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22 October 2013

Chris Collins
Chief Policy Adviser
Pension Protection Fund
Knollys House
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Dear Mr Collins

THE 2014/15 PENSION PROTECTION LEVY

I am writing on behalf of the Association of Consulting Actuaries (ACA) in response to the consultation document issued in September 2013 containing proposals for the 2014/15 Pension Protection levy.

We welcome the PPF's proposed approach for 2014/15, maintaining stability in methodology and therefore predictability of the levy. The approach appears reasonable, based on the information available. We also welcome your early publication of guidance, allowing time for stakeholders to comment. Our detailed response to your specific questions and our comments on some further issues are set out in the appendices to this letter.

We hope that you find our comments of assistance and would be happy to discuss them further if that is helpful. You can contact me on 020 7432 6635 (david.everett@lcp.uk.com), or my colleague Peter Williams on 01372 733 763 (peter.williams@aonhewitt.com).

Yours sincerely

David Everett

David Everett
Chairman
ACA Pension Schemes Committee

Sent by e-mail to consultation@ppf.gsi.gov.uk

APPENDIX A: ACA RESPONSES TO SPECIFIC QUESTIONS

Question 1*: Do you agree with our proposal to allow recertification where certification or recertification has occurred not more than five levy years previously?*

Yes. This is a welcome simplification which does not impact on the risk posed to the PPF.

From a practical perspective, there were particular difficulties for this year's levy because a recertification could not be submitted on Exchange until March 2013. The option to submit a recertification should be made available as early as possible following publication of the final Determination.

Question 2*: Do you agree with the proposed re-wording of the trustees' certification? Would you favour implementation of a change of wording in 2014/15 or prefer a delay to 2015/16?*

The changes you have proposed to the trustees' certification do appear to be a marginal improvement but this is a legal issue. We have a slight preference that any change be deferred until 2015/16 to tie in the other (possibly more substantial) changes. This will avoid making a third change in three years in this area and we are aware that some legal advisers are suggesting that the new wording could require additional work.

Question 3*: We would welcome suggestions or comments on our proposed approach in relation to the "Bridge" case. We would also welcome comments on the impact of such an approach.*

Whilst we understand the PPF's desire to ensure that schemes pay a fair levy based on the revised definition of money purchase benefits, it is difficult to comment on the proposed approach given the lack of detail about how it would work and the current uncertainty around the underlying legislation. The PPF needs to ensure that its approach does not impose onerous requirements on schemes or require schemes to take actions at short notice that would be disproportionately costly compared with the amount of any increased levy income to the PPF. For example:

- Many existing schemes will be affected but only to a very limited extent. In particular, schemes that are predominantly defined benefit but convert money purchase funds (such as AVCs) to pension within the scheme will see a small increase in their section 179 liabilities as a result of the Pensions Act 2011 changes, but a corresponding decrease in their underfunding risk, as the assets will increase by more than the liabilities, assuming that paragraph 5.3 of G5 no longer applies. It would seem impractical to recalculate levies for these schemes.

- For existing schemes where there would be a sizeable increase in section 179 liabilities and schemes that previously were not required to pay a levy the PPF needs to give a reasonable amount of time for the scheme to provide information, and ensure that the costs incurred (eg carrying out a new section 179 valuation) are necessary by reference to the change in levy. We suggest that the PPF should not require section 179 valuations to be carried out at short notice – it may be reasonable for the PPF to set a deadline of 31 March 2015, say (depending on when the new legislation is finalised) for schemes that were not previously required to pay a levy.

From a practical point of view, it may be more efficient for the PPF to wait until existing schemes are required to submit their next section 179 valuation, after a future date – 31 March 2015 say – as it may take them some time to understand the new legislation and its precise impact. We also expect the PPF to provide new guidance and respond to queries promptly, as there are likely to be a range of new benefits to be valued that are not covered by the existing guidance.

Levies could be recalculated retrospectively once the new valuation has been submitted. However, the PPF should set clear rules now as to which schemes will have their levies recalculated based on a future submission.

The PPF should also clarify whether levies will be (re)calculated in respect of years prior to 2014/15 if the legislation is retrospective. We would question whether this is necessary.

***Question 4**: Please include any comments on the draft guidance with your response to the consultation, distinguishing clearly between comments on the consultation and those on the guidance.*

On the Contingent Asset Guidance, it is important that final guidance is published in 2013, with no variations being made to the "final" guidance in early 2014. In addition, the term "full commitment" as used in the certification needs to be clearly defined, so that trustees know what they are certifying. We think it would be helpful to give trustees flexibility here and define "full commitment" as either the estimated section 179 deficit at the certification date (ie the same as the 2013/14 certification), or the stressed and smoothed deficit used for the 2014/15 levy calculation (ie the test used by the PPF, as set out in 5.2 of the draft guidance). This would enable schemes to align their certification with the PPF's assessment, without requiring them to (if, for example, the figures are not readily available).

