Pension
Protection
Fund

Guidance for undertaking the entry valuation in accordance with Section 143 of the Pensions Act 2004

Contents

Part 1 – Overview

1.1 Introduction

1.1.1 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.

1.1.2 In high-level terms, 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.

1.1.3 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.

1.1.4 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.

1.1.5 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.

1.1.6 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.

1.1.7 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.

1.1.8 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.

1.2 Purpose of this guidance

1.2.1 This guidance is intended for actuaries undertaking valuations to determine the level of funding in accordance with **section 143** of the Act.

1.2.2 The Act and associated regulations set out the high level principles relating to the valuation with this guidance setting out the detailed assumptions and discount rates to be applied.

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

1.3 Purpose of the section 143 valuation

1.3.1 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.

1.3.2 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.

1.3.3 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.

1.4 Legislative requirements

1.4.1 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)**);
- the trustees of the scheme make an application to the Board of the Pension Protection Fund (**section 128(1)**) under **section 129**.

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

1.5 Who completes the valuation

1.5.1 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.

1.6 Where to send valuation information

1.6.1 Details relating to the **section 143** valuation (the entry valuation) should be provided to the Pension Protection Fund by the notified date.

1.6.2 For further details about the Pension Protection Fund please visit the Pension Protection Fund website at:

www.pensionprotectionfund.org.uk

1.6.3 The contact address for the Pension Protection Fund is:

Pension Protection Fund
Knollys House
Levels 8 & 9
17 Addiscombe Road
CROYDON
CR0 6SR
Tel: 0845 600 2541

1.7 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 2005. SI2005/825 ('the Cap regulations')

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

The Occupational Pension Schemes (Levies) Regulations 2005
SI 2005/842

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

The Pension Protection Fund (Multi-employer Schemes)(Modification) Regulations 2005
SI2005/441

The Pension Protection Fund (Hybrid Schemes)(Modification) Regulations 2005
SI2005/449

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Part 2 – Introduction

2.1 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.

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

2.3 The Board of the Pension Protection Fund will issue a notice to the trustees or managers of the scheme setting out the requirement for the **section 143** valuation and the time when it must be submitted.

2.4 When the Pension Protection Fund decide to obtain the valuation, in most cases the trustees will be approached to ask the pension scheme actuary to complete the valuation.

2.5 Once obtained, the Pension Protection Fund should 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**)

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

2.7 In this guidance note 'relevant time' has the meaning given in either **sections 127(4)(b)** or **128(3)(b)** of the Act and the valuation regulations as appropriate.

2.8 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 3 – Protected liabilities

3.1 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.

3.2 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 4 – Benefits for and in respect of members

4.1 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 and associated regulations – paras 4(4), 6(4), 9(4), 12(4), 13(4), 16(3)(b), 17(4), 18(4), 20(4), 20(7), 20(8), 23(1), 23(2), 24(1), 24(2), 24(6), 25(1), 25(2), 26(9), 26(10), 28(6), 28(7), 30, 31(2), 31(3), 33, 35(6), 36(5), 37(4), 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.

4.2 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.

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

4.4 Normal pension age for a member or applicable to different parts of a member's benefit 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.

4.5 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.

4.6 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.

4.7 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.

4.8 For a hybrid 'better off' scheme the assets and benefits will relate to only those members where the defined benefits exceed the defined contribution benefits at the relevant time.

4.9 The liability in respect of money purchase benefits shall be disregarded for the purposes of determining the protected liabilities. Money purchase benefits which have been converted into defined benefit rights on retirement before the relevant date must be valued in the same way as other benefits for pensioners.

Part 5 – Assets

5.1 Assets must be taken into account as specified in the valuation regulations. The actuary may also consider a **section 75** debt, contribution notices, financial services directions and restoration orders that falls 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. Furthermore he 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.

5.2. Where there is a **section 75** (of the Pensions Act 1995) 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.

5.3 Advice should also be sought from the Board of the Pension Protection Fund where the valuation of any asset 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.

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

Part 6 – Data

6.1 In 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 practical all potential scheme beneficiaries have been identified. The actuarial valuation must include a description of the action taken and detail any residual concerns.

Part 7 – Valuation method

7.1 Any reasonable age definition may be used for the purpose of the calculation provided consistency with the revaluation and increase periods can be demonstrated.

7.2 For each scheme member the protected liability must be calculated as the present value of the accrued benefits using the assumptions specified in Appendix 1.

Part 8 – Expenses

8.1 Expenses must be determined as specified in Appendix 1.

Part 9 – Reporting

9.1 The results of the valuation must be provided to the Board of the Pension Protection Fund in accordance with regulation 9 of the valuation regulations.

9.2 A certificate in the form set out in Appendix 2 of this guidance note must also be provided to the Board of the Pension Protection Fund.

