The 2020/21 Pension Protection Levy Consultation Document

Foreword

This consultation invites comments on our proposed levy methodology for 2020/21.

This will be the final year of the three year period (the third triennium) during which we aim to maintain stable rules as far as possible. Stakeholders have previously confirmed that they welcome this approach. We are therefore pleased to confirm that we plan to use essentially the same approach to charging the levy in 2020/21 that we have been using this year.

However, the environment in which we are operating has changed. In particular scheme funding is expected to have deteriorated due to declines in the yields on gilts. We expect that to mean that schemes, in aggregate, will be less well funded as a result.

The increased deficits mean we are facing an increase in risk and whilst our levy framework significantly reduces the impact of short term changes in funding - by smoothing asset and liability values over a five year period – we nonetheless expect that this increased risk will lead to an increase in the levies we collect. Our expectation is that our overall collection will rise from around £575 million this year to an estimate of £620 million for levy year 2020/21.

However, as we are not proposing to change any of the key elements of the levy calculation, individual schemes will only see a change in the levy where their own underfunding or insolvency risk has changed. For schemes where this has remained stable the levy will not change.

While for next year we are making very few changes in the rules, we are, of course, planning for the future. In addition to changing insolvency risk information provider to Dun & Bradstreet from 2021/22 there are a number of sources of uncertainty for the future as explained in the following pages.

We remain grateful for our stakeholders' ongoing support and engagement and look forward to hearing your views on our proposals.

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Executive Director and General Counsel

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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 2020/21 Levy Year. We are seeking stakeholder input on these rules and also publishing the amount we expect to collect – the Levy Estimate.

1.1.2. A key feature of our levy Framework is that we have aimed to maintain stability in the way in which the levy is calculated over a three year period (or triennium). This objective has covered both the parameters for the levy (asset stresses, the scaling factor and the like) and rules more broadly. This approach has been widely supported reflecting the value that our levy payers place on stability in the levy rules. 2020/21 is the last year of the current three year period (the third triennium). As such we are not conducting a full scale review of our methodology. Instead we are looking to identify whether any changes are *necessary*, if not we will leave our approach unchanged.

1.2. Our Levy Estimate

1.2.1. We have estimated how much unchanged rules will collect in 2020/21. This is what we refer to as the "neutral levy estimate": neutral in that it differs from the previous year's estimate only due to changes in expected scheme funding and insolvency risks.

1.2.2. For next year, 2020/2021, our neutral levy estimate is that we will collect £620 million. This is around an 8 per cent increase on the £575 million we now expect to collect for 2019/20. The increase in our estimate, relative to collection in 2019/20, reflects the impact of external factors, principally falling gilt yields, which serve to reduce the funding level of pension schemes (and therefore to increase claims in the event of employer insolvency).

1.2.3. Collection in 2019/20, at £575 million, is now expected to be higher than the originally estimated £500 million – though it is broadly in line with collection in previous years. Some of the factors we had expected would reduce levy collection did not do so. We set this out in more detail in section 2.

1.2.4. Having made our neutral estimate we considered whether it was appropriate to alter our rules to target a different level of collection, by altering our levy scaling factor[1].

1.2.5. The increase implied by the neutral estimate is within the maximum permitted by the Pensions Act, and driven by increases in risk. We noted that the external environment is particularly uncertain at the moment. In addition to uncertainties about global and UK markets, there are pension specific uncertainties including from court cases regarding

[1] The levy scaling factor is the constant that we use to adjust levies up or down to the total we aim to collect. For the 2018/19 and 2019/20 years it was set at 0.48.

the UK's obligation to protect pension incomes in insolvency. These have the potential to increase the risks we face, the level of compensation we pay, and therefore affect the level of our funding, of future claims, and of the levies we need to charge.

1.2.6. Accordingly, we do not consider that there is any case for actively seeking to lower the amount we aim to collect.

1.2.7. In aggregate we expect levy invoices in 2020/21 to be around 8 per cent higher than for 2019/20 invoicing. However any increase for individual schemes will depend on the risk characteristics of the specific schemes. For example, a scheme that has hedged its liabilities, and whose employer has remained of the same strength, might see little or no increase.

1.3. Our insolvency risk methodology

1.3.1. We have also reviewed the performance of our insolvency risk model (and other elements of our insolvency risk methodology) and concluded that no significant changes are required.

