

GN19: Retirement Benefit Schemes - Winding-up and Scheme Asset Deficiency

Classification

Practice Standard

Legislation or Authority

Pensions Act 1995 (c.26) ('the Act'). Sections 73 and 75.

The Occupational Pension Schemes (Winding Up) Regulations 1996. SI 1996/3126 ('the Winding Up Regulations').

The Occupational Pension Schemes (Deficiency on Winding Up etc.) Regulations 1996. SI 1996/3128 ('the Deficiency Regulations').

This Guidance Note has been approved by the Secretary of State in accordance with Section 119 of the Act and the Department of Health and Social Services for Northern Ireland in accordance with Article 116 of the Pensions (Northern Ireland) Order 1995.

Application

The Scheme Actuary responsible for giving advice to the trustees of any UK pension scheme to which the Winding Up Regulations or the Deficiency Regulations apply on or after 6th April 1997, broadly any scheme that starts to wind up, where an employer becomes insolvent or where a participating employer ceases to participate in a scheme.

Version 3.0 of GN19 will still be applicable in respect of deficiency calculations for pension schemes that started to wind-up before 19 December 1996 or where the deficiency is being calculated as at a date before 6 April 1997. Version 3.0 is found as Appendix 2.

Northern Ireland has its own body of law relating to pensions and, in relation to Northern Ireland, references to the Great Britain legislation contained in this Guidance Note should be read as including references to the corresponding Northern Ireland legislation. Appendix 1 shows Northern Ireland legislation corresponding to the Great Britain legislation mentioned in this Guidance Note.

Author

Pensions Board

Status

Approved under Due Process (Technical Amendment)

<i>Version</i>	<i>Effective from</i>
1.0	01.04.93
2.0	01.10.93
3.0	01.02.96
4.0	06.04.97
4.1	01.03.98

1 Introduction

- 1.1 In this Guidance Note the term ‘trustees’ should be read as ‘managers’ (as defined in Section 124(1) of the Pensions Act 1995) for schemes which are not established under trust.
- 1.2 If an occupational pension scheme (which is not a money purchase scheme) winds up, a participating employer of such a scheme becomes insolvent or an employer ceases to participate in a multi-employer scheme, the value of the scheme's liabilities and the scheme's assets may need to be determined in order to ascertain:
 - 1.2.1 the assets available for each liability class on winding-up; and/or
 - 1.2.2 if appropriate, a deficiency that falls on the employer(s) following an insolvency, winding-up or cessation of participation.
- 1.3 The schemes to be covered are those to which the Winding Up Regulations and the Deficiency Regulations apply. Section 3 of this Guidance Note applies in respect of 1.2.1 and section 4 applies in respect of 1.2.2.
- 1.4 The actuary should take instructions from the trustees concerning whether a valuation is to be undertaken and for what purpose(s).
- 1.5 The actuary's advice should be addressed to the trustees of the scheme.
- 1.6 The actuary should take instructions from the trustees regarding the effective date(s) of the calculations.
 - 1.6.1 In particular, the Winding Up Regulations provide for the liability categories to be set on the ‘crystallisation date’ (as defined in Regulation 4), i.e. questions as to whether or not a member's entitlement to payment of a pension or other benefit has arisen and whether any amount must be treated as an increase or as part of a pension are determined at the crystallisation date.
 - 1.6.2 In practice the crystallisation date will usually be the effective date of the start of the winding-up process, i.e. early in the process. The date for the purposes of the calculation of the amount to be applied to secure the liabilities (calculation date) will normally be shortly before the trustees secure the liabilities, i.e. late in the process.
 - 1.6.3 The Deficiency Regulations provide for the deficiency calculations to be made at the ‘applicable time’ (as defined in Regulation 2(2)).
 - 1.6.4 The purpose of the crystallisation date is purely to allocate members at that time to liability classes. The calculation of the amount of the liabilities at another time either the applicable time or the calculation date is likely to produce a different result to that which would occur at the crystallisation date.

The effect of assets fluctuating over the period to the calculation date, due to investment return, payments in and out, expenses of winding-up, etc., can mean the lower the priority class the greater the 'risk'.

- 1.6.5 The actuary should be aware that the calculations under both sets of regulations could be different, even if calculated at the same date. As an example, particular regard should be made to the calculation of liabilities where part or all the liability is secured by an insurance contract.

