Pension
Protection
Fund

Guidance for undertaking the risk based levy valuation in accordance with Section 179 of the Pensions Act 2004

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Part 1 – Overview

1.1 Introduction

1.1.1 To calculate the risk based pension protection levy the Pension Protection Fund Board must take account of scheme underfunding. To obtain a consistent basis for determining underfunding schemes will be required to complete a Pension Protection Fund valuation. This valuation will be based on the level of assets and liabilities for the scheme. The liabilities will be based on the scheme benefits taking into account key features of the levels of compensation paid by the Board of the Pension Protection Fund as set out in **Schedule 7** of the Act.

1.1.2 All schemes will be charged an initial levy based on scheme factors only for the levy year commencing April 2005.

1.1.3 The risk based pension protection levy will apply from April 2006. Schemes submitting a Pension Protection Fund valuation prior to 31 March 2006 will be charged a levy based on risk using the information provided in the valuation. The purpose of the risk based levy is to reflect the differing levels of risk pension schemes pose to the fund.

1.2 Purpose of this guidance

1.2.1 This guidance is intended for actuaries undertaking valuations to determine the level of underfunding in accordance with **section 179** of the Act. Such guidance was envisaged in paragraph (4) of **section 179**. The valuation results will be used to set and calculate the risk based pension protection levy in accordance with **section 175**.

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

1.3 Legislative requirements

1.3.1 **Section 179** of the Act requires schemes to undertake a Pension Protection Fund valuation to establish the level of the scheme's assets and liabilities in order to set the risk based levy.

1.3.2 The associated regulations set out the high level principles concerning the way in which the valuation should be conducted with this guidance setting out the detailed assumptions and discount rates.

1.4 Why is this valuation necessary and when is it needed by?

1.4.1 The valuation will provide the Board of the Pension Protection Fund with information on the level of underfunding within a scheme. This will inform the calculation of the risk based pension protection levy.

1.4.2 Schemes have considerable discretion in choosing when to provide their first Pension Protection Fund valuation, **but** the:

- relevant time ('relevant time' for the purposes of **section 179** of the Act, means the date in relation to which the assets and liabilities of the eligible scheme are calculated) of the valuation must be no earlier than 1 November 2004 and no later than 5 April 2008, but see paragraph 3.2 below; and

- valuation must be sent to the Pensions Regulator within a year of the relevant time.

1.4.3 After the initial valuation, schemes must provide the Pensions Regulator with further valuations at regular intervals. The relevant time of each subsequent valuation must be no later than three years after the relevant time of the previous valuation and, again, the valuation must be sent to the Pensions Regulator within a year of the relevant time.

1.4.4 This time scale allows for the valuation to be undertaken in line with a scheme's normal valuation cycle, however, any scheme may complete a Pension Protection Fund valuation at any time after April 2005. Once a Pension Protection Fund valuation is completed, the levies imposed on that scheme will reflect the risk factors – the level of risk that the scheme poses to the Pension Protection Fund.

1.4.5 To pay a risk based levy based on the level of Pension Protection Fund liabilities for the levy year commencing 1 April 2006 schemes must complete and provide the relevant information relating to a **section 179** valuation to the Board of the Pension Protection Fund by 31 March 2006.

1.5 Frequency of valuations

1.5.1 Schemes must undertake levy valuations in accordance with **section 179** of the Act and associated regulations at least once every three years.

1.5.2 Schemes wanting to provide a valuation on a more regular basis may do so. The most recent valuation information provided by 31 March each year will be used to calculate the risk based levy.

1.6 Where to send valuation information

1.6.1 Details relating to the levy valuation should be provided to the Pensions Regulator as part of the normal annual scheme return form process. Where the scheme return form has already been completed and returned to the Pensions Regulator, the valuation details should be provided on the form contained at Appendix 2, and forwarded to the Pension Protection Fund.

1.6.2 For further details about the valuation process please go to 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 179** of the Act the trustees or managers of eligible schemes are required to provide the Board of the Pension Protection Fund with an actuarial valuation of the scheme at prescribed intervals and containing prescribed information.

2.2 An eligible scheme is defined by **section 126** of the Act and associated regulations.

2.3 In this guidance, 'relevant time' has the meaning given in the valuation regulations as appropriate.

2.4 The actuarial valuation must be prepared and signed by a person meeting the criteria specified in **section 179(2)** of the Act and the valuation regulations.

2.5 The **section 179** valuation is a simplified valuation based on the scheme's liabilities but taking into account certain key elements of the Pension Protection Fund compensation as set out in **Schedule 7**.

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 179** of the Act, the valuation regulations and this guidance note.

3.2 The scheme actuary may use prudent approximations in calculating the protected liabilities. Such approximations may include using liability data from a previous valuation, including one carried out prior to 1 November 2004, and rolling forward those liabilities on a prudent basis to the relevant time.

3.3 The scheme actuary is required to certify in his report that, in his opinion, the calculated value of the protected liabilities is unlikely to have been understated.

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. For the purposes of this valuation the amount of the protected liabilities relating to benefits for or in respect of members and to wind-up expenses shall be determined as being the **scheme benefits** (reflecting the provisions of the PPF Valuation Regulations which require scheme benefits, not PPF compensation, to be valued for a s179 valuation) but taking account of the following:

- applying the cap of the amount published in Pension Protection Fund guidance as currently appropriate at the normal pension age for the scheme to the benefits for those members under normal pension age and not in receipt of pension;

- applying the cap of the amount published in Pension Protection Fund guidance as currently appropriate for their age at the valuation date to the benefits for those members under normal pension age for the scheme and in receipt of pension (there is no requirement, for a **section 179** valuation, to take account of the pension equivalent of any lump sum paid at retirement) ;

- reducing the benefits by 10% in respect of those members under normal pension age on a pro-rata basis, excluding ill health, survivors benefits, etc;

- disregarding any indexation applicable to pre 6 April 1997 service on a pro-rata basis;

- allowing for indexation up to RPI but capped at 2.5% on service from 6 April 1997.

