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Part 1 – Effective date of guidance

1.1. This is version H2 of the guidance.

1.2. This version of the guidance is effective for valuations with an effective date on or after 11 September 2006 or for valuations with an effective date prior to 11 September 2006 which are signed on or after 1 January 2007.

1.3. This guidance should be read in conjunction with the most recent version of our *Guidance on assumptions to use when undertaking the valuation in accordance with Section 143 of the Pensions Act 2004.*

Part 2 – Overview

2.1 Process

2.1.1 The Pensions Act 2004 (“the Act”) sets out the conditions that must be met for the Pension Protection Fund to assume responsibility for a scheme.

2.1.2 In order for the Pension Protection Fund to assume responsibility for a scheme, the scheme must satisfy the following key criteria:

- the scheme must be a scheme which is **eligible** for the Pension Protection Fund;
- the scheme must not have commenced wind-up before 6 April 2005;
- an **insolvency event** must have occurred in relation to the scheme's employer which is a **qualifying insolvency event**;
- there must be no chance that the scheme can be rescued; and
- there must be insufficient assets in the scheme to secure benefits on wind-up that are at least equal to the compensation that the Pension Protection Fund would pay if it assumed responsibility for the scheme.

2.1.3 If a qualifying insolvency event occurs in relation to an employer of an eligible scheme, this will trigger the beginning of an assessment period. During this period the Pension Protection Fund will assess whether or not it must assume responsibility for the scheme.

2.1.4 Part of this process involves looking at the scheme’s assets and liabilities to determine whether the scheme can afford to secure benefits that are at least equal to the compensation that the Pension Protection Fund would pay if it assumed responsibility for the scheme.

2.1.5 If the scheme can secure benefits at least equal to the compensation payable by the Pension Protection Fund, it will be ordered to wind-up outside of the Pension Protection Fund by securing benefits in the market or run on as a closed scheme if it qualifies under **section 153** of the Act.

2.1.6 If it cannot and the relevant process and procedures have been completed, then the Pension Protection Fund will assume responsibility for the scheme and compensation will then become payable.

2.1.7 A Pension Protection Fund assessment period is likely to last a minimum of one year and could be longer, depending on the complexity of the financial situation of both the employer and the scheme, and the possibility of a scheme rescue.

2.1.8 The valuation under **section 143** will determine whether the scheme has sufficient funds to pay at least the Pension Protection Fund levels of compensation as set out above.

2.2 Purpose of this guidance

2.2.1 This guidance is intended for actuaries undertaking valuations to determine the level of funding in accordance with **section 143** of the Act. Such guidance was envisaged in **paragraph (6) of section 143**. It should be read in conjunction with "*Guidance on assumptions to use when undertaking a valuation in accordance with Section 143 of the Pensions Act*".

2.2.2 The Act and associated regulations set out the high-level principles relating to the valuation with this guidance setting out the detail.

2.2.3 The legislation and associated regulations relating to these valuations came into force on 6 April 2005.

2.3 Purpose of the section 143 valuation

2.3.1 The purpose of the valuation is to determine whether the Board of the Pension Protection Fund should assume responsibility for a scheme. This valuation is only required within a Pension Protection Fund assessment period, and the Board of the Pension Protection Fund will instruct an actuary to carry out the valuation.

2.3.2 Once the valuation has been completed, the Board of the Pension Protection Fund must approve it in accordance with **section 144**. The valuation becomes legally binding once it has been approved and the period within which the approval may be reviewed has expired.

2.3.3 Where the valuation establishes that the assets are not sufficient to meet the protected liabilities, the Board of the Pension Protection Fund will assume responsibility for the scheme and pay compensation to scheme members in accordance with **Schedule 7** to the Act. Where the assets are sufficient to meet the protected liabilities the scheme will be ordered to wind up outside of the Pension Protection Fund by securing benefits in the market.

2.4 Legislative requirements

2.4.1 The Act sets out the requirement for the Board of the Pension Protection Fund to obtain an actuarial valuation of an eligible scheme where either:

- a qualifying insolvency event has occurred in relation to the employer (**section 127(1)**) of the Act;
- the trustees of the scheme make an application to the Board of the Pension Protection Fund (**section 128(1)** of the Act) under **section 129** of the Act.

