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13 November 2014

Chris Collins
Chief Policy Officer
Pension Protection Fund
Renaissance
12 Dingwall Road
Croydon, Surrey
CR0 2NA

Dear Mr Collins

The 2015/16 Pension Protection Levy Consultation

I am writing on behalf of the Association of Consulting Actuaries (ACA) in response to the above consultation document issued on 6 October 2014.

We broadly welcome the PPF's levy proposals for 2015/16. Most of the changes proposed following the previous consultation are sensible although we have some concerns about the treatment of Type A contingent assets in particular. Our comments on the specific questions you raised are set out in Appendix A. Our wider comments are set out in Appendix B.

We hope that you find our comments of assistance and would be happy to discuss them further if that is helpful. Please contact either me on 020 7432 6635 (david.everett@lcp.uk.com) or my colleague, Peter Williams on 01372 733763 (peter.williams@aonhewitt.com) who prepared the response.

Yours sincerely

David Everett

David Everett
Chairman
ACA Pension Schemes Committee

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

APPENDIX A

ACA'S RESPONSES TO SPECIFIC QUESTIONS

Mortgage Age

Question 1*: What evidence is available to assess how best to judge whether a mortgage or mortgages is/are clearly immaterial?*

No comment.

Question 2*: Are there other factors that we should consider?*

We note that the criteria for assessing whether a mortgage refinancing is on the same or better terms are very limited. It is possible for a refinancing to lead to lower risk even if one of the criteria is not met – for example a longer debt tenor bringing longer term certainty even if at a higher interest rate. Also a higher nominal interest rate may not be a worse outcome if the margin above base rates is the same.

Question 3*: What are your views on the proposed limits and the exclusion of all entities with a CR?*

It is not clear how the proposed limit of 0.5% of total assets has been derived. However, we have not proposed any evidence to assess materiality and the proposed limit is not obviously inconsistent with your stated objective of identifying only the most clearly immaterial items – so that charges are not excluded if there is an element of doubt.

The logic you have set out in paragraph section 15.3, for excluding mortgages relating to employers with investment grade credit ratings, appears reasonable.

Question 4*: Do you have any other comments on the certificates published on the PPF website and the process for certifying secured charges for exclusion from the mortgage age variable?*

No.

APPENDIX B

ACA COMMENTS ON OTHER ISSUES

Asset backed contributions

We welcome the change to the consultation proposal that would have restricted the recognition of ABC arrangements to UK property only. However, we have some further comments:

- We are concerned about the comments in paragraph 7.6.2, which suggest the creation of a duty of care between the trustees' advisers and the PPF. We are surprised at this change and would prefer to maintain the existing chain of accountability through the trustees. As a minimum, the maximum extent of any liability would need to be made clear. Typically, there is a liability cap in the agreement between advisers and trustees. It would not seem appropriate for advisers to have an uncapped liability to the PPF.

- The guidance should explicitly acknowledge that there is not an expectation of any joint and several liability under a duty of care across advisers, particularly where some advisers may use other advisers' work (e.g. incorporating a valuation specialist's results into a wider report on the ABC value).

- Where a "Partial ABC Certificate" is being submitted, we believe that this should include "ABC Payments" made up to 31 March 2015, rather than the date of the latest Scheme Accounts. If no other value is applied to such payments (because the scheme does not wish to calculate the "ABC Value"), it is appropriate to give such Coupon Payments recognition in the levy calculation as they are a genuine cash sum that the trustees can invest. To ignore such payments would be inconsistent with the treatment of Deficit Reduction Contributions.

- It does not seem right that a stress is applied to the insolvency value of the ABC asset rather than the underlying asset before the scheme's interest on an insolvency basis is assessed.

- The automatic exclusion of loan-based ABCs if not secured on an underlying asset seems incongruous with the rigour in the ABC certification process and the parallels that can be drawn with the process being introduced for type A contingent assets. Any valuation would reflect the fact that the loan is unsecured, forming a view on the realisations that may be achieved in an insolvency, whilst still allowing for structural sub-ordination that is typically adopted that can give the same effect as granting formal security.