4.2 In accordance with **section 179(5)** 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 **section 179** valuation purposes, benefits for an active member should be calculated as though he had become a deferred pensioner immediately before the valuation date. In practice PPF compensation may be calculated slightly differently.

4.4 The pre-retirement decrements to be used to value benefits for non-pensioners are retirement at Normal Pension Age and death before Normal Pension Age.

4.5 For **section 179** valuation purposes, Normal Pension Age for a scheme member should be assumed to be the same as MFR Pension Age. This is the age at which the member will first become entitled under the provisions of the scheme to receive a full pension on retirement of an amount determined without a reduction to take account of its payment before a later age (but disregarding any entitlement to pension on retirement in the event of illness, incapacity or redundancy). See Regulation 7(10) of the Occupational Pension Schemes (Minimum Funding Requirement and Actuarial Valuations) Regulations 1996.

Paragraphs 34(1) and 34(2) of Schedule 7 to the Pensions Act 2004 should not be applied.

There will therefore be one Normal Pension Age for each scheme member for **section 179** valuation purposes. In practice PPF compensation may, of course, be payable in two or more tranches beginning at different ages, but this should be ignored for the purpose of a **section 179** valuation.

4.6 It should be assumed that there is no commutation of pension at retirement for non-pensioners.

4.7 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.

4.8 For schemes with a partial crown guarantee the valuation must only be of that part of the scheme that is not covered by a Crown guarantee.

4.9 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.

4.10 The liability in respect of money-purchase benefits shall be disregarded for the purposes of determining the protected liabilities.

Part 5 – Assets

5.1 Assets must be taken into account as specified in the valuation regulations. The valuation regulations specify that for the purposes of determining a **section 179** valuation the appropriate person shall adopt the value given of the assets of the scheme stated in the relevant accounts, less the amount of the external liabilities, and that value shall be taken to be the value of those assets at the relevant time.

5.2 The assets in respect of money-purchase benefits should not be included in the assets in accordance with **section 179 (6)** of the Act.

Part 6 – Data

6.1 The Pension Protection Fund regards it as best practice for trustees or managers to take appropriate action to ensure that, as far as is practicable, all potential scheme beneficiaries have been identified and that the associated membership data is correct. To the extent that there are residual uncertainties about the membership data, prudent approximations by the scheme actuary will be acceptable. This is an aspect of the prudent estimation of protected liabilities described in Part 3.

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 scheme actuary's report on the section 179 valuation should be addressed and sent to the trustees. The certificate in Appendix 2 should form part of the scheme actuary's report. The results of the **section 179** valuation should be included on the next annual scheme return form issued by the Pensions Regulator.

9.2 If the levy calculation in respect of a levy year commencing on 1 April in year (x) is to be based on the latest **section 179** valuation results, then:

- either these latest results must be incorporated into the annual scheme return sent to the Pensions Regulator in year (x-1)
- or the certificate attached at Appendix 2 must be completed electronically on the Pension Protection Fund website (from the homepage go to the Guidance Section and follow the link to Valuation Guidance) and provided to the Board of the Pension Protection Fund by 31 March in year (x).

Part 10 – Review

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

Appendix 1: Basis for use when undertaking valuations

Version: 2

Effective in respect of valuation reports signed on or after 1 November 2005:

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. Yields should be calculated to two places of decimals (e.g. 2.04% p.a.)

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. Yields should be calculated to two places of decimals (e.g. 4.76% p.a.)

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 5 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. Yields should be calculated to two places of decimals (e.g.1.93% p.a.)

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.

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 liabilities (excluding benefit installation / payment expenses) up to £50 million;

plus

2% of liabilities (excluding benefit installation / payment expenses) between £50 million and £100 million;

plus

1% of liabilities (excluding benefit installation / payment expenses) in excess of £100 million.

b) Benefit installation/payment expenses

Non-pensioners
An allowance of £500 per member should be made.

Pensioners
An age-related allowance per member should be made, according to the table below:

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

Appendix 2: S179 Valuation Certificate

Section 179 Valuation Certificate

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Scheme / Section Details

Full name of scheme

Pension Scheme Registration number

Does this scheme have sections or segregated parts? (see note below) Yes ○ No ●

Name of section or segregated part of scheme

Section number (XXX) of (XXX)

Address of scheme (or section, where appropriate)

Post code

Valuation Details (all figures in pounds, not thousands or millions)

Total assets.. £

Amount of external liabilities deducted to reach this figure.......................... £

Date of relevant accounts..

Total protected liabilities, excluding external liabilities.......................... £

Liabilities for pensioners, excluding expenses.......................... £

Liabilities for all deferred pensioners, excluding expenses.......................... £

Liabilities for active members, excluding expenses.......................... £

Estimated costs of winding up (excluding the estimated expenses of benefit installation/payment).................. £

Estimated expenses of benefit installation/payment.......................... £

Effective date of this valuation

Version number of section 179 guidance used for this valuation 1

Certification

☐ I certify that this valuation has been carried out in accordance with the Pension Protection Fund (Valuation) Regulations 2005 and with the latest section 179 guidance issued by the Board of the Pension Protection Fund. I also certify that the calculated value of the protected liabilities (excluding the external liabilities) is, in my opinion, unlikely to have been understated.

Name **Qualification**

Date **Employer**

Note

As per regulation 8 of the Pension Protection Fund (Valuation) Regulations 2005, a separate valuation and certificate should be prepared for each section or segregated part of a multi employer scheme.