1.4. SWoSS/ Commercial Consolidators

1.4.1. In recent years we have introduced specific rules concerning the calculation of the levy for schemes without a substantive sponsor (SWoSS) and commercial consolidators. This year we are not proposing significant changes but we do wish to hear stakeholder views on how the levy rules might need to be developed in the future.

1.5. Contingent Assets

1.5.1. We have reviewed our experience of the requirement introduced in 2018/19 for guarantor strength reports to be submitted to us where the anticipated levy benefit was £100,000 or more. While we were satisfied with the rigour applied in most cases, we have revised our guidance with the aim of ensuring that the reports provide a holistic assessment and avoid a tick box approach. We have also clarified our approach to guarantor employers.

1.6. Levy rules from 2021/22

1.6.1. We will be consulting over the next year on the rules that will form the basis of the levy calculations from 2021/22 and later years. Our first consultation will focus on the measurement of insolvency risk and the move to D&B – including providing insolvency risk information through a new portal. We will then consult over the next year on other aspects of the rules.

2. The Levy Estimate and Parameters

2.1 Levy Estimate for 2020/21

2.1.1 We indicated prior to the start of the first levy triennium (which started in 2012/13) that it was our intention for the Levy Scaling Factor and scheme-based levy multiplier that are used in the levy calculation to remain constant through the triennium unless this would result in setting a Levy Estimate outside an acceptable range. This was to provide stability for our levy payers – ensuring the levy would only change in response to movements in the risk presented by their scheme.

2.1.2 2020/21 is the final year of the third levy triennium. Our starting point therefore has been to estimate how much unchanged rules (including a Levy Scaling Factor and scheme-based levy multiplier remaining at 0.48 and 0.000021) will collect in 2020/21. This is what we refer to as the "neutral levy estimate": neutral in that it differs from the previous year's estimate only due to changes in expected scheme funding and insolvency risks. This results in a Levy Estimate for 2020/21 of £620 million, which compares to around £575 million that is being invoiced for 2019/20. We have arrived at the 2020/21 estimate after making assumptions about data which will not be known until April 2020 or later.

2.1.3 The principal reason for our 2020/21 estimate rising above the level we will invoice this year is that scheme funding is expected to have deteriorated due to reductions in gilt yields over recent months. To the extent that liabilities are not hedged, reductions in yields serve to increase the level of schemes' underfunding, which leads to the risk of larger claims on the PPF in the event that sponsors become insolvent.

2.1.4 Additionally, levy collection in 2019/20 is expected to be higher than the published estimate of £500 million as a result of:

- lower than expected funding improvements when new s179 valuations were submitted ahead of the March 2019 submission date; and
- the absence of improved insolvency risk scores, contrary to the experience of prior years.

2.1.5 If our 2020/21 assumptions are realised in practice, then there will typically be a change in the levies charged to individual schemes compared to 2019/20 – in aggregate around an 8 per cent increase. However, the change will depend on the circumstances of each scheme and how their underfunding and insolvency risk has changed. For those schemes that hedge their liabilities – and therefore have seen their funding level unaffected – there may be little or no change in levy unless the scheme's individual circumstances have altered.

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, primarily reflecting legislative restrictions[2], we intended to keep the levy parameters unchanged throughout the third triennium. In 2019/20 our published estimate was £500 million, so that the upper limit on the 2020/21 estimate is £625 million, and our framework does not require a change to the parameters.

2.2.2 We remain on course to reach our funding objective, with an 89 per cent probability of success as at 31 March 2019. Our reserves, which we hold to fund future claims, have decreased in our most recent accounts from £6.7 billion to £6.1 billion. This was largely due to the liabilities brought by the Kodak Pension Plan No.2, the largest claim we have faced to date. This claim has also been the main cause of the 4.2 percentage points reduction of our funding ratio to 118.6 per cent.

2.2.3 However we are aware of several areas of uncertainty that could materially affect our position. In addition to global and UK market uncertainties there are pension specific uncertainties including from court cases regarding the UK's obligation to protect pension incomes in insolvency. These have the potential to affect the risks we face, the level of compensation we pay, and therefore both the level of our funding and future claims.

2.3 Our assumptions for the 2020/21 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 will use for invoicing will be provided up to the end of March 2020 (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 2020.

2.3.2 In setting our assumptions we have adopted the same approach as we took for 2019/20. This is to look at trends in recent years and market data. It is always difficult to judge the setting of individual assumptions, 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 for each of these areas are set out below.

