and so we have not addressed this risk in the levy.

3.8.3. If in future the model were to become more widespread, the charging mechanism might need to be adjusted to address this risk - for example by including a component linked to concentration risk.

3.8.4. In addition, the emergence of consolidators is also likely to add to the costs of PPF operation – though to an extent as yet unclear. There may be a case for charging a different scheme-based levy to reflect costs.

4. The Measurement of Insolvency Risk

4.1. Introduction

4.1.1. We introduced several changes for the start of the third triennium in Levy Year 2018/19.

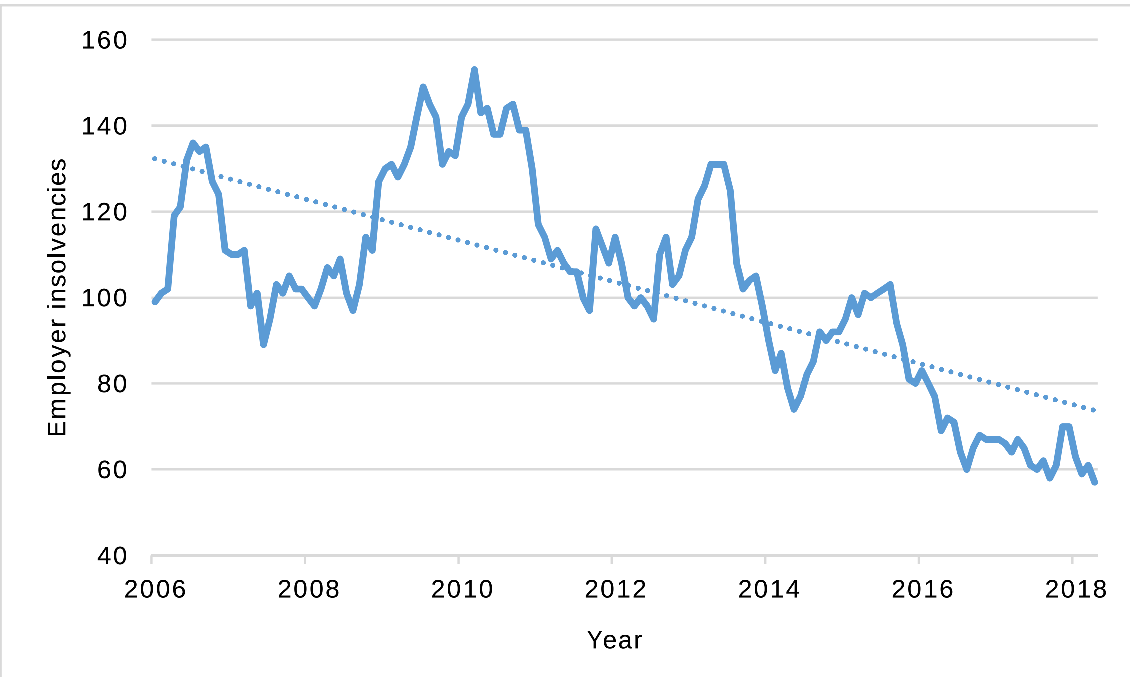
4.1.2. We made changes to the PPF-specific model creating or re-building five scorecards and re-calibrating three scorecards.

4.1.3. We decided to use public credit ratings where employers have them and they meet the criteria specified and to use the S&P credit model for regulated banks, building societies and insurance providers.

4.1.4. We identified a small group of employers who, if they met certain objective criteria could apply to be confirmed as special category employers. Broadly speaking, these are employers set up by legislation or governmental bodies whose legal structure and the nature of their accounts is such that the other available categories don't reflect the risk they pose to us.

4.1.5. In the third triennium consultation document we commented that the level of insolvency risk has been broadly steady between March 2016 and March 2017 having fallen substantially over the preceding years. Chart 1 shows that the rolling annual number of S120 filings[6] since the inception of the PPF has decreased until 2016, after which insolvency experience has been broadly flat.

Chart 1: Trend in insolvencies of employers (based on s120 filings)



[6] The PPF must be notified when an insolvency event occurs (such as the appointment of administrators) at a company that sponsors a pension scheme. The insolvency practitioner looking after the affairs of the company will notify us by sending a Section 120 Notice.

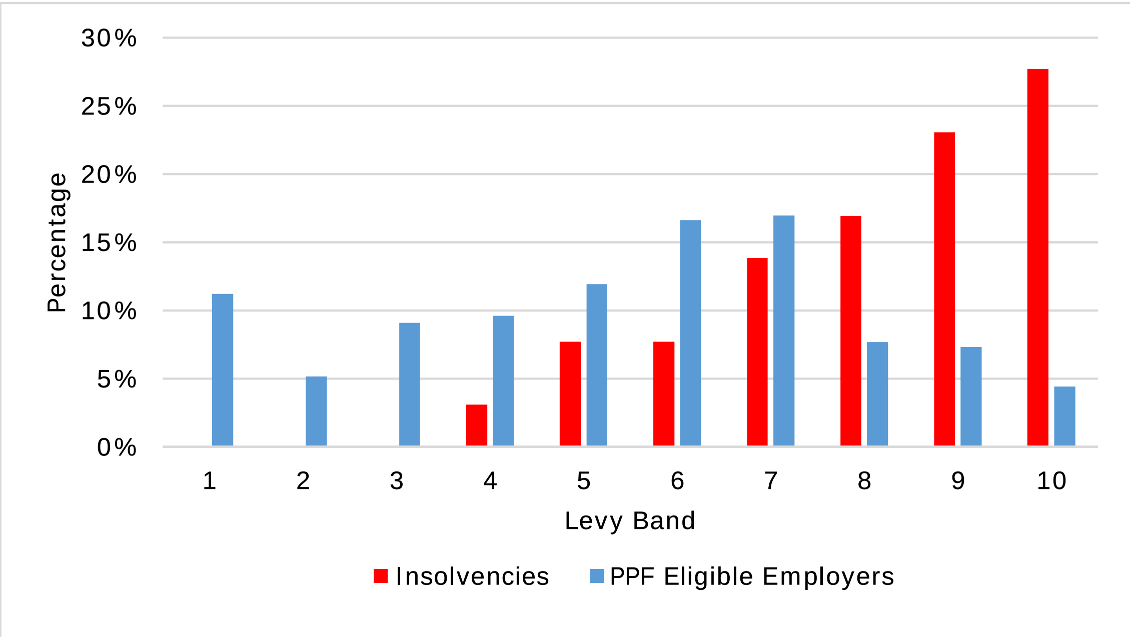
4.2. PPF Specific Model – Overall Assessment

4.2.1. The 2018/19 Levy Year gives the first opportunity to test the performance (ie the predictive power) of the PPF-specific insolvency risk model using the insolvency experience since the changes were made. Although the additional data is limited we are satisfied that the PPF's methodology for insolvency risk scoring remains fit for purpose.