The ABC guidance and certificate should clearly set out the submission requirements once these are finalised. The only reference in the draft documentation appears to be A2.2(4) of the Determination, which is difficult to find.

Block transfers

We note that the formula in paragraph 13 of the Transfers Appendix refers to 28 June 2013 rather than the correct date – 30 June 2015. (This error was also contained within the final version of the Appendix for the 2014/15 levy year.)

We repeat our request from previous years for the PPF to 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 section 179 valuation, without any loss of levy income for the PPF.

Contingent assets

We continue to have a number of concerns about the proposed adjustment of the Guarantor's levy band:

- You have now presented a different analysis of how gearing affects insolvency from that shown in the original consultation. We are concerned that neither of these shows a particularly strong link to the adjustment to levy calculations that is proposed.

- More importantly, we are concerned that the adjustment of the Guarantor's levy band is a different way of assessing the Realisable Recovery, and therefore there is an element of double counting here, as presumably the impact on gearing will be an element of the analysis in the certification of the Realisable Recovery. If the Realisable Recovery is certified correctly (ie the trustees have carried out detailed analysis to conclude that the Guarantor has a high probability of being able to pay this amount) it is not at all clear to us why the insolvency probability of the Guarantor should be arbitrarily increased on the basis of one factor in this analysis. This is effectively saying that, despite the detailed analysis, you are going to assume that the Guarantor automatically has a lower probability of being able to pay the Realisable Recovery.

- We are also concerned by your approach to consultation in this area. The original analysis outlined an approach that suggested adjusting the Experian score. Paragraph 8.2.13 of the current consultation suggested that most respondents also favoured this approach, but yet you now appear to be proposing a completely different approach (ie adjusting the Levy Band) without any further consultation.

We welcome your acceptance of surety bonds as a Type C(ii) contingent asset.

Deficit reduction contributions

We assume that paragraphs 10 and 12 of the DRC Appendix should refer to version A7 rather than A6 of the assumptions guidance for consistency with other areas of the Determination (notably the Transformation Appendix), and paragraph 11.5.1 of the consultation document.

Experian issues

Experian does not seem to have any scope to apply interpretation if the information in the accounts is not clear. For example, we are aware of a case where “Capital Employed” and “Current Liabilities” are not defined. Experian hence cannot calculate (or approximate) a Capital Employed figure and so have set it to zero which is very unfavourable. We ask that consideration is given to enabling Experian to use its judgement to approximate data items if the PPF definitions clearly do not work and a zero entry is clearly wrong.

We are finding that the Experian scoring system gives rise to a number of odd (presumably unintended) situations. For example, an employer which is a holding company (and hence has nil employees), currently being scored under the Group >£50m turnover and which is in levy band 4. The company is being scored based on “average remuneration per employee” of nil/nil, but if that company had one employee receiving £40,000, its levy band would move from 4 to 1. That does not seem right.

“Full accounts” definition

There are two different definitions of “Full accounts”.

The one in the Determination is:

> *“Individual Accounts which are not Consolidated Accounts and contain a balance sheet and profit and loss account”.*

The one in the Insolvency Risk appendix is

> *“Whether an Employer's Latest Accounts are deemed to be Full Accounts is assessed as follows:*
>
> *(a) subject to (b) below, by reference to the account type indicator which is delivered to Experian by Companies House or, in the absence of such indicator, an Employer will be deemed as filing Full Accounts if its accounts show a Turnover figure;*
>
> *(b) where Rule E2.4(2)(c) has applied for the purposes of the 2015/16 Levy Year, but has not applied in any subsequent Levy Year, the Employer concerned will, nonetheless, be categorised for the purposes of any subsequent Levy Year as follows:*
>
> *(i) Group <£10m in the case of an Employer which is part of a Group; or*
>
> *(ii) Independent Full in the case of an Employer which is not part of a Group.[1]”*

But the actual definition used by Experian appears to be a combination of the two (ignoring (b) which is not to be used for the 2015/16 levy year). Please can you revisit.

Last man standing deadline

The deadline for confirming last man standing status is 31 May 2015, which is a Sunday. In keeping with your normal practice we would have expected the deadline to be brought forward to a working day.

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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