Scheme Funding

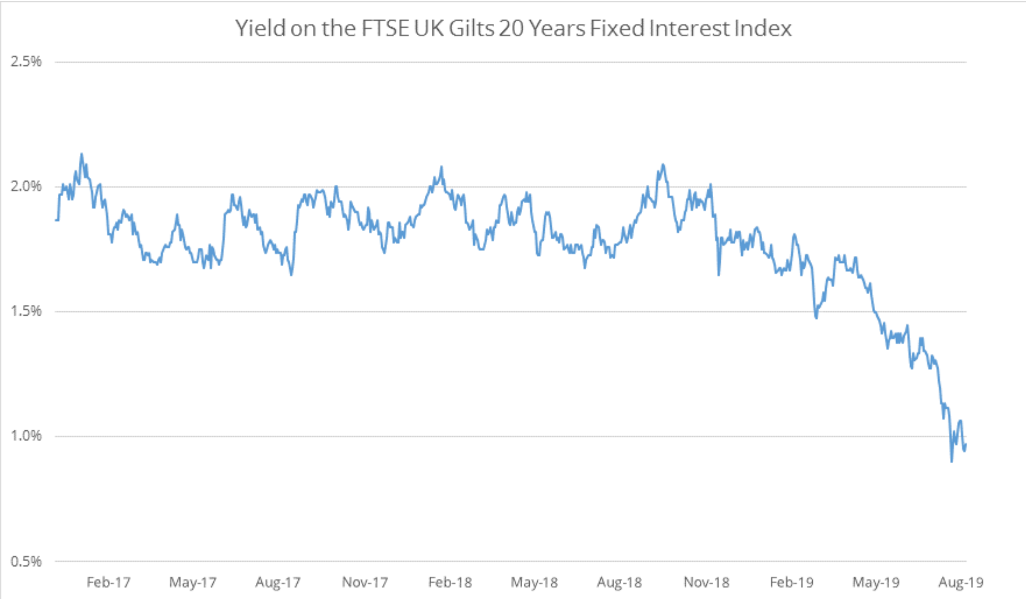
2.3.4 Each year the funding risk of schemes changes as a result of market movements, new accrual and payments to reduce deficits. The assumptions for market movements are

[2] Section 177 of the Pensions Act 2004

particularly important 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. For the 2020/21 levy, this will be the five year period up to 31 March 2020.

2.3.6 In recent months we have seen significant reductions in gilt yields. For example, the yield on the FTSE UK Gilts 20 years Fixed Interest Index (a key measure used in valuing s179 liabilities), has reduced during 2019, with a large reduction over the period May to August. As at August 2019 the FTSE Gilts 20 year index was at around 1.0%, compared to around 1.7% at December 2018.



2.3.7 Lower gilt yields serve to increase schemes' underfunding (to the extent they are not invested in matching assets), producing higher levies. For the remainder of the period to March 2020, consistent with practice in previous years, we have used an assumption for gilt yields that is market consistent. This assumption makes little allowance for a recovery in yields, and produces a five year smoothed position which is expected to increase underfunding, and hence the levy estimate, relative to 2019/20. To the extent that there were a recovery in yields over the period to March 2020 this would reduce collection. Conversely, were yields to fall further this would increase collection. We will monitor this situation up to the point at which we make the final Levy Rules in December, recognising that the period from December to March 2020 will remain unknown at that point.

2.3.8 In addition, we also reflect our experience that when new valuations are submitted, these have historically shown an improved funding position, relative to the previous valuation rolled forward to the new date. For the 2020/21 levy estimate, consistent with our approach last year, we assume the impact will be in line with the average for the last three years.

Insolvency risk scores

2.3.9 The insolvency risk scores for the 2020/21 levy estimate are derived from the Monthly Scores for the 12 months up to 31 March 2019, allowing for subsequent appeals. We have previously seen improvements in scores from year to year, however this trend is no longer visible, so we have assumed no improvement in scores over the period to 31 March 2020.

Risk Reduction Measures

2.3.10 We have assumed that Deficit-Reduction Contributions (DRCs), contingent assets and asset backed contributions will have a similar levy impact as they have had in 2019/20.

2.4 Our Levy Parameters and Levy Estimate for 2020/21

2.4.1 We have reviewed the other levy parameters (for example, the 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 throughout the third levy triennium.

2.4.2 S179 valuations will be converted to a common date of 31 March 2020, using version A8 of our assumptions guidance. Any valuations prepared under version A9 will be transformed back to the A8 assumptions. This is consistent with our normal policy of converting to the same set of assumptions in each year of a triennium.