2 Future Revisions

- 2.1 This Guidance Note will be revised in due course to cover schemes commencing winding up after the end of the transitional winding-up period in April 2007.

3 Priorities on Winding-up

- 3.1 The amount of the liabilities of schemes, including the value of annuities in 3.6, should be calculated in accordance with The Occupational Pension Schemes (Minimum Funding Requirement and Actuarial Valuations) Regulations 1996 SI 1996/1536 ("the MFR Regulations") and GN27: Retirement Benefit Schemes - Minimum Funding Requirement. The relevant references are Regulations 7 and 8(2) of the MFR Regulations and GN27 (but see paragraph 3.8).
- 3.2 The actuary should make it clear to the trustees that the calculations of the liabilities and allocation to priority classes have been carried out in accordance with GN19.
- 3.3 The actuary should take instructions from the trustees as to the liabilities which fall into each priority class at the 'crystallisation date'.
- 3.4 All the calculations referred to in the remainder of this section are carried out as at the date instructed by the trustees.
- 3.5 **Pensioners**
- 3.5.1 When valuing the liabilities under Section 73 (3)(b) of the Act (pensions in payment etc.), the benefits should be calculated ignoring any allowance for post-retirement pension increases not effective at the crystallisation date, whether or not statutory.
- 3.5.2 When valuing the liabilities under Section 73(3)(d) of the Act, the benefits should be calculated with full allowance for post-retirement pension increases, less that calculated under 3.5.1.

3.6 Annuities in Payment

- 3.6.1 The actuary should take instructions from the trustees on any benefits secured by annuities potentially falling under Section 73(3)(aa) of the Act. For the purposes of the comparison in Section 73(3)(aa)(ii), any surrender value is to be compared with the MFR calculation of the relevant liability. Any pension increases to be taken into account, which are not secured by such annuities, are included in liabilities under Section 73(3)(d) of the Act.

3.7 Active and Deferred Members

- 3.7.1 When valuing the liabilities under Section 73 (3)(c), (e) and (f) of the Act (accrued benefits for active and deferred members etc.), revaluation (whether or not statutory), should be included up to pension age as allowed for in the MFR calculation.
- 3.7.2 When valuing the liabilities under Section 73(3) (c) of the Act, the benefits should be calculated ignoring any allowance for post-retirement pension increases.
- 3.7.3 When valuing the liabilities under Section 73(3)(e) of the Act, the benefit should be calculated with full allowance for post-retirement pension increases, less that calculated under 3.7.2.

3.8 Expenses

- 3.8.1 In accordance with Winding Up Regulation 4(1)(b), no allowance for expenses should be made as set out in E.1 of the Appendix to GN27.

3.9 Contracted-out hybrid schemes

- 3.9.1 Contracted-out hybrid schemes will have combinations of defined benefit element(s) and/or money purchase element(s) above the underlying contracted-out guarantee (e.g. equivalent pension benefits, protected rights, guaranteed minimum pensions and/or Section 9(2B) rights (i.e. post 97 COSR rights) as referred to in Section 73(3)(c) and (e) of the Act). For active and deferred members of these schemes, the part of their liability which falls under Section 73(3)(c) and (e) of the Act is to be determined by the appropriate contracted-out guarantee. Paragraph 3.9.2 gives further guidance in respect of the treatment of protected rights. All of any residual amount of liability falls into the class defined under Section 73(3)(f) of the Act. To determine the amount of this latter liability, the full amount of liability in respect of the member is calculated on an individual basis from which those amounts calculated under Section 73(3)(c) and (e) of the Act are deducted.

3.9.2 Protected rights

3.9.2.1 For the calculation of some liabilities under Section 73(3) of the Act it is necessary to apportion the protected rights parts of money purchase liabilities between those elements relating to post-retirement pension increases and those not. The money purchase element that falls within Sections 73 (3) (c) of the Act (i.e. excluding pension increases) should be calculated as:

$$\text{(protected rights part of the money purchase account)} \times \frac{\text{(annuity without increases)}}{\text{(annuity including increases)}}$$

3.9.2.2 The difference between the protected rights part of the money purchase account and the result of the calculation in paragraph 3.9.2.1 should be that element allocated to Section 73 (3) (e) of the Act. Protected rights element relating to different pension increases should be appropriately apportioned before the calculation in 3.9.2.1.