2.4.2 An eligible scheme is defined by **section 126** and associated regulations.

2.5 Who completes the valuation

2.5.1 The actuarial valuation must be prepared and signed by a person appointed by the Board of the Pension Protection Fund, who must meet the criteria specified in **section 143(11)(a)(ii)** and the valuation regulations.

2.6 Where to send valuation information

2.6.1 Details relating to the **section 143** valuation (the entry valuation) should be provided to the Pension Protection Fund by the date requested by the Board of the Pension Protection Fund and no later than 28 days after the date on which the valuation is signed.

2.6.2 For further details about the Pension Protection Fund please visit the Pension Protection Fund website at: www.pensionprotectionfund.org.uk

2.6.3 The contact address for the Pension Protection Fund is:
Pension Protection Fund
Knollys House
17 Addiscombe Road
CROYDON
CR0 6SR
Tel: 0845 600 2541

2.7 Legislation or authority for actuarial valuations

The Pensions Act 2004 (the Act)

The Pension Protection Fund (Valuation Regulations) 2005 SI 2005/672 (“the valuation regulations”)

The Pension Protection Fund (Partially Guaranteed Schemes)(Modification) Regulations 2005 SI 2005/277

The Pension Protection Fund (Pension Compensation Cap) Order 2006. SI 2006/347 (“the Cap regulations”)

The Occupational Pension Schemes (Modification of Pension Protection Provisions) Regulations 2005 SI 2005/705

The Pension Protection Fund (Compensation) Regulations 2005 SI 2005/670

The Pension Protection Fund (Multi-employer Schemes)(Modification) Regulations 2005 SI 2005/441

Part 3 – Introduction

3.1 Under **section 143** of the Act the Board of the Pension Protection Fund must obtain an actuarial valuation of an eligible scheme (an “entry valuation”) where either:

- a qualifying insolvency event has occurred in relation to the employer (**section 127(1)** of the Act): or
- the trustees of the scheme make an application to the Pension Protection Fund (**section 128(1)**) under **section 129** of the Act.

3.2 An eligible scheme is defined by **section 126** of the Act and the Pension Protection Fund (Entry Rules) Regulations 2005.

3.3 When the Board of the Pension Protection Fund decides to obtain the valuation, in most cases the trustees will be approached to ask the pension scheme actuary to complete the valuation.

3.4 Once obtained, the Board of the Pension Protection Fund will consider whether to approve the valuation. Following approval, trustees will be required to notify members of their entitlements under the approved valuation. Members have the opportunity to dispute these entitlements and can request a review (**Schedule 9**).

3.5 The valuation becomes legally binding once any rights of review have been exhausted.

3.6 In this guidance note “relevant time” has the meaning given in either **sections 127(4)(b)** or **128(3)(b)** of the Act as appropriate.

3.7 The actuarial valuation must be prepared and signed by a person meeting the criteria specified in **section 143(11)(a)(ii)** of the Act and the valuation regulations.

Part 4 – Protected liabilities

4.1 The scheme's protected liabilities are defined in **section 131** of the Act. The amount of the protected liabilities relating to benefits for or in respect of members and to wind-up expenses shall be determined in accordance with **section 143** of the Act, the valuation regulations and this guidance note.

4.2 The amount of protected liabilities relating to liabilities that are not liabilities to or in respect of members shall be determined in accordance with **section 143** of the Act, the valuation regulations and this guidance. The liabilities to members are taken to be the estimated cost of securing scheme benefits (applying the provisions of **Schedule 7**) to members by purchasing an annuity at the market rate.

Part 5 – Benefits for and in respect of members

5.1 The benefits for and in respect of members of the scheme should be valued as at the relevant time and should be determined as at that date in accordance with **Schedule 7** to the Act, the associated regulations and the scheme's admissible rules (as defined in paragraph 35 of **Schedule 7**). The benefits to be valued for any reviewable ill-health pensions should be as determined and notified by the Board of the Pension Protection Fund in accordance with **section 141(2)** of the Act.

5.2 In accordance with **section 143(7)** of the Act the value of liabilities should not be limited to the value of the assets, even where the scheme rules may so provide.