3. The Measurement of Insolvency Risk

3.1 Introduction

3.1.1. We assess most employers' insolvency risk using the PPF-specific model. This has been developed using the evidence of insolvency amongst the sponsors of defined benefit pension schemes. As this is the final year of the third levy triennium where possible we aim to keep changes to a minimum.

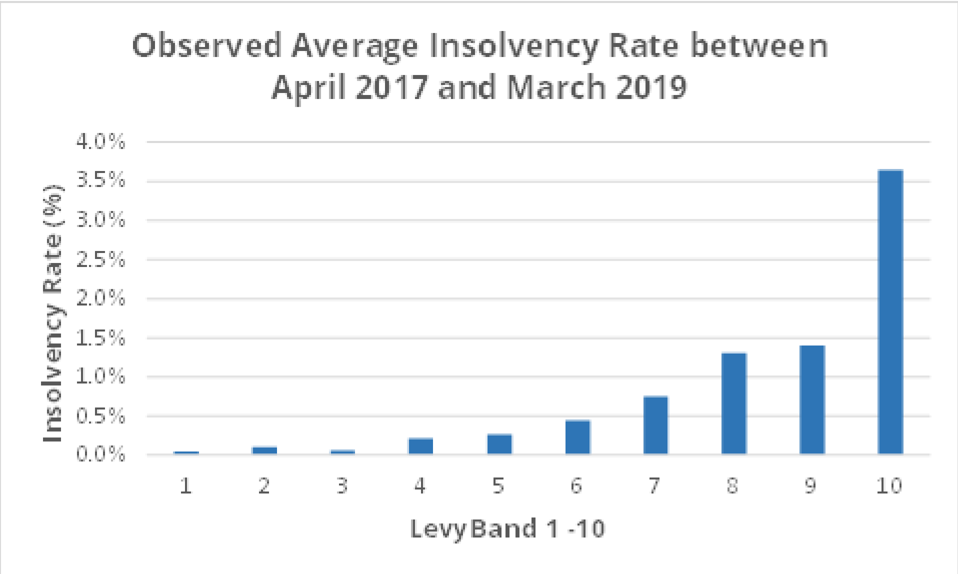
3.1.2 We also use public credit ratings and the S&P credit model (for specified regulated banks, building societies and insurance providers) where appropriate.

3.1.3 Finally we assess a small group of employers who, if they meet certain criteria, can apply to be assessed as special category employers.

3.2. PPF-specific model – overall assessment

3.2.1. We have continued to monitor the performance of the model over the first two years of the third triennium and are satisfied that it remains fit for purpose for 2020/21.

3.2.2. The graph below shows the distribution of insolvencies by levy band over the first two years of the third triennium (up until March 2019). It will be seen that insolvencies are strongly concentrated in the weaker levy bands – with only a handful of insolvencies in the better bands. Experience is comfortably within the 95% confidence interval for expected insolvency experience.



3.2.3. We are not therefore proposing changes to the model or scorecards. We are however completing a review of the model in our work with D&B looking ahead to 2021/22 and later years.

3.3. Comments on the operation of the model

3.3.1. We have had very few comments on specific areas of the model that stakeholders are dissatisfied with. The review of the model at the end of the current triennium will provide an opportunity for a more significant review of any aspects that are causing concern.

3.3.2. One stakeholder has asked us to consider again the potential impact of Guaranteed Minimum Pensions (GMP) equalisation adjustments included in annual accounts[3] on insolvency risk scores in certain very specific circumstances: where the scorecard includes a profit variable (scorecards 1, 2 & 8 only), where the adjustment leads to a company moving from profit to a loss (in and of itself) and where the result was a change of more than one levy band.

3.3.3. In previous years we have rejected requests for a variety of adjustments of published accounts information where it is argued that unadjusted they would not fairly reflect the company's strength. The primary reasons for this are that it could lead to subjectivity in assessing whether a particular adjustment was justified, and so a complex and costly process. It would also weaken the link between the evidence base used to develop the variables (unadjusted) and the results calculated in practice.

3.3.4. At this point we do not have evidence of actual cases that might potentially justify some form of adjustment. We have looked for cases where there has been a movement from profit to loss directly as a result of the impact of GMP equalisation adjustments in accounts and more than a one levy band movement as a result. We are not persuaded that there is a strong enough case for the need and way in which such a certification process could operate. However we are willing to consider evidence from stakeholders who have seen an impact on their score directly as a result of an equalisation adjustment – and what evidence it would be possible to provide to that effect (e.g. a GMP adjustment identified in published accounts / a letter from the company's auditor).