3.9.2.3 The annuities shall be calculated using age 60 or the age of the member, if higher. Due allowance should be made for contingent beneficiaries' benefits in the annuity. The post-retirement increases included in this calculation should be those allowed for in the MFR calculation. Where different levels of increase are appropriate, the protected rights part of the money purchase account should be appropriately subdivided.

4 Section 75 Deficiencies

- 4.1 The value of the assets and the amount of the liabilities and expenses should be calculated in accordance with the MFR Regulations and GN27. The relevant references are Regulation 3(2), 3(3) and 4 to 8 of the MFR Regulations and GN27.
- 4.2 In determining the assets, only when the scheme is winding-up should the full value of employer-related investment be included (i.e. not capped at 5%) as set out in Deficiency Regulation 3(4).
- 4.3 Deficiency Regulation 3 sets out the approach to calculation. If a deficiency is revealed the certificate to be signed is found in Schedule 1 to the Deficiency Regulations.
- 4.4 In multi-employer schemes which are not sectionalised, as defined in Section 75(1B) of the Act, the overall deficiency in respect of the entire scheme should initially be calculated.
- 4.5 It should be noted that the onus of providing information necessary for allocating liabilities in respect of employment with an employer to the relevant employer is on the trustees. The actuary should consult with the trustees of the scheme before determining the appropriate allocation.

- 4.6 Contributions equivalent premiums (CEPs) are debts of the scheme, rather than liabilities, and therefore as an expense, they rank as a first priority on wind-up. Until the trustees of the scheme make an election to pay CEPs, then the liability to pay a GMP still exists.
- 4.7 In these schemes, the proportion of the deficiency attributable to each employer may be set out in the rules of the scheme, in which case the actuary should take instructions from the trustees on the apportionment. Otherwise, the proportion of the deficiency in respect of each employer should be calculated as the ratio which the value of the scheme's liabilities (excluding any provision for expenses) in respect of employment of employees and former employees with that employer bears to the total value of the scheme's liabilities (excluding any provision for expenses) in respect of employment of employees and former employees with all those who at that time count as employers for the purposes of Section 75 of the Act.

Appendix 1: Northern Ireland Legislation

GB Provision

Pensions Act 1995 (c.26)

Section

Section 73

Section 75

Section 119

Section 124 (1)

Pension Schemes Act 1993 (c.48)

Section 9 (2B)

Occupational Pension Schemes (Winding Up) Regulations 1996 (SI 1996/3126)

Occupational Pension Schemes (Deficiency on Winding Up etc.) Regulations 1996 (SI 1996/3128)

Occupational Pension Schemes (Minimum Funding Requirement and Actuarial Valuations) Regulations 1996 (SI 1996/1536)

NI Provision

Pensions (Northern Ireland) Order 1995 (SI 1995/3213 (NI 22))

Article

Article 73

Article 75

Article 116

Article 121(1)

Pension Schemes (Northern Ireland) Act 1993 (c.49) Section 5(2B)

Occupational Pension Schemes (Winding Up) Regulations (Northern Ireland) 1996 (SR 1996 No.621)

Occupational Pension Schemes (Deficiency on Winding Up, etc.) Regulations (Northern Ireland) 1996 (SR 1996 No.585)

Occupational Pension Schemes (Minimum Funding Requirement and Actuarial Valuations) Regulations (Northern Ireland) 1996 (SR 1996 No.570)

APPENDIX: 2

GN19: Retirement Benefit Schemes-Deficiency on Winding-up

Classification

Practice Standard

Legislation or Authority

Occupational Pension Schemes (Deficiency on Winding-up etc.)
Amendment Regulations 1996. SI 1996/5.

Pension Schemes Act 1993 (1993, c.48). Section 144.

Application

Any actuary responsible for giving advice to the trustees of any UK pension scheme.

Author

Pensions Board

Status

Approved under Fast Track.
Required to complete Due Process by 1.6.97

<i>Version</i>	<i>Effective from</i>
1.0	01.04.93
2.0	01.10.93
3.0	01.02.96

1 Introduction

- 1.1 If an occupational pension scheme, which is not a money purchase scheme, winds-up or a participating employer of such a scheme becomes insolvent, the values of the scheme's liabilities and scheme's assets are to be determined by being calculated and verified in such a manner as may be approved by an actuary appointed by the trustees of the scheme.
- 1.2 This Guidance Note relates to the circumstances as outlined in paragraph 1.1 and must be read in conjunction with the Occupational Pension Schemes (Deficiency on Winding-up etc.) Amendment Regulations 1996.