5.3 The pension of a pensioner who

- is not a dependant
- is not an ill-health pensioner
- has not attained Normal Pension Age at the relevant time

is subject to the compensation cap appropriate to the age at the relevant time. This capped pension is then subject to multiplication by 90% (the compensation level).

5.4 The pension at Normal Pension Age of a non-pensioner who has not attained Normal Pension Age is subject to the Compensation Cap at Normal Pension Age. This capped pension is then subject to multiplication by 90% (the compensation level).

5.5 For the purpose of determining and valuing the benefits, the compensation cap should be assumed to increase by 1.5 % a year in excess of limited price index increases during any period of deferment after the relevant time.

5.6 Normal Pension Age should be determined as provided within **Schedule 7** to the Act, paragraph 34. Benefits for non-pensioners must be valued as payable at the Normal Pension Age applicable to each part of the benefit.

5.7 It should be assumed that there is no commutation of pension for a lump sum at retirement for non-pensioners. Where, however, a scheme provides for a defined separate lump sum to be paid at retirement, other than as a result of commutation, such a lump sum should be valued.

5.8 The Act provides that in certain circumstances where the Board of the Pension Protection Fund is satisfied that it is not possible to identify one or more elements of the benefit formulae as defined in **Schedule 7** to the Act, they may direct how the benefit should be calculated. Where this is the case the scheme actuary must apply to the Board of the Pension Protection Fund for a determination to be made.

5.9 Where a scheme with more than one employer operates a sectionalised scheme, separate valuations will be required for each separate section of the scheme, setting out the assets and benefits attributable to each section.

5.10 For schemes with a partial Crown guarantee, the valuation should only be of the part of the scheme that is not covered by the Crown guarantee.

5.11 For a hybrid "better of" scheme, the assets and benefits will relate to only those members where the defined benefits exceed the defined contribution benefits at the relevant time. The calculation for each individual should consider whether the underpin bites at the relevant time using the current scheme methodology and section 143 valuation assumptions. Only those members for whom the defined benefits exceed the defined contribution benefits should be included in the liability calculations. The compensation cap and the 90% level should be applied to the defined benefit members of the hybrid scheme (after the underpin test has taken place).

5.12 In a hybrid defined contribution scheme with a defined benefit underpin, for any period of service where the defined benefit underpin would not apply, the corresponding assets and liabilities should be excluded from the valuation. In a hybrid defined contribution scheme with a defined benefit underpin that only applies for a particular period of service, the member's fund in relation to that period of service alone should be compared to the underpin.

5.13 The liability in respect of money purchase benefits shall be disregarded for the purposes of determining the protected liabilities. The definition of what constitutes a money purchase benefit is a matter of some uncertainty. Please refer to the Pension Protection Fund website for further information.

Part 6 – Assets

6.1 Assets must be taken into account as specified in the valuation regulations.

6.2 The actuary may also consider a **section 75** (of the Pensions Act 1995) debt, contribution notices, financial services directions and restoration orders that fall due to the scheme before the valuation is approved **even if it falls due after the relevant time of the valuation** as an asset of the scheme.

6.3 The actuary can assign assets a different value from that shown in the relevant accounts if he thinks it appropriate, and take into account any other amounts that might fall due to the scheme after the relevant time if, in his opinion, it is appropriate that it should be counted as an asset. Such amendments and additions should be highlighted in the valuation results report.

6.4. Where there is a **section 75** debt, contribution notice, financial support direction or restoration order, the actuary should obtain advice from the Board of the Pension Protection Fund as to how much of that debt should be taken into account when establishing the assets. If there are no such assets, the actuary should make a comment to that effect.

6.5 Advice should also be sought from the Board of the Pension Protection Fund where the valuation of any assets not included in the relevant accounts is to be used to determine assets for this valuation, for example:

- assets acquired after the relevant time;
- proceeds from any relevant insurance policy.

6.6 The assets in respect of money purchase benefits shall be disregarded in accordance with **section 143(11)(d)** of the Act.