3.3.5. See also section 6 in relation to the impact of GMP equalisation on Section 179 valuations.

3.4. Full and Small Accounts classification

3.4.1. For the 2020/21 rules we are proposing an amendment to the Small Accounts definition in the Determination which means Experian will no longer rely solely on the accounts type indicator to categorise certain accounts types[4] as small. The draft rules provide a mechanism for the PPF to instruct Experian to categorise these accounts as full accounts if the data collected supports this.

[3] GMP equalisation adjustments may be required where a company's liabilities to its pension scheme have previously been understated in the light of the Lloyds Bank court decision –[*Lloyds Banking Group Pensions Trustees Ltd v Lloyds Bank plc and Others [2018] EWHC 2839 (Ch)*] .

[4] The 2019/20 rules deem accounts types 2,3,5,9,E,F,G & Z to be filed as small accounts.

3.5. Use of public credit ratings and S&P credit model

3.5.1. We do not propose any changes to the use of public credit ratings or (with the exception of the recalibration described below) the use of the S&P credit model for 2020/21.

3.5.2. Public credit ratings continue to provide a very strong Gini performance with levels between 93 and 95%[5]. The Gini coefficient shows how well the scorecard differentiates between insolvent and non-insolvent companies - above 55% is considered strong.

3.5.3. The S&P Credit Model is used to score around 70 employers in the banking and insurance sector that do not have a public credit rating. We explained in the 2019/20 Policy Statement that an S&P's annual validation report recognised that the Banks / Building Society model was showing a favourable bias of an average of one notch and that a recalibration to amend this was required. Prior to the recalibration, S&P released their second validation report indicating that the Banks /Building Society model is now showing a favourable bias of an average of two notches. S&P have released a recalibrated version of the model to correct this. Insurance companies are not impacted by these changes. We have conducted a test on our impacted employers and the average change is 1.8 notches. The recalibrated model is due to be rolled out into the PPF universe shortly and it is expected that this will lead to a worsening of scores for some. We will write to employers subject to recalibration before the revised model is put in place.

3.5.4. We stated in the 2019/20 Policy Statement[6] that we would apply the revised scores as soon as they were available and that if the recalibration were not implemented into the model by the end of April 2019 we would recalculate scores for April 2019 and later months after it was.

[5] Based upon reports of the relevant ratings agencies between February and April 2019
[6] Section 3.2

4. Contingent Assets

4.1. Standard forms

4.1.1. In 2019/20 schemes with contingent asset agreements that included a fixed cap element were required to re-execute them on the updated contingent asset forms[7] in order to obtain levy recognition.

4.1.2. We are not aware of any widespread issues that arose for schemes that needed to re-execute in 2019/20. However we would be interested to hear if stakeholders encountered any difficulties.

4.1.3. From 2018/19 schemes with a Type A contingent asset where the levy benefit of the guarantee being accepted by the PPF was £100,000 or more were expected to submit a guarantor strength report that complied with the published guidance. We accepted the great majority of those guarantor strength reports received under the new rules, including all those voluntarily submitted.

4.2. Guarantor strength

4.2.1. We have reviewed the contingent asset guidance in the light of our examination of reports and have made some changes. The revised guidance aims to be more high level – focussing more on the fundamental question of whether the guarantor could be expected to meet the certified realisable recovery. It is therefore less prescriptive in stating what should or could be included in the reports – but, rather, relies on the advisor exercising professional judgement and framing their analysis upon an assessment of the guarantor's financial information in practice, avoiding a more simplistic tick box approach.

4.2.2. However, we do set out within the guidance a (non-exhaustive) list of issues we would expect to see covered in the report. Where the professional advisor considers that any of those issues are not relevant, an explanation of why this is the case should be included in the report. We would also expect the advisor to include consideration of any issues they regard as relevant that might not be referred to in the guidance. We have also taken the opportunity to clarify and refine our requirements relating to the certification of Realisable Recoveries in respect of guarantor-employers, the application of the guarantor-employer component in the levy formula and the levy treatment of guarantors to service companies (see section 7 for more detail).

4.2.3. We would welcome feedback on the changes we have made and whether there is additional guidance we could provide.

[7] First published in January 2018

5. SWoSS and Commercial Consolidators

5.1. Introduction

5.1.1. In recent years we have introduced specific rules upon which to base the levy calculation for schemes without a substantial sponsor (SWoSS) and for commercial consolidators. These were developed to provide a more appropriate levy calculation than the standard rules. The SWoSS rules were developed in 2017/18, and then building on these the consolidator rules were developed in 2019/20 to reflect features of emerging proposals for superfund consolidators.