We note in passing that paragraphs 5.2.3 and 5.2.4 look new compared to last year and would seem to set a higher bar – it now not being good enough for the guarantor to be able to meet the guarantee; it needs also to be able to continue to trade.

We are not sure whether the example in paragraph 5.1.21 remains appropriate given the new positive form of certification (the last sentence uses the old “no reason to believe” wording). Might there be situations in which the trustees could now certify £80m? We suggest that you revisit this example.

We have noted a number of typos and paragraph mis-references which no doubt will be addressed in the final guidance.

We have one comment on the Levy Practice Guidance: for new example 2 (page 8) to be correct, it needs to be made clear that the value of the annuity holding is included in the asset value shown in the scheme accounts. Many schemes do not include the value of an annuity policy in their accounts, and in such cases it would be correct to show a 0% holding in the asset allocation, as the annuity policy is taken account of in the levy calculation by virtue of the field "Proportion of assets held in the form of insurance contracts not included in scheme accounts" in the section 179 valuation certificate. The guidance should clearly differentiate between the two methods of recording annuity policies in scheme accounts.

We have no comments on the guidance for block transfers and the guidance for the bespoke stress calculation.

APPENDIX B: ACA COMMENTS ON OTHER ISSUES

__1__ Actuarial Certificate of Deficit Reduction Contributions (ACDRC)

Firstly, it would be helpful if an ACDRC could be submitted at any point in the year, not just after the final Determination is issued. This would ensure that the work could be completed at the most efficient time, rather than imposing an unnecessary restriction.

Secondly, the PPF should amend and/or clarify its position in relation to the treatment of the following for ACDRC purposes:

- Contributions that are used by the trustees to purchase an interest in a Special Purpose Vehicle;
- Assets, such as gilts, that are re-designated directly to the scheme (rather than the scheme receiving a contribution which it uses to purchase the assets).

In particular, we ask that the treatment of these assets/contributions for ACDRC purposes is consistent with that for section 179 valuation purposes.

Such assets are valued in the scheme's audited accounts and therefore included in the scheme's asset value for section 179 valuation purposes. In most cases they become an asset of the scheme as a result of an amount which is shown as a contribution in the accounts (even though it may not be an actual cash payment). We therefore ask that such contributions can be taken into account for ACDRC purposes for consistency. We also note that they clearly fulfil the underlying ACDRC requirement in Levy Rule G1.1(iii) of "reducing the difference between the scheme’s assets and protected liabilities, or increasing the difference where the scheme is in surplus". We see no reason why they should not be taken into account.

In particular, we are confused by various comments in the PPF's FAQs dated 4 March 2013, which suggest that the PPF requires a contribution to be a quantifiable cash payment in order to be taken into account for ACDRC purposes. We are unsure why the "cash" requirement has been introduced. The definition of "Deficit-Reduction Contribution" was amended in the 2013/14 Determination to include the word "cash", which did not appear previously and does not appear anywhere else in the Determination or the ACDRC Appendix. We ask the PPF to clearly explain the reason for this change (if it is not reversed), as it has not previously done so.

There is an implicit suggestion in these FAQs that the scheme actuary needs to analyse any amounts shown as a "contribution" in the scheme's audited accounts and only take into account actual "cash contributions" for ACDRC purposes. If this really is what the PPF intends, then it needs to make this much clearer in the Levy Determination, as it is not usual for the actuary to question the value or type of contributions shown in the scheme's audited accounts.

__2__: Areas where the policy intent or wording is unclear or inconsistent

The PPF should review its requirement for a block transfer certificate to be submitted in cases where there is fundamentally no change in the risk posed to the PPF. This most commonly occurs where a single-section scheme has transferred in its entirety to a newly-created segregated section of another scheme, such that the liabilities in the new section of the receiving scheme are exactly the same the day after the transfer as the liabilities of the transferring scheme the day before the transfer.

In our view, submission of a block transfer certificate in such cases is unnecessarily onerous, as we see no reason why the previous section 179 valuation of the transferring scheme cannot be used as the basis for calculating the levy for the new section of the receiving scheme (ie without applying the poor data methodology). We ask the PPF to consider introducing a less onerous form of notification in such cases. For example, the trustees or actuary of the receiving scheme could confirm that a single-section scheme has transferred in its entirety to a newly-created segregated section of their scheme which has been set up solely for the purpose of receiving only those liabilities. This will allow the most recent section 179 valuation of the transferring scheme to be used until the new section completes its own section179 valuation, without any loss of levy income for the PPF.

About the Association of Consulting Actuaries (ACA)

Members of the ACA provide advice to thousands of pension schemes, including most of the country's largest schemes. Members of the Association are all qualified actuaries and all actuarial advice given is subject to the Actuaries' Code. Advice given to clients is independent and impartial. ACA members include the scheme actuaries to schemes covering the majority of members of private sector defined benefit pension schemes.

The ACA is the representative body for UK consulting actuaries, whilst the Institute and Faculty of Actuaries is the professional body.

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