

# 2020/21 PPF Levy Policy Statement

## 1. Introduction

- 1.1. Our consultation on the Levy Rules for 2020/21, published on 25 September 2019, closed on 5 November 2019. Proposals for changes to the rules were extremely limited, as 2020/21 marks the final year of a three-year period during which we have sought to maintain stability in rules.
- 1.2. We received a total of 15 responses. These were considered by the Board in determining the final Levy Rules. This document summarises the responses we received, our analysis of the issues raised and conclusions reached.
- 1.3. The Levy Rules that will govern the calculation of the levies for 2020/21, as specified in the Board's Determination under section 175(5) of the Pensions Act 2004, are published alongside this Policy Statement. Together with the Levy Rules we have published guidance for schemes on how to meet the requirements of the Levy Rules, and to explain how we expect to make use of the areas where the Levy Rules provide us with flexibility. We are also publishing updated certificates.
- 1.4. In the Consultation Document we proposed maintaining a Levy Scaling Factor ('LSF') of 0.48 and Scheme-based Levy Multiplier of 0.000021. We also announced that the Levy Estimate – the amount we estimated these parameters would raise – was £620 million for 2020/21.
- 1.5. We received three responses mentioning the levy estimate, all of which were generally supportive of the principle to maintain stability of the levy rules and parameters during a triennium.
- 1.6. We have kept our levy estimate under review since October, in the light of factors that might cause it to alter (such as market movements and changes in insolvency risk) but have concluded it remains appropriate. Accordingly, we are now confirming that for 2020/21 we will use the LSF of 0.48 and the Scheme-based Levy Multiplier of 0.000021, and confirming the Levy Estimate of £620 million.
- 1.7. The European Court of Justice will shortly be delivering its decision in the German case known as 'Bauer'<sup>1</sup>. The case relates to the level of protection member states must provide for employee pensions in the event of employer insolvency. The judgment could have a financial impact on the PPF. However, we are not delaying publication to wait for the judgment. Even if there is an impact which makes a case for increasing the levy, there is very limited scope to do so for 2020/21 - as the Levy Estimate is only slightly below the maximum the Pensions Act allows us to set relative to the previous year's estimate.

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<sup>1</sup> Pensions-Sicherungs-Verein VVaG v Bauer (Case C-168/18)

## 2. Insolvency Risk

### PPF-specific model

- 2.1. We received very few responses concerning the operation of either the scorecards or variables. We will respond individually regarding any issues not covered below.

### GMP equalisation and impact on Monthly Scores

- 2.2. We sought views on the impact of GMP equalisation adjustments on PPF-specific model scores, in response to concerns raised in our SME Forum. We received seven responses broadly supportive of action (though we were given evidence of only one case impacted in practice).
- 2.3. Theoretically, taking account of GMP equalisation costs in accounts can lead to changes in levy. However, movements in the degree of profit reported are very unlikely (in isolation) to have an impact. Scores are, however, more sensitive for movements from profit to loss. In principle, therefore, where GMP equalisation costs move an employer from profit to loss this could generate a move of up to two levy bands. However, from the analysis we have done it is clear that such circumstances will probably only arise in a very small number of cases – we have only found one employer so significantly affected and while this number may grow as further accounts are filed, we expect numbers will stay very small.
- 2.4. Even so, despite very limited numbers, we consider there is a case for adjusting our insolvency risk calculation in the most affected cases. First, the impact on individual scheme levies (likely to be schemes sponsored by SMEs) could be significant and there is a reasonable argument that a profit charge in one year for increased costs which will actually be met over a number of years doesn't affect insolvency risks substantially. We also appreciate that the impact of GMP equalisation may be seen in our assessment of underfunding risk in some cases.
- 2.5. We will, therefore, allow employers to request an adjustment providing all the following conditions apply:
  - a specific amount can be identified in accounts used to calculate one or more Monthly Scores that solely relates to a GMP equalisation adjustment
  - allowing the adjustment would result in the company being viewed as reporting a pre-tax profit rather than a loss
  - allowing the adjustment would result in a change of Mean Score to a Levy Band with a lower Levy Rate
- 2.6. We would emphasise that this does not mark a general departure from our view that information as reported in accounts should be used in scoring. We will produce a simple form – with guidance on how to complete – to help guide levy payers through providing appropriate evidence. Requests should be made within 28 days of Mean Scores being published (which we expect to be in early July-2020).