- 1.3 The Guidance Note relates to all occupational pension schemes other than those where all the benefits are provided on a money purchase basis. Therefore schemes which provide at least one benefit which is not money purchase are affected by the provisions of this Guidance Note.
- 1.4 The Guidance Note relates to both funded and unfunded schemes which are constituted by trust.

2 Date of the Calculations

- 2.1 The calculations can be carried out as at any date after the commencement of the winding-up of a scheme but not later than the time a relevant insolvency event occurs, as specified in Section 144 of the Pensions Scheme Act 1993. If the scheme is not winding-up the calculations need to be carried out each of the times at which a relevant insolvency event occurs in relation to any of the employers to whom the scheme relates. In both cases, the earliest date calculations need be made is 1 July 1992.
- 2.2 The actuary must take instructions from the trustees of the scheme as to the appropriate date as at which the calculations are to be carried out.

3 Basis for the Calculations

- 3.1 The calculation of the value of the liabilities should not limit this value to the value of the assets, even where the rules of the scheme may so provide. In particular, in the valuation of the liabilities in money purchase schemes which give a final salary benefit promise, the value of the final salary benefit promise should not be limited to the value of the assets of the scheme, even if the rules of the scheme restrict the benefit promise where there are not sufficient assets in the scheme.
- 3.2 The benefits to be valued for active members will normally be the leaving service benefits unless the benefits payable under the winding-up rules of the scheme are greater, in which case these higher benefits will be valued. The leaving service benefits to be valued for active service members with less than two years' qualifying service should be the accrued deferred benefits as opposed to any contribution refund benefits, unless the value of any contribution refund benefits is higher.

- 3.3 The actuarial value of the benefits for active members described in paragraph 3.2 and of the benefits for deferred pensioners should be calculated using the same basis as the actuary employs in the calculation of cash equivalents under GN11 except that whilst allowance should be made for discretionary benefits already granted no allowance should be made for future discretionary benefits. No adjustment should be made if the value of the scheme's assets is insufficient to cover the scheme's liabilities as described in paragraph 4.1 of GN11. For members in receipt of pension and any associated contingent pensions, the liability, making no allowance for future discretionary benefits, should be quantified having regard to insurance company immediate annuity rates.
- 3.4 Any of the benefits that are secured by an insurance policy which exactly matches the benefits may be ignored for the purposes of the calculations. The calculation of the value of the assets should be correspondingly reduced in these circumstances (see paragraph 3.7).
- 3.5 In calculating the value of the liabilities the actuary should make due allowance for the expected expenses, fees and costs relating to the winding-up of the scheme.
- 3.6 The market value of the assets should be used for the purposes of these calculations except as provided in paragraph 3.7 below. The actuary should ensure, taking such other specialist professional advice as is necessary, that the market value used for the calculations for any self-investment or any other asset whose value may be affected by the particular circumstances represents a realistic amount. The actuary should obtain an audited statement of the assets of the scheme as at the date of the calculations. If an audited statement of assets is qualified in any way, or such is not forthcoming, or a set of scheme accounts is prepared that qualifies the value of assets in any way, then the actuary should not certify the amount (if any) of the 'debt on the employer' (see paragraph 3.8 below).
- 3.7 If the assets of the scheme include insurance policies, the actuary should, where appropriate, have regard that the practice of the particular life office in the winding-up of pension contracts in the valuation of these assets and, in particular, if these policies or substituted policies are to be used to secure any of the benefits, these insured benefits should, where appropriate, be disregarded from both the calculation of the liabilities and the calculation of the assets.