4.2.2. There were 70 insolvencies within the PPF universe of employers over the period April 2017 to March 2018, representing 0.67 per cent of the population[7].

4.2.3. We found that none of the insolvencies were for employers scored using either public credit ratings or the S&P credit model[8]. Chart 2 below shows the distribution of employers across levy bands and the levy band that the employers that became insolvent were in, in April 2017. Employers are placed into one of ten bands with Band 1 assessed as the lowest risk and Band 10 the highest.

Chart 2: Distribution of insolvencies by levy band compared with the distribution of sponsors of eligible DB Schemes



4.2.4. Most employer insolvencies were for employers scored in the highest risk levy bands (bands 7 -10, representing our highest risks) and only one was in levy bands 1 to 4 (those associated with an "investment grade" quality).

[7] This is only modestly lower than the 0.72 per cent predicted using the model

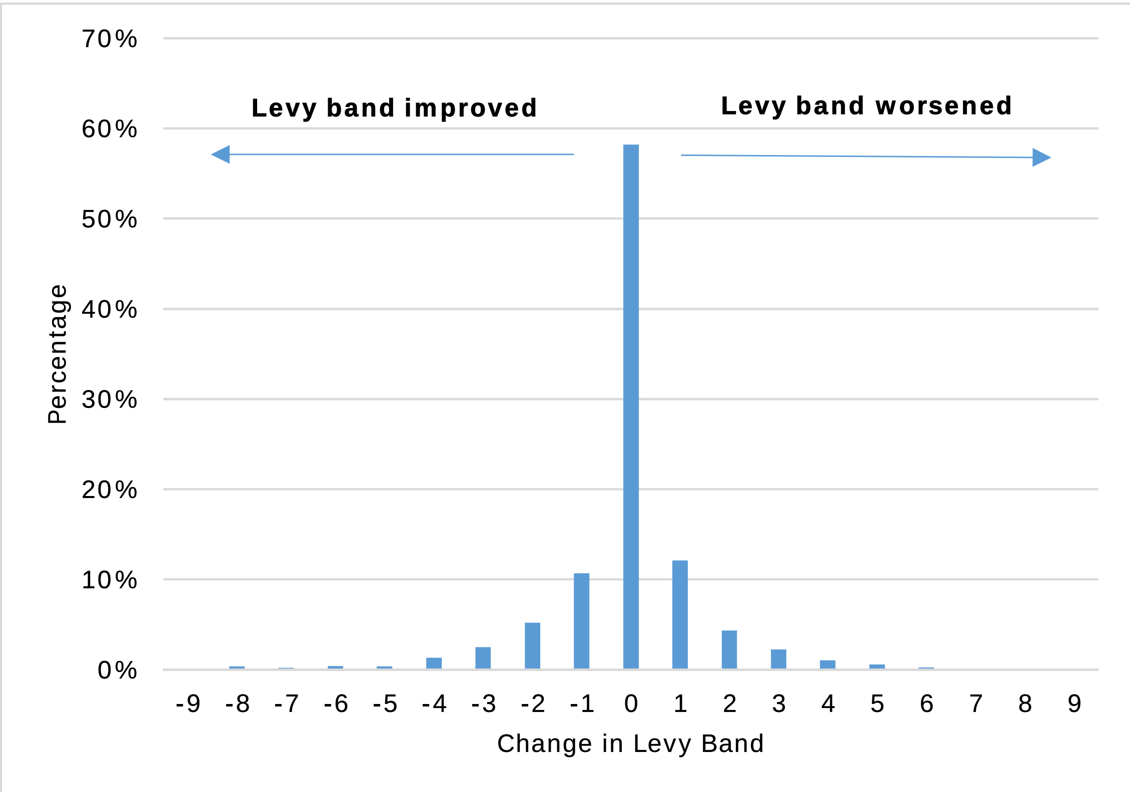
[8] This is an expected result given limited numbers of companies scored and their low insolvency probabilities.

Over half of insolvencies arose amongst employers scored in Bands 9 and 10, though these bands contain around one in ten of all PPF employers.

4.2.5. The Gini coefficient measures how well the PPF-specific model scorecards discriminate between solvent and insolvent sponsors. We have calculated the Gini coefficient for the model over the period April 2017 to March 2018. When the model as a whole is considered the performance continued to be "strong" [9] at 62.4 per cent.

4.2.6. In the third triennium policy statement[10] we predicted that, following an initial movement in scores on transition, the new scorecards would prove to be as stable as their predecessors. This was supported by testing the effect of past changes in accounting information at that time. We have now verified our expectation by looking at movement in scores between April 2017 and March 2018 for employers scored on the new scorecards. Chart 3 shows the level of change in levy band over 2017/18. The new data confirms our expectation that the new scorecards are as stable as their predecessors.

Chart 3: Change in levy band of sponsors of eligible DB Schemes between April 2017 and March 2018



4.2.7. In the third triennium consultation some stakeholders questioned whether adopting the new scorecard 1 (ie, Non-subsidiaries > £30m and largest subsidiaries) was justified. This was on the basis of a limited difference in

[9] Scores of below 45% would typically be considered weak, 45-55% is average and anything above 55% strong.

[10] Published in September 2017 with the 2018/19 Consultation Document.

predictiveness compared to one of its predecessor scorecards (the Large and Complex scorecard), but significant impacts on scores (and levies) for some employers assessed.