5.1.2. This is an area that is still evolving and it seems likely that we will need to develop these rules further in future years. For 2020/21 we are therefore not proposing changes this year, but we would be interested in views of stakeholders on how the rules might evolve.

5.2. The 2020/21 levy year

5.2.1. Our guidance on commercial consolidators was set out in the 2019/20 Policy Statement, and will continue to apply in the event of any relevant arrangement arising. We plan to formalise this once the regulatory structure is clearer and we have had more practical experience of these types of arrangements in practice.

5.2.2. We have considered the case for developing the SWoSS and consolidator rules for 2020/21. These were both consulted on for 2019/20, and since the publication of the final rules for that year in December 2018 we have not received any further comment on either rule. We have also yet to have practical experience of considering a superfund consolidator proposal through to the point of making a decision about whether the criteria set out in our policy statement have been met.

5.2.3. Accordingly, given the limited further evidence available to us, we consider that the consolidator rule is broadly fit for purpose for 2020/21. In relation to the SWoSS rule, one area we have considered is the potential for proposals to be brought forward that utilise some elements of the superfund consolidator model, or indeed elements of conventional scheme structures such as group company guarantees, For the short term, there is considerable flexibility in aspects of the rules if a proposition were to emerge and we therefore do not see a clear case for change now.

5.2.4. We would, however, be interested to receive comments on the current rules and any issues we ought to consider.

5.3. Potential development in later years

5.3.1. We are working closely with Government and the Pensions Regulator as they develop a regulatory approach to superfund consolidators that aims to balance protection from the risks of failure with the potential to enhance member outcomes. We are also aware of growing market interest in alternative pension scheme structures such as schemes without substantive sponsors.

5.3.2. Arguably, the nature of the risks SWoSS and consolidators pose to their members and to the PPF are the same: that their funding level falls and they are left with insufficient funds to pay members in full (e.g. because of failures in their investment strategy). And while they may arise in different ways, it is also possible to envisage scenarios in which they are set up in almost precisely the same way, as part of a corporate transaction for example.

5.3.3. A proposition we saw recently demonstrates how similar the two structures can be. This envisaged an SPV employer and a buffer fund held separately from the scheme with the prospect of surplus being returned to the group at a later date. Although our view was that the scheme would have been a SWoSS, the wider protections involved mirrored features of commercial consolidators.

5.3.4. We always anticipated that our SWoSS and consolidator levy rules would need further development as the market develops. In particular, it may be appropriate to bring the separate sets of rules for both more closely in to line. However, given that consolidator models in particular remain very much in development we think changes are better taken forward in a later year, so that they can benefit from greater clarity on the wider environment. In particular, the Department for Work and Pensions (DWP) concluded their consultation on pension scheme consolidation in February this year. We will need to consider their conclusions and any wider regulatory changes that might result, and whether our rules should be amended in the light of wider developments. However, at this point we would be interested in stakeholders' thoughts on the direction of the market and how we should be thinking about developing the rules in the long term.

6. Other issues

6.1. GMP equalisation and s179 Valuations

6.1.1. We published FAQs in December 2018 which confirmed that we expected s179 valuations with effective dates of December 2018 or later to include an assessment of the impact of the Lloyds and Beaton[8] decisions.

6.1.2. The Lloyds decision concerned Guaranteed Minimum Pension (GMP) equalisation, on which a number of stakeholders have raised additional issues. In particular they have raised the time expected to be taken to complete implementation of the decision, the complexity involved in the calculations, whether we could allow or direct some form of standard adjustment, and concerns about certification where an estimated value of additional protected liabilities was included.

6.1.3. Our starting point in considering such requests is that actuaries need to include the value of additional liabilities arising from GMP equalisation in s179 valuations going forward, as the legal position has now been clarified.

6.1.4. Our view is that GMP equalisation is very unlikely to be particularly material to the calculation of total scheme liabilities. It is one of several factors that can change between s179 valuations, and other factors are likely to have significantly larger impacts than GMP equalisation. It is inherent within a 3-year valuation cycle that there will be a certain fluctuation in member benefits reflected in scheme valuations completed on a staggered basis.