- 3.8 The actuary should certify (using the form of the certificate in the Appendix) to the trustees of the scheme the amount (if any) of the ‘debt on the employer’, being the excess of the value of the scheme’s liabilities over the value of the scheme’s assets.
- 3.9 The actuary needs to point out to the trustees of the scheme that the amount certified in paragraph 3.8 has been calculated in accordance with GN19 and does not represent the amount of cash required by the scheme to secure the liabilities of the scheme by insurance policies as at that date.
- 3.10 The actuary should also confirm the effective date of the calculations to the trustees of the scheme and point out that this date will normally be different from the payment date of the amount of the debt on the employer’, with its consequent effect on the entitlement of individuals, particularly active service and deferred members.
- 3.11 In a multi-employer scheme, the ‘debt on the employer’ only applies if the whole scheme is in deficiency. In these circumstances the amount of the debt due from a particular employer should be calculated as a proportion of the overall notional debt on the employer as if the whole scheme were to be wound-up equal to the ratio of the value of the scheme’s liabilities attributable to employment of employees and former transfer credits allowed under the scheme in connection with employees with that employer (including liabilities in respect of any employment with that employer) to the total value of the scheme’s liabilities. In these circumstances, notwithstanding paragraph 3.7, allowance should be taken for any insured liabilities and assets. Separate certificates should be provided to the trustees of the scheme for each of the participating employers. Where a centralised scheme of non-associated employers meets the requirements of Section 144 of the Pension Schemes Act 1993 then each section must be treated as a separate scheme for purposes of determining the ‘debt on the employer’.
- 3.12 Section 144 of the Pension Schemes Act 1993 sets out the circumstances in which another pension scheme can take over responsibility for paying all the benefits of the scheme that is winding-up, eg following a block transfer. In such cases, the employer and trustees of the original scheme can make arrangements for the employer to make contributions to the recipient scheme to enable that scheme to provide the benefits going forward. It is not necessary for the benefits provided by the recipient scheme to be identical to those of the original

scheme, but may be 'broadly equivalent'. As long as contributions are paid in accordance with the arrangement and the benefits meet this requirement, then the 'debt on the employer' is still certifiable but not recoverable. Actuaries should bear in mind that, although they may be called upon to give advice on the interpretation of 'broadly equivalent' in this context, the responsibility for interpreting such is a matter for the trustees of both the original and recipient scheme. An actuary asked for such an opinion must take all relevant facts into consideration.

Appendix: Certificate

To: The Trustees of the Scheme named below

Name of Scheme:

PSO Reference Number (if any):

This certificate is given having regard to the Occupational Pension Schemes (Deficiency on Winding-up etc.) Amendment Regulations 1996 and has been prepared in accordance with Guidance Note GN19 issued jointly by the Institute of Actuaries and the Faculty of Actuaries and must be read in conjunction with the notes listed overleaf.

I hereby certify that, in my opinion, as at

* The value of the liabilities of the scheme did not exceed the value of the assets of the scheme.

* The value of the liabilities of the scheme exceeded the value of the assets of the scheme by £

The values of the liabilities and assets have been determined in accordance with the principles and requirements of Guidance Note GN19.

Signature Date

Name Qualification

Address Name of Employer
(if applicable)

*Delete as appropriate

Notes

1. The value of the scheme liabilities has been quantified-
 - (a) for members in receipt of pension and any associated contingent pensions having regard to insurance company immediate annuity rates, and
 - (b) for active members and deferred members, by taking the actuarial value of those members' entitlements having regard to market rates of interest. This is the same basis as would be used in the calculation of Cash Equivalents (transfer values) under Guidance Note GN11 issued by the Faculty of Actuaries and the Institute of Actuaries.
2. For the purpose of 1(b) above no adjustment has been made if the value of the scheme's assets is insufficient to cover the scheme's liabilities as described in paragraph 4.1 of GN11.
3. In calculating the value of the liabilities, no allowance has been made for any future discretionary benefits that may be paid.
4. Due allowance has been made in the calculation of the liabilities for the expenses, fees and costs relating to the winding-up of the scheme.
5. The market value of the assets has been taken account of for the purposes of this certificate.
6. The benefits that would be secured by the actuarial value in 1(b) above depend on the future returns achieved by the investment of that sum. This sum does not represent the amount of cash required by the scheme to secure the member's accrued entitlement by using non profit insurance company rates at the date stated.
7. The date of the payment of any shortfall is likely to be different from the effective date of the calculations.
8. **Additional Information**

It would be permissible for the actuary giving the certificate to add any additional information under this note that would help to clarify or amplify the benefits that had been taken into account in valuing the liabilities in the certificate; it must not be used to modify the certificate in any way.