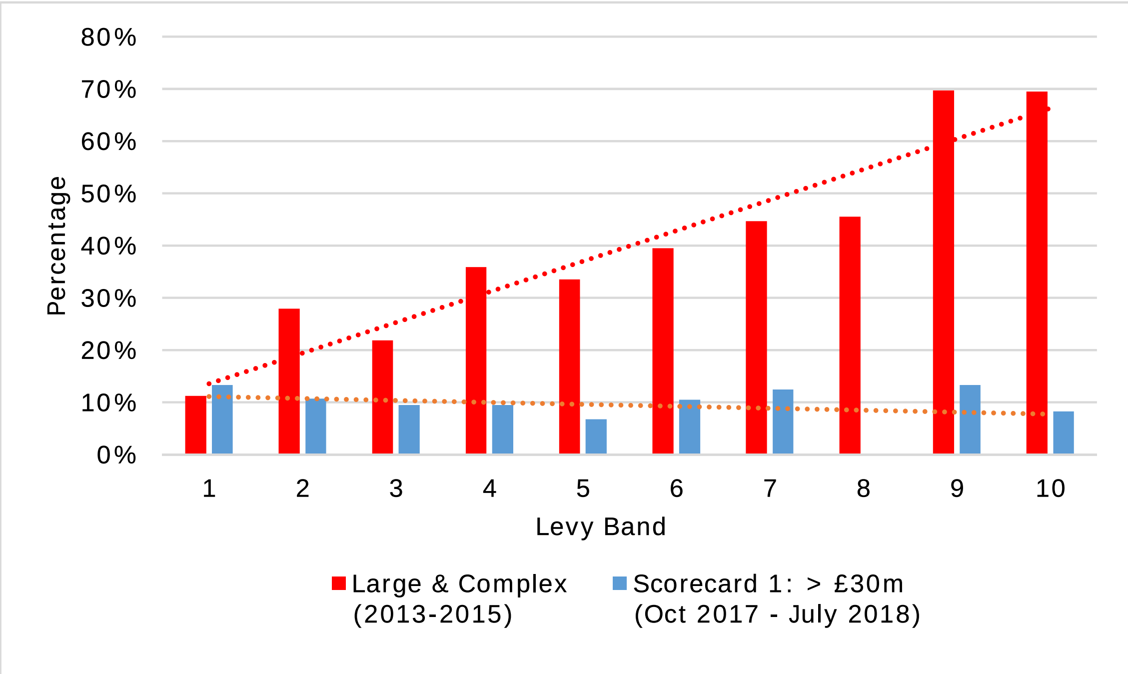
4.2.8. Two important factors that led us to decide to rebuild the predecessor scorecards were:

(1) There had been a very significant change in the population actually scored on the predecessor scorecards, since they were built.

(2) There was significant potential for future changes in population, given the opportunity for employers to move scorecard by changing their corporate structure.

4.2.9. Chart 4 shows that when we look at scorecard 1 over the period between October 2017 and July 2018 we are no longer seeing the level of change in population seen previously. Also we no longer observe the strong link previously seen between high levy band and high scorecard movement.

Chart 4: Distribution of sponsors of eligible DB Schemes that changed scorecards



4.3. Should We Use the S&P Credit Model for Additional Regulated Sectors?

4.3.1. It was suggested, during the third triennium consultation, that the use of S&P credit model could be extended beyond entities in the regulated financial services sector, with a specific suggestion of extension to the regulated energy sector. We said in our December 2017 Policy Statement that we could consider the case for extending within the current triennium rather than waiting for the fourth triennium.

4.3.2. In principle we recognise that insolvency risk scoring developed upon industry sectors may be more predictive but we have identified a significant risk that employers may seek to get themselves onto a particular scorecard if they believe it will produce a lower risk result. In the past we saw employers changing their standard industry classification (SIC) where this could lead to an advantage. Therefore when we introduced the use of the S&P credit model we limited its use to employers on the Bank of England list of banks, building societies and insurance providers. Therefore it is important that any regulatory licensing regime is not easy to ‘join’ and/or ‘leave’ and captures entities that are clearly within that sector.

4.3.3. When considering whether there was a case for extending the use of the S&P credit model beyond the regulated financial services sector, we looked at the three main utility types (and their regulators): Gas & Electricity, Water and Telecommunications.

4.3.4. The regulated energy sector is overseen by the Office of Gas and Electricity Markets (Ofgem). They are the only utility regulator that provides regulated party/licence holder lists (in a similar way to the Bank of England’s), which are updated on a regular basis, allowing us to confidently identify authorised parties. Therefore, our work focussed on the Gas & Electricity sector.

4.3.5. We identified 34 employers of eligible schemes which have been licensed to carry out activities concerning gas and electricity. Of those, 19 are currently scored using a public credit rating (which would continue to be used in priority to an S&P credit model score). Ten appeared to have Electricity/Gas as their core industry, but five did not.

4.3.6. While we were satisfied that the Ofgem licensing regime would limit entry and exit to the population to be scored, holding a licence is not conclusive evidence that gas and electricity activities are an entity’s core activity. Benefitting from a licence were for example also universities, banks, and oil & gas companies. Therefore we would need to be able to objectively assess an individual entity’s activities and/or to rely on an alternative industry categorisation (e.g. an algorithm run by an external provider). We think this adds too much complexity and subjectivity, especially given the limited number involved.

4.3.7. We were not attracted to such an approach as it would result in reduced transparency and only be used to score a small number of employers.

Consultation question: do you agree that we should not extend the use of the S&P credit model for the regulated energy sector?

4.4. Accounting Standards Changes - IAS 19

4.4.1. As the PPF-specific model relies upon annual accounts information we monitor changes to accounting standards and consider whether they could impact the performance of the model. Since Levy Year 2017/18 we have allowed schemes to complete certificates where the adoption of FRS 101/102[11] has affected the calculation of ‘change’ variables (ie, variables where accounts data from a current year is compared to the same data in an earlier year). We did this because a difference in the two sets of accounts

[11] Revised financial reporting standards that could impact employers within multi-employer schemes.

may be because the data is on a different basis rather than the data reflecting an improving or worsening position.

4.4.2. We have considered the possible impact of a change to the accounting standard IAS (International Accounting Standard) 19 Employee Benefits. The changes apply to accounting periods starting on or after 1 January 2019 (so would not be expected to impact monthly scores until 2020/21 at the earliest).

4.4.3. The changes to IAS 19 include to the calculation of the cost of providing pensions. Specifically there will be a requirement to immediately recognise the cost of scheme benefit improvements. A pension scheme surplus can be recognised on the balance sheet and IAS 19 also clarifies the way in which the asset ceiling operates for such surpluses.

4.4.4. The change does not affect the total cost of scheme improvements, but it could require costs to be recognised earlier. Where variables use reported data from a single set of accounts our starting point is that adjustments to accounting standards should simply result in more accurate data being used.

4.4.5. Change variables are now a less significant feature of the PPF-specific model. Only one of the re-built scorecards and three of the recalibrated group scorecards now has change variables. We do not believe that any of the change variables (Change in Fixed Assets, Change in Total Assets, Change in Turnover or Change in Employee Remuneration) will be materially affected as a result of any adjustments made as a result of the change. We are not therefore proposing any adjustments or the use of certificates as we did for FRS101/102.

4.4.6. There is another forthcoming change (IFRIC 14), concerning the availability of refunds from a defined benefit pension scheme which may have a more significant impact. We will monitor this and make proposals if necessary.

4.5. Special Category Employers

4.5.1. In 2018/19, we introduced a rule which allowed employers to apply to be classified as Special Category Employers (SCE) for the first time. As mentioned above, these are, broadly speaking, employers set up by legislation or governmental bodies whose legal structure and the nature of their business is such that the other available categories don't reflect the risk they pose to us.

4.5.2. We made clear when we introduced the rule that we expected only limited numbers to be within the scope of the rule and this has been the case in practice.