6.1.5. We have concluded that it would not be appropriate for the PPF to seek to include an adjustment for GMP equalisation, for example expecting schemes to provide estimated data out of cycle or using a single uniform basis of adjustment. An adjustment would result in some schemes being overcharged and others undercharged.

6.1.6. One particular point of concern raised with us has been that because of the potential complexity of the GMP equalisation calculations, some scheme actuaries would be concerned about providing confirmation that these liabilities are (in the opinion of the actuary) unlikely to have been understated (the principle of prudence contained in the s179 guidance).

6.1.7. We have published an information note for actuaries preparing s179 valuations. This confirms, amongst other aspects of the calculation principles, that an interim allowance for GMP equalisation (where such equalisation has not yet been implemented) may, in isolation, be calculated on a best estimate basis. It should be noted that the principle of prudence continues to apply to all other elements of the protected liabilities, without relaxation.

[8] *Beaton v the Board of the Pension Protection Fund* [2017] EWHC 2623 (Ch)

6.1.8. The information note also sets out that, where an interim GMP equalisation allowance in a s179 valuation has been calculated on a best estimate approach, the actuary should amend the certification to the trustees to reflect this and may refer to the relevant provisions of the information note. The s179 certification wording on Exchange is standardised and will continue to confirm that the protected liabilities are (in the opinion of the actuary) unlikely to have been understated. However, actuaries submitting s179 valuations on Exchange may rely on the status of the information note (in particular, the best estimate provisions for interim GMP equalisation allowances) as s179 guidance to supplement version G8 of our s179 valuation guidance.

6.1.9. More broadly we note that the cross industry GMP Equalisation Working Group (GMPEWG) is developing guidance in a range of areas and we hope this will help schemes apply the decision to their specific circumstances.

6.2. Hampshire and Bauer judgments

6.2.1. Our FAQs published in December 2018 confirmed our interim position with respect to s179 valuations following the judgment in the Hampshire[9] case by the European Court of Justice. We advised that valuations should continue to be carried out under version G8 of our s179 valuation guidance, and no additional allowance should be made as a result of the Hampshire judgment.

6.2.2. We have subsequently been working through the impact of the judgment, but our interim position is unchanged. The exact mechanics of how the judgment translates to PPF compensation levels (and hence s179 liabilities) remain unclear, due to ongoing uncertainty following various court actions. However, we anticipate that the impact will be marginal in all but a minority of cases.

6.2.3. In view of these factors, and until we have sufficient clarity to be able to set out a robust methodology in guidance, we consider that the current approach of no additional allowance in s179 valuations continues to be the most appropriate.

6.2.4. We are also following progress of the German case, PSV v Bauer at the European Court of Justice (CJEU). In this case, the court is considering the scope and interpretation of Article 8 of the Insolvency Directive 2008/94/EC on the protection of employees in the event of the insolvency of their employer, including under what circumstances the losses suffered by employees could be considered to be manifestly disproportionate.

6.2.5. The Advocate General in Bauer[10] has delivered an opinion that EU member states are required to establish systems that aim to protect pensions in full. This view is a significant departure from previous rulings which recognise a member state's considerable discretion to determine their approach to pension protections (balancing the level of compensation provided with the cost of doing so). If the court rules in line with the Advocate General's view that would imply a significant shift in that balance, a situation that would need very careful consideration by Government. However, it is important to

[9] *Hampshire v Board of the Pension Protection Fund* [2019] ICR 327, (Case C-17/17)

[10] Opinion of the Advocate General Hogan in *Pensions-Sicherungs-Verein VVaG v Günther Bauer* (Case C-168/18) of 8 May 2019

stress that the court has not yet ruled and a range of outcomes are possible (including that the status quo is retained).

7. Draft Levy Rules 2020/21

7.1. Introduction

7.1.1. This section summarises changes we have made to the Determination, Appendices and guidance, some of which are not covered elsewhere.

7.2. Determination, Contingent Asset Appendix, and Contingent Asset Guidance

7.2.1. **Submission of hard copy contingent assets:** submissions should now be addressed to the Levy Operations Team.

7.2.2. **Insolvency of guarantor-employers:** We have clarified that trustees should consider whether the immediate insolvency of all the employers other than the guarantor would be likely to precipitate the insolvency of the guarantor-employer itself. Where this applies and the guarantee ranks commensurately with the s75 debt, the Realisable Recovery should be reduced to reflect any consequent reduction in the anticipated recovery of the s75 debt from the guarantor-employer.