Part 7 – Data

7.1 To assist with assessing the scheme's protected liabilities to and in respect of its members, the trustees or managers of the scheme must :

- take appropriate action to ensure that, as far as is practicable, all potential scheme beneficiaries have been identified
- do all they can to resolve any data uncertainties in respect of all potential scheme beneficiaries. This may necessitate, for example, going through paper records and liaising with scheme members.

7.2 The actuarial report should summarise both the process the trustees have taken to assure themselves on the accuracy of the data and the checks the actuary themselves have undertaken. The actuarial valuation must detail any residual concerns regarding the data, and indicate so if no such concerns exist.

Part 8 – Valuation method

8.1 Any reasonable age definition may be used for the purpose of the calculation provided consistency with the revaluation and increase periods can be demonstrated. The age definition should be stated within the report.

8.2 For each scheme member, the protected liability must be calculated as the present value of the accrued benefits using the assumptions specified in the most recent version of *"Guidance on assumptions to use when undertaking a valuation in accordance with Section 143 of the Pensions Act 2004"*.

Part 9 – Expenses

9.1 Expenses must be determined as specified in the most recent version of *"Guidance on assumptions to use when undertaking a valuation in accordance with Section 143 of the Pensions Act 2004"*.

Part 10 – Reporting

10.1 The results of the valuation must be provided to the Board of the Pension Protection Fund in accordance with **regulation 9(1)** of the valuation regulations. The valuation results report must be provided to the Board of the Pension Protection Fund as soon as practicably possible following completion of the valuation but certainly within 28 days of completion.

10.2 The valuation results report must also contain:

- The assessment date.
- Which version of this guidance has been used.
- Which version of the assumptions guidance has been used.
- Yield in deferment.
- Yield in payment for pension accrued before 6 April 1997.
- Yield in payment for pension accrued after 5 April 1997.
- The age definition used.
- A description of any additional assumptions made and justification, if appropriate.
- Data and liability component information.

  Where, for a membership category, tranches of benefits are payable at more than one NPA, then there should be more than one table (each corresponding to a different NPA) for that membership category. Where some individual members have more than one NPA, then these members will contribute data to more than one row in a particular category. An electronic version of the Data and Liability component information spreadsheet, along with example figures, is available on the PPF website.
- Any residual concerns about the data.
- Estimated expenses of wind-up.
- Estimated expenses of benefit installation / payment.
- The liabilities of the scheme which are not liabilities to, or in respect of its members.
- Total protected liabilities.
- A statement about whether there is a section 75 debt, contribution notice, financial support direction or a restoration order included in the assets value.
- The assets figure in the relevant accounts split into the major asset types.

- The assets figure used for the valuation split into the major asset types.
- A reconciliation of the above two assets figures.

10.3 The report should be signed and dated by the actuary. The actuary's full name should be printed below his/her signature. His/her qualification should be stated as well as their employer details.

10.4 The actuary should also complete, sign and date the certificate in Appendix 1. The certificate should be sent to the Board of the Pension Protection Fund along with the valuation report.

Part 11 – Review

11.1 This guidance note will be reviewed at regular intervals as the Board of the Pension Protection Fund deem appropriate.

Appendix 1: Certificate for the purposes of section 143 of the Pensions Act 2004

Scheme name :

Relevant time :

End of period covered by relevant accounts :

Version number of section 143 guidance used :

Version number of section 143 assumptions used :

Protected liabilities		**£'000**
a	Liabilities for and in respect of members, excluding benefit installation/payment expenses and cost of winding up	
b	Liabilities other than for and in respect of members	
c	Benefit installation/payment expenses	
d	Estimated cost of winding-up	
Total		

Assets

Funding level in accordance with section 143 of the Pensions Act 2004 **%**

I certify the protected liabilities have been determined in accordance with the provisions of the Pensions Act 2004 and its relevant regulations and the Pension Protection Fund guidance for professionals.

In my opinion appropriate action/insufficient action* has been taken to ensure that as far as practical all potential scheme beneficiaries have been identified and data uncertainties resolved. The formal report on the actuarial valuation details my residual concerns where appropriate.

*delete as appropriate

A copy of the formal report on the actuarial valuation for the purposes of section 143 of the Pensions Act 2004 is attached.

Signature .... Date ....

Name ....

Qualification................................. Employer...