9.3 Both documents must be provided to the Board of the Pension Protection Fund once the valuation has been completed and certified by the actuary. This must be done as soon as practicably possible following completion of the valuation but must be within 28 days of completion.

Part 10 – Review

10.1 This guidance note will be reviewed at least annually. It may be reviewed and revised at more frequent intervals, as the Board of the Pension Protection Fund deem appropriate.

Appendix 1: Basis for use when undertaking valuations

Version: 1

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1 Yield in deferment

For each non-pensioner the liability for the period of deferment must be obtained by discounting the benefit at normal pension age at the adjusted net index-linked gilt yield shown below. As this yield implicitly allows for increases to normal pension age no allowance should be made for increases to benefits between the relevant date and normal pension age.

Adjusted net index-linked gilt yield = Yield A (**i**) – 0.5%

(**i**) Yield A should be determined daily as 50% of the sum of the FTSE Actuaries' Government Securities Index-Linked annualised Real Yields over 15 years assuming:

a 5% inflation; and

b 0% inflation.

For any dates where yields are not available the yields for the nearest preceding date should be used.

2 Yield in payment

For each pensioner and each non-pensioner for the period from which payments are assumed to commence the liability must be obtained by reference to the following (adjusted) yields:

Pensions with no increases in payment

Yield = Yield B (**ii**)

(**ii**) Yield B should be determined daily as the annualised yield on the FTSE Actuaries' Government 10 year Fixed Interest Index.

For any dates where the yield is not available the yield for the nearest preceding date should be used.

Pensions increasing in payment

Adjusted yield = Yield C (**iii**) – 0.5%

(**iii**) Yield C should be determined daily as 50% of the sum of the FTSE Actuaries' Government Securities Index-Linked annualised Real Yields over five years assuming:

a 5% inflation; and

b 0% inflation.

For any dates where yields are not available the yields for the nearest preceding date should be used.

3 Mortality

The mortality tables to be used in respect of a member and the member's dependant shall be PMA92 (for males) and PFA92 (for females), as appropriate, in each case with the medium cohort mortality improvement rates. These mortality tables are published by the actuarial profession. For each individual, the set of mortality rates used shall be those applicable to that individual's year of birth.

The derived rates shall be subject to an age rating based on an individual's benefit size as follows:

Pension size*	**Age rating**
< 25% x compensation cap	+ 2
25% - 50% x compensation cap	0
> 50% x compensation cap	-2

* For non-pensioners to include revaluation to calculation date only, and to include the pension equivalent (calculated on the basis of actuarial equivalence) of any lump sum entitlement.

4 Assumptions for contingent benefits

a) Proportions married

Where the scheme provides for survivor pensions:

For pensioners:

Where the scheme makes provision for survivor pensions for 'relevant partners' an assumption consistent with 90% (males) or 80% (females) at normal pension age.

Where the scheme does not make provision for survivor pensions for 'relevant partners' other than legal spouses an assumption consistent with 80% (males) or 70% (females) at normal pension age.

For non-pensioners:

Where the scheme makes provision for survivor pensions for 'relevant partners' the assumption must be, at the assumed date of retirement or earlier death, 90% (males) or 80% (females).

Where the scheme does not make provision for survivor pensions for 'relevant partners' other than legal spouses the assumption must be, at the assumed date of retirement or earlier death, 80% (males) or 70% (females).

b) Age difference between member and dependant

Female assumed to be 3 years younger than male.

c) Children's pensions

No specific additional allowance to be included for prospective children's pensions. Children's pensions already in payment should be assumed to cease at age 18, or age 23 if currently aged over 17.

5 Expenses

a) Estimated wind-up expenses

3% of any liability value up to £50million plus:

- 2% of any liabilities between £50million and £100million;
- 1% of any liabilities in excess of £100million.

b) Benefit installation/payment expenses

For the purposes of the certificate these should be included as part of the liabilities for or in respect of members.

Pensioners - Age related scale

Age	**Expense allowance per member £**
< 60	450
60 – 70	400
70 – 80	300
80 +	250

Non-pensioners

An allowance of £500 per member should be made.

Appendix 2: Certificate for the purposes of section 143 of the Pensions Act 2004

Scheme name :

Relevant date :

End of period covered by relevant accounts :

Protected liabilities		**£'000**
a	Liabilities for and in respect of members, including expenses of payment	
b	Liabilities other than for and in respect of members	
c	Estimated cost of winding-up	
Total		
Assets		
Funding level in accordance with section 143 of the Pensions Act 2004		**%**

I certify the protected liabilities (a) and (c) 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 #1, version ______________________________

The value of the assets and protected liabilities (b) have been provided by

____

In my opinion appropriate action/insufficient action* has been taken to ensure that as far as practical all potential scheme beneficiaries have been identified. The formal report on the actuarial valuation includes a description of the action taken and 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..