### Full and small accounts

- 2.7. We received two responses on our proposed change to the small accounts definition. One response from scheme advisors welcomed the change, suggesting it would reduce the need for appeals. The other asked us to alert affected schemes to the change and to confirm that schemes would retain the normal right to appeal. We are confirming this change and we are writing to any schemes where employers change scorecard explaining why that is happening. Schemes' right to appeal their Mean Score is unaffected.

## S&P Credit Model

- 2.8. The S&P Credit Model is an 'off-the-shelf' proprietary model that we use to score banks and building societies without a credit rating and as such it is expected that it will require periodic recalibration to ensure it remains effective.
- 2.9. We indicated in the 2019/20 Policy Statement (December 2018), and again in our consultation document, that the S&P Credit Model was being recalibrated and that the recalibrated scores would be used as soon as they were available or from April 2019 if that was earlier.
- 2.10. The revised scores are expected to be available in the portal by the end of January. As previously explained, these recalibrated scores will be used from April 2019 in the calculation of Mean Scores for 2020/21. We believe it remains right to implement recalibration from April 2019 as this reflects the best view that S&P have of the strength of the assessed company - otherwise we would be scoring banks more favourably than is justified by the evidence.

## 3. Contingent Assets

### Guidance on Guarantor Strength Reports

- 3.1. Alongside our 2020/21 draft rules we published updated guidance on Type A contingent assets and in particular on guarantor strength reports, which are expected for contingent assets that result in a levy saving of £100,000 or more if accepted.
- 3.2. The thrust of the changes was to discourage a "tick box" approach in assessing the ability of the guarantor to meet the amount guaranteed, and instead to promote an approach which relies on the professional advisor's judgement.
- 3.3. We received 11 responses which were broadly positive about the direction of travel of the guidance – with a number of detailed points being raised. We have accepted several of the suggestions made including the following.
- 3.4. We have revised the wording in several parts where inadvertently there was a risk of an unnecessarily prescriptive approach being suggested (for example changes of 'must' to 'should' and 'will' to 'may'). Broadly, our view is that the guidance ought to be followed except where there is a good reason for doing something different – and then that the different approach should be justified.
- 3.5. Some responses suggested that the requirements for guarantor strength reports had become too onerous and might discourage their creation and/or certification. Subject to avoiding an overly prescriptive approach as explained above we think that the requirements are reasonable, particularly in the light of the significant levy savings that can be achieved (i.e. over £100,000 in levy)
- 3.6. We received comments about the parts of the guidance dealing with the likely circumstances of a service company insolvency. The premise of the guidance is that service company insolvency is most likely where the company it provides services to becomes insolvent. Where that company is the guarantor, it is therefore necessary to assess whether the guarantee can be met if the guarantor is insolvent. A small number of respondents queried whether this is always the most appropriate assumption. We have not significantly changed our drafting as we think that it adequately covers the typical arrangements we see. We accept, however, that there may be particular circumstances

which could make an alternative assumption reasonable. The guidance does not prevent this but if an alternative assumption is used we would expect to see a clear explanation of why it is appropriate.

- 3.7. We have clarified the wording of certain parts taking account of feedback received (e.g. our explanation of guarantor obligations).

#### Contingent assets – other issues

- 3.8. We requested feedback on whether any difficulties had been encountered in the re-execution process and certification where this was necessary to obtain credit for 2019/20. No significant issues were reported and this is consistent with our own experience in 2019/20.
- 3.9. We have decided to use the equivalent of the hard copy deadline for contingent assets that we used in 2019/20. Therefore the hard copy deadline will be 5.00pm on 1 April 2020.

## 4. Other issues

### Levy for commercial consolidators and schemes without a substantive sponsor

- 4.1 We explained the basis on which our policy and rules had developed with respect to SWOSS and Commercial Consolidators and requested feedback. The responses we received did not suggest a need to alter the rules in the short-term. There was agreement that the development of regulation and experience of transactions should help inform the development of the rules in the future.

### Comments on the PPF's GMP equalisation information note

- 4.2 Although not part of the formal consultation package, we were pleased to receive a number of helpful observations on the information note we published to help schemes preparing to submit s179 valuations. We have taken this opportunity to reissue the information note incorporating a few clarifying amendments.

### Other drafting changes

- 4.3 We have also made a number of minor drafting changes to the levy rules and guidance with the intention of clarifying how we expect the rules to operate:
- a) We have updated, where relevant, date references to account for the leap year (29 February 2020) and to extend the date for submission of information to the last working date of the month.
  - b) We have updated references to the Solicitors Regulation Authority (SRA) requirements in relation to professional indemnity insurance to reflect the changes that came into effect on 25 November 2019.

## Pension Protection Fund

16 December 2019