

PREMIER PENSIONS MANAGEMENT

TECHNICAL UPDATE: 02/09

Pension Protection Fund (PPF) Levy

The PPF have issued a consultation document on proposed changes to the levy formula. These changes are scheduled to take effect from the 2011/12 levy year. This consultation builds on PPF analysis which shows that there is a mismatch between the risks that schemes pose to the PPF and the share of the total levy that they are charged.

In summary, the proposed changes are:

- **Scheme-based Levy** - this will continue to be calculated in the current way, but the proportion of the total levy that it represents may reduce from the current 20% level.
- **Risk-based Levy** - Under the PPF proposals, this would be a two step calculation:
 - a) **Short-term risk component** - this would be calculated broadly as at present, including a one year insolvency probability. Changes are proposed in the basis for calculating the underfunding figure. The existing shorter-term risk calculation will be expanded to include a scaling factor, known as the rate for short-term risk, which would be publicised before the start of each levy year.
 - b) **Long-term risk component** - this element will reflect the Scheme's contribution to long-term risk. A new insolvency probability will be derived by expanding the process used to calculate the one year scores. The calculation of the underfunding figure may also be different.
- **Investment risk** - The PPF has not made a specific recommendation about the way in which investment risk may be taken into account. The consultation paper provides five different ways in which investment risk could be taken into account as follows:
 - **No differentiation by schemes**

This would make an adjustment based on the combined investment allocation of all eligible schemes.

- **Certification of low risk investments**

A scheme would submit a certificate indicating which of their assets are regarded as “low risk”. Schemes which submitted an acceptable certificate would have a reduced risk factor applied to the value of their assets.

- **Use scheme return information**

Data collected via the existing scheme return will be used to estimate the investment risk within the levy.

- **Voluntary certificate using simple stress test**

Stress tests could involve providing results allowing for a 10% increase and decrease in a scheme’s growth assets such as equities and property.

- **Internal models approach**

Schemes could be allowed to submit results of models prepared to show the sensitivity of their investment models to changes in risk factors. These results could be submitted in a certificate which would then allow the PPF to calculate a suitable adjustment.

The PPF have commented that the effects of these proposals are complex as three different factors interact:

- Schemes with good short-term risk characteristics but greater long-term risk would tend to see an increase in levy as their long-term risk will be properly recognised.
- Schemes with low investment risk would tend to pay less and those with riskier investments would tend to pay more.
- The lower Scheme-based levy means that larger schemes will pay less than otherwise.

They also observed that they want to collect comments on their investment risk proposals before deciding which method to adopt.

The PPF expect to publish a summary of responses, together with a statement of the final policy, during late Spring 2009.

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This update includes general information and cannot be relied upon for individual schemes issues. You should contact your adviser or Paul Couchman at Premier Pensions Management Ltd, Capital Business Centre, Units 14 & 15, 22 Carlton Road, South Croydon, Surrey, CR2 0BS. DL: 020 8916 2129. Email: paul.couchman@premierpensions.co.uk, if you require definitive advice