4.5.3. We believe the process for considering applications worked well and we intend to follow a similar approach for future years for new applications. If there are employers that believe this rule could apply but did not apply in 2018/19 we would encourage them to apply in good time for 2019/20.

4.5.4. For 2019/20 we have made changes to the rule to reflect that those employers that were granted SCE status would remain classified provided the employers complete certain review and confirmation requirements (so we can be sure the employer still thinks the SCE status is still appropriate). For instance:

(1) Confirmation that there has been no material change that would affect the SCE status. If employers don't reply by 31 March 2019, the SCE status will be revoked.

(2) For those employers who have been granted SCE status on the basis of the de minimis state aid regime, confirmation that the levy saving afforded by the SCE status in 2019/20 remains within the de minimis financial limits. Again, if employers don't reply by 31 March 2019, the SCE status will be revoked.

4.5.5. We have also made minor updates to the guidance to reflect comments received from our stakeholders, mainly to make clearer the documentation and evidence that we require in order for an application to be successful.

4.6. Categorisation of Employers on the Basis of the Type of Accounts Filed

4.6.1. The 2018/19 Levy Rules included a discretion for the PPF to be able to instruct Experian to categorise employers that Experian would otherwise categorise as filing full accounts as being categorised as appropriately scored on a small accounts scorecard.

4.6.2. This change was introduced as stakeholders raised with us the impact of changes in the accounts classifications. Some employers had filed small accounts and scored on the appropriate scorecard for a number of years. However when they started to file a new form of abbreviated accounts, (Exempt: Full Accounts), Companies House classified them as a type of full accounts and consequently Experian initially scored them on full accounts scorecards. As these accounts, like small company accounts, did not include Profit & Loss items including turnover and profit this resulted in unknown scores being applied to several variables.

4.6.3. We instructed Experian to re-categorise those employers as scored on small accounts scorecards where we thought such re-classification was appropriate, for example where they had previously filed small accounts and whose size suggested this would be consistent with the employer accounts that those scorecards were developed on.

4.6.4. Employers filing abbreviated accounts with Companies House can still provide full accounts (with the profit and loss account items included) on a voluntary basis to Experian though once they have opted to do this Experian will continue to score the employer on the appropriate full accounts scorecard even if they do not voluntarily file in future.

5. Contingent Assets

5.1. Introduction

5.1.1. We undertook an additional consultation exercise in late 2017 which led to the publication of revised standard form agreements in January 2018. We explained in our December 2017 Policy Statement that certain schemes would need to re-execute their agreement using the new standard form agreements for 2019/20.

5.1.2. Affected schemes are those with contingent assets that include a fixed sum element in the cap on the amount that could be recovered under the guarantee (this includes those where the fixed sum element is within a 'lower of' formula). This would need to be completed by the deadline for certification (which we intend will be 31 March 2019 for online actions and 5pm on Friday 29 March 2019 for hard copy documents).

5.2. Re-execution and Levy Recognition for Type A and B Contingent Assets in 2019/20

5.2.1. For 2019/20 Levy Year, as previously indicated, we propose to only recognise in the levy contingent assets **which include a fixed sum maximum amount element** (this includes those where the fixed sum element is within a 'lower of' formula) **(a "fixed cap")** that are on the new standard form agreements we published in January 2018[12]. We refer to this as the "Re-execution Requirements".

5.2.2. Where schemes with agreements with fixed caps (on the old standard forms, ie, available before 18 January 2018) do not re-execute the agreement and certify it as a new or recertified contingent asset we intend that no levy credit will be given.

5.2.3. As in previous years, any new contingent assets entered into are required to be on the new standard forms if levy credit is sought.

5.2.4. Schemes may also choose to re-execute other agreements (Type As or Bs with fluctuating caps or Type Cs) using the new standard form agreements, even though they are not required to do so for levy recognition.

5.2.5. In view of the time it can take to put a new contingent asset agreement in place we have taken a number of steps to encourage schemes to take early action to ensure everything is in place by the end of March 2019. We sent out an e-mail in March to all schemes that we could identify as having certified contingent assets in 2018/19 or the prior four years to encourage them to start thinking about whether they would need to re-execute and the planning that would entail. We have also produced a short video, available on our website and you tube channel explaining which schemes may need to re-execute and what they should do.

[12] These were republished in March 2018 to pick up minor/typographical points.

5.3. Re-execution Requirements: Recertification or New Certification?

5.3.1. For contingent asset agreements that are being entered into in order to satisfy our re-execution requirements, we are expecting to be able to provide suitable categorisation on Exchange to identify these as recertifications with or without changes (as the case may be), rather than expecting these agreements to be certified as new submissions. This is so that we can identify those schemes that have taken steps to comply with the re-execution requirements.

5.3.2. We have considered what documentation requirements should apply, and have concluded that where a new agreement is entered into for the re-execution requirements, we should require generally the same documents as for any new contingent asset submission, namely the following, which will need to be sent to the PPF by 5pm on Friday 29 March 2019:

- Certified copy of the legal agreement
- Legal opinion (though this may be a refreshed/updated version by reference to an existing legal opinion)
- Comparison document showing any changes from the standard form
- Copy of the Contingent Asset certificate
- Certain confirmations/advice in relation to the value of the Contingent Asset.

Full details of the certification requirements are included in the draft Contingent Asset Appendix and Guidance.

5.3.3 Where a guarantor strength report is provided, though, we propose that a refresher report, explaining what has changed, would be acceptable, provided that a guarantor strength report was produced on the same guarantor for the 2018/19 Levy Year.

5.3.4 Where Type A agreements move onto the new standard forms by way of amendment and restatement, it is our expectation that we are likely to require the same documents and certifications as if the contingent asset were newly executed, but we would welcome views.

5.3.5 If a Type B contingent asset is being re-executed this will require the creation of a new charge in favour of the pension scheme. We will work with Experian to identify any such charges related to these re-executions. This will mean schemes will not need to submit a mortgage exclusion certificate to maintain the existing age of the most recent charge (ignoring the new charge created as part of the re-execution). The mortgage age variable now only impacts the group turnover based scorecards 3, 4 and 5.

Consultation question: is there any further guidance that is needed to help you complete the re-execution of contingent assets?

Consultation question: do you consider that any relaxation would be appropriate for the documentation and certification requirements for Type A agreements that are amended/restated rather than re-executed afresh?

5.4. Type C Contingent Assets

5.4.1 Type C contingent assets are not affected by the issue which requires re-execution of Type A and B contingent assets. However, due to their nature, some Type C contingent assets are renewed annually. Our preference is that schemes move on to the January 2018 standard forms when they come to refresh their Type Cs after expiry, but we understand some stakeholders feel some changes could be made to the new standard forms. Therefore, we invite further input so that we can consider all in the round in deciding whether the Type Cs need updating.

