Institute
and Faculty
of Actuaries

Consultation on the Levy Results for 2015/16

Response to the Pension Protection Fund

13 November 2014

About the Institute and Faculty of Actuaries

The Institute and Faculty of Actuaries is the chartered professional body for actuaries in the United Kingdom. A rigorous examination system is supported by a programme of continuous professional development and a professional code of conduct supports high standards, reflecting the significant role of the Profession in society.

Actuaries' training is founded on mathematical and statistical techniques used in insurance, pension fund management and investment and then builds the management skills associated with the application of these techniques. The training includes the derivation and application of 'mortality tables' used to assess probabilities of death or survival. It also includes the financial mathematics of interest and risk associated with different investment vehicles – from simple deposits through to complex stock market derivatives.

Actuaries provide commercial, financial and prudential advice on the management of a business' assets and liabilities, especially where long term management and planning are critical to the success of any business venture. A majority of actuaries work for insurance companies or pension funds – either as their direct employees or in firms which undertake work on a consultancy basis – but they also advise individuals and offer comment on social and public interest issues. Members of the profession have a statutory role in the supervision of pension funds and life insurance companies as well as a statutory role to provide actuarial opinions for managing agents at Lloyd's.

Institute and Faculty of Actuaries

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Chief Policy Adviser
Pension Protection Fund
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13 November 2014

Dear Chris

Consultation on the Levy Rules for 2015/16

1. The Institute and Faculty of Actuaries (IFoA) welcomes the opportunity to respond to this consultation. Our response has been prepared by the Pensions Consultations Subcommittee. We have limited our response to those questions that require specific actuarial comment.

Chapter 13

We would be grateful for comments on the drafting of the Levy Rules. In particular, we would welcome comments on the ABC Appendix, and any points we should clarify in associated Guidance.

2. The IFoA welcomes the revised approach to valuing, for the PPF's purpose, asset-backed contributions (ABCs), based on the lower of the stressed insolvency value and the fair value in the scheme accounts, rather than the net present value (NPV) of future cash flows. We would welcome further clarification from the PPF on the details of the exceptional circumstances in which discretion might be used to recognise an ABC at a different value to that shown in the certificate.

3. Although ABC terms vary, the amount that the pension scheme can realise from the ABC on the insolvency of the sponsor will reflect:

   - The value (given insolvency) of the underlying asset (the value of the ABC Asset);
   - The intended formula payment under the ABC terms on insolvency/default (which may depend on discount rates at the relevant date); and
   - The funding position of the scheme at that time.

   Given this variability, we would encourage the PPF to provide further detail from the PPF on how it intends to calculate the stressed insolvency value.

4. We would encourage the PPF to confirm if its intention is that the stressed insolvency value is calculated by applying the relevant stress to the value of the ABC Asset and that the derivation of the expected pay-out would then be based on:

   - That *stressed* value of the ABC Asset;
   - The *unstressed* value of the formula payment; and

- The *unstressed* value of the scheme funding deficit.

Additional clarity in the ABC Appendix and Guidance about the comparison with the stressed insolvency value would also be useful; we would suggest that it is currently unclear if the comparison should be with the stressed, or unstressed, accounts value.

5. Our interpretation of the current ABC Appendix and Guidance suggests that the preparation of the accounts would not be included within the definition of the advice; advice that feeds into the derivation of the ABC Value and must comply with (for example) part 6 of the Guidance (i.e. the value placed on the ABC instrument in the accounts is taken as a factual data input). The preparation of the accounts would include any advice on the fair value of the ABC instrument; for both the accounts and the audit of those accounts. We would welcome a strengthening of the Guidance to clarity the intent in this regard; as currently drafted, we would suggest that it may be open to misinterpretation.

6. With regard to the DRC Appendix, we note the proposed approach to the new definition of money purchase and believe this seems reasonable and simple to apply. It could be clarified that ABC payments, as well as the initial purchase contribution, should be excluded from the contributions figure 'a', if an ABC has been certified.

Chapter 15

Are there other factors that we should consider?

7. The proposed approach for overseas companies appears reasonable.

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

8. The IFoA welcomes the proposal to exclude mortgages that are deemed to be immaterial. In the absence of evidence to suggest that the test is set at the right level, a test, based on the size of the charge, is a pragmatic approach.

9. We would question the exclusion of all entities with a credit rating. As the PPF has identified, it may be possible that mortgages may still be used for financing by these entities, and therefore such exclusions may not always be appropriate.

10. If entities with a credit rating are to be excluded, then the PPF should consider what should happen if the entity is downgraded, after submitting a certificate, and is no longer investment grade. For example, will Experian apply the certificate indefinitely; or should the entity apply to Experian to have it retracted?

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?

11. We understand from the consultation that if a mortgage certificate is submitted, it will apply to all previous month end scores in that levy year - and any future scores for that and future levy years. We would welcome clarification from the PPF that this is the correct interpretation of the levy determination.

12. We note that mortgages must be certified to Experian rather than the PPF. We would question whether it is proportionate for Experian to receive copies of the mortgage documents, given that these mortgages will be deemed immaterial, and that the certificates should contain all relevant information. Ideally, the process should be as simple as possible and we are unsure whether companies would be willing to send further, potentially commercially sensitive, information to Experian for this purpose.

13. Finally, we note that the definition of the officer who can sign the certificate is different on the credit rating certificate. We assume this is intentional, but a paragraph similar to 1c might be useful on the other certificates to cover different legal structures.

14. In relation to Type A Contingent Assets, we accept the logic for applying an adjustment where the Guarantor is not the parent of all the guaranteed employers, or it does not file consolidated accounts. The PPF has accepted that no adjustment needs to be applied where the Guarantor is the ultimate parent of all the guaranteed employers and files consolidated accounts on the basis that the deficit is already reflected in the Guarantor's accounts, albeit on a different measurement basis. However, the same argument applies equally to any Guarantor which is a parent of all the guaranteed employers and files consolidated accounts, whether or not it is the ultimate parent. We would ask the PPF to re-consider whether it would be appropriate to extend this treatment to a Guarantor which is a parent of all the guaranteed employers and files consolidated accounts rather than just to such Guarantors that are the ultimate parent.

15. If you have any questions about our consultation response, or if you wish to discuss any of our comments in more detail, you should contact Philip Doggart, Policy Manager at the IFoA, in the first instance. (Philip.Doggart@actuaries.org.uk / 0131 240 1319)

Yours sincerely

Nick Salter

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