7.2.3. **Application of the guarantor-employer component in the levy formula:** We have clarified that the existence of a valid Guarantor Strength Report does not preclude us from considering the application or disapplication of the guarantor-employer component on its own merits, and that the component will be automatically dis-applied if the trustees have certified only a zero Realisable Recovery or Recoveries in respect of the guarantor-employer.

7.2.4. **Service Companies:** We have introduced a definition of Service Company and clarified that the existence of a valid Guarantor Strength Report in respect of such a guarantor does not preclude us from considering the contingent asset on its own merits. In addition, clarification of our expectations when considering Service Companies in the context of assessing certified Realisable Recovery have been added to Part 2 of the Contingent Asset Guidance.

7.3. Transformation Appendix

7.3.1. We have amended the references to the IPD property indices (used in the asset return roll up) to reflect the rebranding to MSCI property indices. We understand from MSCI that the composition and calculation of the relevant indices and benchmarks remains unchanged, and therefore there is no impact on levy amounts.

7.4. Insolvency Risk Appendix

7.4.1. **Recalibration of Credit Model:** We have included wording to reflect that we will apply the anticipated recalibration of the S&P Credit Model to scores from April 2019, once that recalibration has been applied to the Credit Model. We have also made the corresponding necessary minor change to the Levy Rules.

7.4.2. **Equity Gearing Definition:** We are correcting the description of this calculation. The revised wording is consistent with the basis on which the calculation has been and will continue to be calculated and displayed in the portal (including through the what-if tool). Scores will not change as a result.

7.4.3. **Identification of entities for the purpose of assignment to Group category:** We have clarified the process to be carried out by Experian in identifying entities that form part of a Group, for the purposes of calculating the parental strength variable, by stating that Experian should carry out the process in line with their ordinary course of business or by using reasonable practical endeavours.

7.4.4. **Return on Shareholder Funds:** We have removed a redundant reference to Return on Shareholder Funds, originally retained for information only.

7.5. Measurement Time in 2020/21

7.5.1. We are proposing to maintain the standard Measurement Time for the online submission of scheme data of midnight at the end of 31 March 2020. The measurement time for hard copy contingent asset documents to be received by the PPF is proposed as 5pm on 31 March 2020.

7.5.2. The Measurement Time for certification of deficit-reduction certificates is 5pm on 30 April 2020 and for block transfers 5pm on 30 June 2020.

8. Consultation Arrangements and Key Dates

8.1. 2020/21 Consultation

8.1.1. The consultation on the 2020/21 Levy Rules runs from 25 September 2019 to 5pm on 5 November 2019. Please ensure your response reaches us by the deadline. Submissions may be made by email or post, using the details below.

Email: consultation@ppf.co.uk

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

8.1.2. 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.

8.1.3. 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 data for the purpose of the public consultation exercise, it is understood that a respondent consents to its disclosure and publication.

8.1.4. 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 GOV.UK website:

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

8.1.5. A summary of responses and the Board's final Determination and confirmed policy will be published on the PPF website at:

https://www.ppf.co.uk/

8.2. Key Dates

8.2.1. 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 31 March 2020, except as detailed below.

Item	**Key dates and times**
Monthly Experian Scores, Credit Ratings and S&P Credit Model scores to be used in the 2020/21 risk-based levy	Between 30 April 2019 and 31 March 2020
Deadline for providing updated information (to Experian) to impact on Monthly Experian Scores	One calendar month before the relevant Score Measurement Date
Submission of scheme return data on Exchange	Midnight on 31 March 2020
Reference period over which funding is smoothed	5 year period to 31 March 2020
Certification of contingent assets	Online by midnight 31 March 2020, hard copy documents by 5pm 31 March
Certification of asset-backed contributions (e-mailed to the PPF)	By midnight on 31 March 2020
Certificates impacting Monthly Experian Scores – mortgage exclusions, employee information, FRS 101/102 certificates-(emailed to Experian)	By midnight on 31 March 2020
Applications for Special Category Employer Status	By midnight on 31 March 2020
Certification of Deficit-Reduction Contributions	By 5pm on 30 April 2020
Applications for Exempt Transfers	By 5pm on 30 April 2020
Certification of full block transfers	By 5pm on 30 June 2020
Invoicing starts	Autumn 2020

8.3. Comments on the Consultation Process

8.3.1. The consultation is being conducted in line with the Cabinet Office's Consultation Principles:

https://www.gov.uk/government/publications/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.co.uk

Deadline for consultation responses is 5pm on 5 November 2019