Consultation question: do you have any drafting comments on the Type C contingent assets?

5.5. Guarantor Strength Reports

5.5.1 2018/19 was the first Levy Year that we required guarantor strength reports to have been obtained and submitted by the time the trustees certified/re-certified Type A contingent assets where their acceptance would generate a levy benefit of £100,000 or more. We would be interested in stakeholders' observations on the guidance we published last year, in the light of carrying out assessments.

5.5.2 We identified 87 contingent assets that triggered the guarantor report requirement and reports were received for the vast majority. We are currently completing our checking of these reports and will report on any lessons learnt when we publish our policy statement in December. One early observation we have made is that the duty of care requirement appears to have been correctly included in the reports we have examined so far – from a wide range of covenant advisers.

5.5.3 We are working with TPR to improve the certification process on the Exchange system. We hope this will make it easier to confirm whether a report is required and that it has/will be sent to the PPF (by 5pm on 29 March 2019).

6 Implementation of Other Third Triennium Changes

6.1 Introduction

6.1.1 We introduced changes to several areas for the third triennium. We have reviewed how these have worked in practice and in some cases are proposing tweaks to ensure they achieve the intended results.

6.2 Deficit Reduction Certificates (DRCs)

6.2.1 We introduced changes for the third triennium that provided greater flexibility in the submission of DRCs.

- **Option Alpha -** removed the requirement to deduct investment management expenses and an option for all schemes
- **Option Beta** – allowed scheme trustee certification for small schemes closed to future accrual based on recovery plan and certain 'special' contributions.

6.2.2 In 2018/19 we saw a higher value of DRC certification (up to £24.7 billion from £20.4 billion) as were the number of schemes certifying, up to 2,350 from 2,125. Of those certifying (ie, ignoring those that simply allowed their previous certificate to roll over for 2018/19) around 90 per cent certified under Option Alpha and 10 per cent under Option Beta (most without actuarial certification).

6.2.3 We have reviewed and updated the DRC Appendix and Guidance to clarify further the exclusion of investment management expenses. In addition, we have clarified that in order to be eligible for Option Beta a scheme must be closed to accrual in its entirety and that accrued benefits must not retain any element of salary linkage. In practice, we would expect this to be supported by a scheme status of 'Paid-up' on Exchange.

6.2.4 Our rationale for clarifying this is to ensure that Option Beta remains a simple, straightforward methodology, not just in terms of calculating the amount of DRCs to certify, but in establishing in the first instance whether a scheme is eligible. However, we are keen to encourage the take-up of Option Beta and would welcome feedback as to whether drawing the definition in this way is likely to prevent a significant number of schemes which would otherwise be eligible.

6.2.5 Although the response of stakeholders both during and following the consultation has been positive we note that there still appear to be significant numbers of levy payers who have not applied to obtain credit for contributions. We produced a short video (available on our website) explaining the new certification options before the 2018/19 deadline for certification and will look for other opportunities to ensure schemes that could benefit from the new arrangements are aware of them.

6.2.6 To help promote reporting of deficit reducing payments we

- have reviewed and updated the DRC Appendix and Guidance to clarify them where necessary
- have put a range of material on the website, and

- are considering the opportunity for targeting information to schemes we think are eligible but are not using Option Beta

6.2.7 Last year a number of schemes contacted us to seek clarification as to whether a substitute could enter the DRC certificate details into Exchange on behalf of the person specified in the DRC appendix. We have updated the DRC appendix and DRC guidance to clarify that a 'duly appointed substitute' can complete the DRC certificate on Exchange.

6.2.8 We have become aware of a scheme with rules that allow a member on retirement to opt to exchange future pension increases for a higher initial pension. We are considering whether such a member option should be regarded as an augmentation for the purposes of certifying the scheme's DRC. We would welcome stakeholder views as to whether this is a common member option and whether it is generally considered an augmentation.

We would welcome any suggestions as to how we can ensure all schemes eligible for either method are aware of the changes, which we hope will help ensure all schemes making contributions will receive recognition for them.

Consultation question: do you have any comments on the clarifications we are proposing to the guidance and rules on DRCs?

6.3 Block Transfers

6.3.1 We introduced different reporting requirements for Exempt Transfers, in circumstances where the whole assets and liabilities are transferred from one scheme or section to another.

6.3.2 Where successful applications were made by 30 April the receiving scheme/section was not required to complete a block transfer certificate and s179 data and other scheme information was carried forward.

6.3.3 We have reviewed both the guidance and process we followed for Exempt Transfer applications in 2018/19 and identified a number of improvements we can make.

- We will introduce an application form for 2019/20 which will help applicants ensure all the relevant information is provided and provide consistency amongst applications
- We have revised the guidance and rules taking account of the 2018/19 experience, in particular the certification requirements (for ABCs, DRCs and Contingent Assets).

6.3.4 Separately we set out proposals for the calculation of the levy for consolidation vehicles. Where schemes or sections are transferring into such vehicles we do not believe exempt transfer eligibility would be appropriate. We make it clear in the proposals for those types of arrangements that the need for comprehensive up to date information will be an important element of the requirements to ensure such vehicles are charged an appropriate levy.

6.3.5 We have also considered whether we should make changes to the block transfer certificate. Our aim is to enable receiving schemes to be able to provide additional information either through the scheme return or through the block transfer certificate. We do not expect that it will be possible to implement any changes to Exchange for 2019/20 and so we also intend to provide guidance on the circumstances in which we would be likely to exercise our discretion and accept data not provided through the scheme return or block transfer certificate.

6.3.6 We believe that some receiving schemes can face difficulties in providing data through the scheme return if they have not had scheme audited accounts completed at the time they complete the scheme return. In these cases they can find themselves locked out of the scheme return and unable to complete asset split information and other scheme information.

6.3.7 We are investigating with The Pensions Regulator (TPR) the possibility of making changes to the Exchange system that might reduce the areas of the return that are blocked if audited accounts have not yet been produced. We are also considering whether it might be possible to amend the question asked on Exchange (about completed audited accounts) for recently established receiving schemes to allow information to be provided that has been prepared by the scheme actuary on a similar prudent basis as for estimating the s179 valuation – not understating the value of protected liabilities or overstating the assets.

6.3.8 In addition we are exploring the possibility of extending the block transfer certificate to allow the reporting of the following

- Asset split information
- Bespoke Stress Test information
- Employer membership split information
- Normal Pension Age (NPA) information

6.3.9 As we do not expect to be able to implement changes on Exchange for 2019/20 we also want to provide guidance on when we are likely to exercise our discretion to allow data to be provided where full transfers have occurred, other than through the scheme return or block transfer certificate. Where the reason for the data not being provided through these methods is that audited accounts having not yet been produced and the transfer occurred within the year ending on 31 March we are likely to accept data providing asset and liability information is provided on the basis set out in 6.3.7.

Consultation question: do you agree with our proposals to seek to improve the opportunities for full transfer receiving schemes to provide accurate data for schemes following a full transfer?

6.4 Levy Payment

6.4.1 We have received requests from a small number of stakeholders and more recently have had the issue raised in the Work and Pensions Select Committee to consider whether we could take additional steps to help schemes (in particular schemes with small or medium employers) plan for their levy payments and avoid having to find a significant sum over what could be a short time.

6.4.2 The levy is a charge on the scheme - although in many cases the charge is passed on to the scheme employers - and is capped at 0.5% of the scheme's liabilities. Currently, the overwhelming majority of levy payers pay their invoices within 28 days. The issue, therefore, is not about schemes' ability to pay, rather whether we can do more to help schemes and their employers with managing their cash flow, helping ensure any disruption caused by levy bills is minimised as far as possible.

6.4.3 We think there are two aspects to this. Firstly, allowing schemes and employers to plan ahead – identifying likely changes in levy bills ahead of time. Currently we support this by publishing our Levy Rules three months before the start of the Levy Year, and providing "real time" access to insolvency risk scores through the PPF/Experian portal. In principle, therefore, schemes can identify for their sponsors the levy that will be charged before it is invoiced and (if appropriate) plan payments from the employer to meet that levy. However, we recognise that our rules are technical and that converting insolvency risk scores to estimated levy charges is not straightforward. We know that many advisers provide their clients with estimated levy charges shortly after the annual publication of our rules, but schemes without advisers may struggle to gain the same level of insight. We would, therefore, welcome views on what additional support we could usefully provide to assist with forward planning and how we might tailor this to reach those schemes most in need of additional support.

6.4.4 The second element is supporting schemes to pay their invoice. We currently encourage schemes facing difficulties in payment to contact us to discuss the possibility of a payment plan. We can then offer flexibility, though payments made outside our normal terms accrue an interest charge for late payment, and we will not ordinarily waive this. We would welcome views on the current payment system and on what further support could be helpful.

6.4.5 We are interested in all thoughts (including for example on payment methods) but have been asked in particular whether payments by instalments might be made a more standard option to assist SMEs. We are mindful of two particular points here. Firstly, given the vast majority of bills are currently paid on terms, the introduction of payments by instalments would risk making levy collection slower, less certain and more costly – which would impact all levy payers and stakeholders. Secondly, whilst current legislation would allow us to specify that the levy is payable in parts at different dates, our view is that this would have to apply to all schemes and could not be limited to SMEs, increasing the risk that material amounts of levy are collected later and potentially increasing the administrative burden on schemes. Legislation does also allow payment by instalments of an invoice following an application from the scheme trustees or managers; the Board can then consider whether allowing instalments would be appropriate taking account of any exceptional circumstances (for example, where the scheme is in genuine difficulties) that apply to that scheme. However, this does not allow payments by instalment to become routine.

6.4.6 In view of these issues, we would therefore welcome specific thoughts on when in the year the levy should be payable (for example making the levy payable in more than one part at different dates), and on the approach we take to payments by instalments.

Consultation question: what additional support could we usefully provide to assist schemes with forward planning?

Consultation question: what further support could we offer schemes to assist them with paying their levy invoice?

Consultation question: to what extent is it worth exploring the potential to charge the levy in parts at different dates? Which categories of scheme would most benefit? Is there a case for legislative change to allow "automatic" payment by instalments to become routine for specific categories of scheme?

6.5 The impact of Britain's exit from the European Union

6.5.1 Section 7 sets out a summary of legal changes proposed for 2019/20. This includes a proposed discretion that would allow the PPF to deal with consequential impacts from Britain's exit from the European Union.

6.5.2 Such impacts might include references to the definition of Nominated Jurisdiction (which refers to countries that are members of the EU) and the Type C contingent asset requirement that giver is FCA regulated/approved 'either directly or on the basis of rights in European Union law'.

Consultation question: do you have any suggestions of issues that we should consider in relation to Britain's exit from the European Union?

7. Draft Levy Rules 2019/20

Overview of Determination and Appendices

7.1.1. We have made a number of minor amendments to the Determination and Appendices including:

i. Picking up updates to certain cross references.

ii. Updates to deadlines.

Determination

iii. Amendment to the definition of 'Refinance Mortgage' (Rule A1.1) so as to relax the documentation requirements supporting Mortgage Exclusion certificates.

iv. A general Board discretion so that the Board can effectively and appropriately respond in regard to Brexit in the Levy Year (Rule A1.2(18)).

v. An update to the interpretation provisions to make clear that website documents and links are as updated from time to time (Rule A1.2(19)).

vi. Clarification of Rule D3.2 in relation to the bespoke investment stress tests – so that it's clear that the calculation and submission is expected even where the audited accounts are the same as the previous year.

vii. Amendment of Experian's postal address for the purposes of voluntary submissions of data (Rule E2.3) and Experian appeals (Rule E7.3). Documents should normally be sent to Experian by e-mail at experianppf@mailgb.custhelp.com . They should only be sent by post where Experian have given written permission for this method.

viii. Clarification of the timings of updates to credit ratings, with a change in Rule E2.4(1) and a corresponding change in Rule E2.8(1). Credit ratings are applied in the month after collection, and this is not changing, but we consider the new drafting makes this clearer by setting the timing in E2.4 rather than requiring a reading of E2.8(1) too.

ix. Amendment of the special category employer rule (E3.1(11)) so as to allow the special category employer status to carry forward where there has been no material change and/or the de minimis requirements are met.

x. Clarification of the exempt transfer provisions to make clear that for 1-to-1 transfers nominal accrual for the purposes of enabling the transfer to occur is permitted (Rule F4.1(b)(i)). Also to make clear that exempt transfers are 'Full Transfers', but the requirements for full transfers don't apply, and instead the exempt transfer regime applies (Rule F4.2).

Appendices

xi. Amendment to paragraph 4(13) of the Contingent Asset Appendix to set out that the UK is a 'Nominated Jurisdiction'.

xii. Contingent Asset Appendix. Amendment of the provisions in relation to the applicable standard form to require the Type A and B contingent assets that include a fixed sum element to move to the standard forms published in January 2018 – ie the 're-execution requirements' (paragraph 4(18)).

xiii. Clarification of paragraph 17 of the Contingent Asset Appendix to ensure the multiple guarantors follow the strongest-first principle.

xiv. Clarification of paragraph 21A of the Contingent Asset Appendix in relation to guarantor-employers, to allow for certain scenarios where recognising the guarantor in the calculation would lead to a lower levy.

xv. Amendment of the hard copy submission requirements in the Contingent Asset Appendix to set out that where the re-execution requirements apply, the submission must be as for a new contingent asset (subject to guarantor strength requirements being allowed on an update only basis if the Type A is only moving onto the new standard form with no other changes).

xvi. Some clarifications relating to parent strength adjustments in paragraph 3.4 of the Insolvency Risk Appendix.

xvii. Incorporation of S&P public credit ratings "SD" (selective default) and "R" (regulatory supervision owing to financial condition) in Table 5 in Part 4 of the Insolvency Risk Appendix. For completeness, it is appropriate to add them to our list.

7.2. Measurement Time in 2019/20

7.2.1. We are proposing to maintain the standard Measurement Time for the online submission of scheme data of midnight at the end of 31 March 2019. The measurement time for hard copy documents to be submitted is proposed as 5pm on 29 March 2019 (including for the certification of contingent assets where agreements have been re-executed to be recognised for 2019/20).

7.2.2. The Measurement Time for certification of deficit-reduction certificates is 5pm on 30 April 2019 and for block transfers at 5pm on 28 June 2019.

7.2.3. Please note that our telephone support service for stakeholders on 29 March 2019 will be available up until 5pm as in previous levy years – and this will also be true of Experian's.

8. Summary of Consultation Questions

Scheme consolidation and schemes without a substantive sponsor

i. Do you think the proposed definition will adequately identify those schemes that ought to be levied as a consolidation vehicle?

ii. To incentivise consolidators to have appropriate wind-up-triggers, do you think it better to adjust the strike price or set a higher scheme-based levy?

iii. Do you agree that we should make prudent assumptions in the event information is not forthcoming?

iv. Do you have comments on the approach proposed in relation to buffer funds?

v. Do you have comments on the adjustments we ae making to the SWOSS methodology (and which will also apply in the commercial consolidator methodology)?

vi. Are the information requirements that we propose ones that consolidators can reasonably comply with?

vii. If not are there simplifying assumptions that we should use?

The measurement of insolvency risk

viii. Do you agree that we should not extend the use of the S&P credit model for the regulated energy sector?

Contingent assets

ix. Is there any further guidance that is needed to help you complete the re-execution of contingent assets?

x. Do you consider that any relaxation would be appropriate for the documentation and certification requirements for Type A agreements that are amended/restated rather than re-executed afresh?

xi. Do you have any drafting comments on the Type C contingent assets?

Implementation of other third triennium changes

xii. We would welcome any suggestions as to how we can ensure all schemes eligible for either method are aware of the changes, which we hope will help ensure all schemes making contributions will receive recognition for them.

xiii. Do you have any comments on the clarifications we are proposing to the guidance and rules on DRCs?

xiv. Do you agree with our proposals to seek to improve the opportunities for full transfer receiving schemes to provide accurate data for schemes following a full transfer?

xv. What additional support could we usefully provide to assist schemes with forward planning?

xvi. What further support could we offer schemes to assist them with paying their levy invoice?

xvii. To what extent is it worth exploring the potential to charge the levy in parts at different dates? Which categories of scheme would most benefit? Is there a case for legislative change to allow “automatic” payment by instalments to become routine for specific categories of scheme?

xviii. Do you have any suggestions of issues that we should consider in relation to Britain’s exit from the European Union?

9. Consultation Arrangements and Key Dates

9.1. 2019/20 Consultation

9.1.1. The consultation on the 2019/20 Levy Rules runs from 20 September 2018 to 5pm on 25 October 2018. Please ensure that your response reaches us by the deadline. Submissions may be made by email or post, using the details below.

Email: consultation@ppf.gsi.gov.uk

Postal address: Chris Collins
Chief Policy Adviser
Pension Protection Fund
Renaissance
12 Dingwall Road
Croydon, Surrey
CR0 2NA

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

9.1.3. Under the Freedom of Information Act 2000 (FoIA), all information contained in the response, including personal information may be subject to publication or disclosure. By providing personal information for the purpose of the public consultation exercise, it is understood that a respondent consents to its disclosure and publication.

9.1.4. If this is not the case, the respondent should limit any personal information which is provided, or remove it completely. If a respondent requests that the information given in response to the consultation be kept confidential, this will only be possible if it is consistent with FoIA obligations and general law on this issue. Further information can be found on the website of the Ministry of Justice at:

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

9.1.5. A summary of responses and the Board's final Determination and confirmed policy are planned to be published on the PPF website at:

http://www.pensionprotectionfund.org.uk in December 2018.

9.2. Key Dates

9.2.1. We will continue to use information from the annual scheme return that is submitted via the Pension Regulator's Exchange system to calculate levies. The deadline for submission is midnight at the end of Sunday 31 March 2019, except as detailed below.

Item	Key dates
Monthly Experian Scores, Credit Ratings and credit model scores to be used in 2019/20 levy	Between 30 April 2018 and 31 March 2019
Deadline for providing updated information (to Experian) to impact on Monthly Experian Scores	One calendar month prior to the Score Measurement Date
Submit scheme returns on Exchange	By midnight 31 March 2019
Reference period over which funding is smoothed	5-year period to 31 March 2019
Certification of contingent assets	Online by midnight 31 March 2019 Hard Copy documents by 5.00pm on 29 March 2019
Certification of asset backed contributions (e-mailed to PPF)	By midnight 31 March 2019
Experian certificates – covering mortgages, FRS 101/102, employee information (e-mailed to Experian)	By midnight 31 March 2019
Applications for Special Category Employer Status	By midnight 31 March 2019
Applications for Exempt Transfers	By 5pm on 30 April 2019
Certification of deficit-reduction contributions	By 5pm, 30 April 2019
Certification of full block transfers	By 5pm, 28 June 2019
Invoicing starts	Autumn 2019

9.3. Comments on the Consultation Arrangements

9.3.1. This consultation is being conducted in line with the Cabinet Office's Consultation Principles that can be found on their website at:

http://www.cabinetoffice.gov.uk/resource-library/consultation-principles-guidance

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

Trish O'Donnell
Stakeholder Manager
Pension Protection Fund
Renaissance
12 Dingwall Road
Croydon, Surrey
CR0 2NA

Email: corporateaffairs@ppf.gsi.gov.uk

Deadline for consultation responses is 5pm on 25 October 2018.

APPENDIX A: Cumulative Impacts of Changes

Example scheme 1 with: 55 per cent hedging bonds and cash, 45 per cent alternative / hybrid assets, derivatives.

Assets	£1.05bn	£1.10bn	£1.15bn	£1.20bn
S179 Liabilities	£1bn	£1bn	£1bn	£1bn
Funding Ratio	105%	110%	115%	120%
RBL – 2018/19 SWOSS methodology (with latest risk-free rate)	£3.35m	£960k	£225k	£45k
RBL – above with Garman-Kohlhagen method	£3.99m	£1.18m	£290k	£60k
RBL – above with adjusted s179 liabilities (see Appendix B) - assumed to have increased by 1.5% p.a.	£5.49m	£1.75m	£460k	£100k
RBL – above with iterative approach	£6.25m	£1.83m	£465k	£100k
2019/20 RBL	**£6.25m**	**£1.83m**	**£465k**	**£100k**
2019/20 RBL with 120% s179 profit extraction threshold	£6.67m	£2.22m	£765k	£295k
2019/20 RBL with 100% s179 strike price (only if no wind-up trigger)	£54.63m	£19.63m	£7.44m	£2.68m

Example scheme 2 with 85% hedging bonds and cash, 15% hedge funds, derivatives.

Assets	£1.05bn	£1.10bn	£1.15bn	£1.20bn
S179 Liabilities	£1bn	£1bn	£1bn	£1bn
Funding Ratio	105%	110%	115%	120%
RBL – 2018/19 SWOSS methodology (with latest risk-free rate)	£75k	£5k	0	0
RBL – above with Garman-Kohlhagen method (implies zero risk free rate)	£120k	£5k	0	0
RBL – above with adjusted s179 liabilities (see Appendix B) - assumed to have increased by 1.5% p.a.	£280k	£15k	0	0
RBL – above with iterative approach	£280k	£15k	0	0
2019/20 RBL	**£280k**	**£15k**	**0**	**0**
2019/20 RBL with 120% s179 profit extraction threshold	£285k	£15k	0	0
2019/20 RBL with 100% s179 strike price (only if no wind-up trigger)	£17.09m	£2.69m	£305k	£20k

Note that the factors used to calculate the levy amounts above are based on the current s179 assumptions (A8). New s179 assumptions are being consulted on and may be introduced later this year, and it is anticipated that new conversion factors will be used to maintain the applicable strike price when there is a wind-up trigger in place.

Commentary

It will be seen that each change proposed tends to increase the levy that would be paid by a consolidator, where the impact is more significant when the funding position of the consolidator falls to being only slightly over-funded.

The change that has the greatest effect is to move the strike price, which would only apply if there is no wind-up trigger. Also of note is the sensitivity of the levy amounts to the level of risk in the investment strategy.

APPENDIX B: Information Requirements for Commercial Consolidators

The information requirements set out below are those which are necessary to permit the calculation of the risk-based levy for a Commercial Consolidator for the Levy Year 2019/20, in accordance with the draft Commercial Consolidator Appendix and without the application of any prudent assumptions or default parameters. We do not envisage that this will represent an undue burden upon Commercial Consolidators, as we anticipate that each item will either be produced as part of their ongoing business operations or can be readily derived from information produced for this purpose.

Information Requirement	Comments
Section 179 Valuation	This can be submitted on Exchange in the usual way, or otherwise provided to the PPF in an agreed manner. The effective date of the Section 179 Valuation should be no earlier than 1 January 2017.
Adjusted Section 179 Valuation	This should be carried out at the same effective date as the Section 179 Valuation, but incorporating allowance for anticipated increases in PPF liabilities for existing members up to 31 March 2020. Further details are given below.
Bespoke stress analysis	This should be carried out at the date of the most recently audited accounts, showing the breakdown of the unstressed asset value into the refined asset classes set out in the draft Investment Risk Appendix, as well as the underlying values of PV01 and IE01.
Extracts from governing documents, showing:	
1. provision for extraction of funds from scheme assets and any ‘buffer’;	1. This relates to extractions on an ongoing basis (ie, before buyout of liabilities), over and above normal running costs and other than for the benefit of members.

2. the threshold above which such extractions are possible; and 3. any wind-up trigger.	2. This should be expressed as a funding level on a Section 179 basis (instead of or in addition to a funding level on any other basis). 3. This should be expressed as a funding level on a Section 179 basis (instead of or in addition to a funding level on any other basis), and should be designed so as to automatically trigger employer insolvency and the commencement of a PPF assessment period once funding falls below the specified level.
Details of any actual extractions under 1 above	This should identify those extractions which have depleted the scope for future extractions over the period to 31 March 2020, noting whether they are reflected in the Section 179 Valuation assets.

Adjusted Section 179 Valuation

An Adjusted Section 179 Valuation is obtained by adjusting the corresponding Section 179 Valuation to take account of the following:

- accrual of benefits after the relevant time and up to the earlier of 31 March 2020 or Normal Pension Age (as defined in the relevant version of the Section 179 Valuation guidance) is included for all active members at the relevant time;
- benefits in deferment at the relevant time and accrued before 6 April 2009 are increased at the relevant time to anticipate any difference between the revaluation due and revaluation up to CPI capped at 5 per cent a year, both measures assessed over the period after the relevant time and up to the earlier of 31 March 2020 or Normal Pension Age for each affected member (where the benefits of active members as well as deferred members are assumed to be in deferment);
- benefits in deferment at the relevant time and accrued after 5 April 2009 are increased at the relevant time to anticipate any difference between the revaluation due and revaluation up to CPI capped at 2.5 per cent a year, both measures assessed over the period after the relevant time and up to the earlier of 31 March 2020 or Normal Pension Age for each affected member (where the benefits of active members as well as deferred members are assumed to be in deferment);
- the compensation cap is applied only to members who will be under Normal Pension Age at 31 March 2020;
- benefits are reduced by ten per cent only in respect of members who will be under Normal Pension Age at 31 March 2020;
- benefits in payment at the relevant time and accrued before 6 April 1997 are increased at the relevant time to anticipate any increases due between the relevant time and 31 March 2020 for each affected member;
- benefits in payment at the relevant time and accrued after 5 April 1997 are increased at the relevant time to anticipate any difference between the increases due and indexation up to CPI capped at 2.5 per cent each year, both measures

assessed over the period after the relevant time and up to 31 March 2020 for each affected member; and

- temporary pensions in payment at the relevant time which are due to cease by 31 March 2020 are excluded.

For the avoidance of doubt:

- the Adjusted Section 179 Valuation is carried out at the same relevant time as the Section 179 Valuation, using the same version of the Section 179 Valuation assumptions guidance and the same version of the Section 179 Valuation guidance, with the latter modified only to the extent specified above. In particular, no adjustment is made to the value of the assets;
- the Adjusted Section 179 Valuation contains no allowance for salary increases in excess of revaluation after the relevant time; and
- the Adjusted Section 179 Valuation assumes that each active member at the relevant time will remain an active member to the earlier of 31 March 2020 and Normal Pension Age.