PENSION PROTECTION FUND – LEVY REDUCTION MEASURES

January 2015

The PPF has issued its determination and final documents in relation to the 2015/16 risk based levy. Companies that participate in defined benefit pension plans and trustees of such plans should now consider whether they can save money by taking advantage of any of the levy reduction measures available.

There are a number of changes to levy reduction measures for 2015/16, including: a new certification requirement for Type A contingent assets; the option for employers to apply to exclude certain mortgages/charges from the risk assessment; and the recognition of Asset Backed Contributions with any underlying asset. These measures require careful consideration at an early stage so that the appropriate advice can be obtained and documentation can be submitted by the PPF's deadlines. Any trustees certifying their pension plan as a 'last man standing' scheme on the scheme return should ensure that they have received legal advice confirming this status.

We highlight the key changes below but recommend that employers and trustees seek advice on the options available to them.

Contingent Assets

Type A

Trustees who are certifying a Type A contingent asset (i.e. a parent or group company guarantee) will be certifying the following statement which, as expected, is changed from last year:

> *"The trustees, having made reasonable enquiry into the financial position of each certified guarantor, are reasonably satisfied that each certified guarantor, as at the date of the certificate, could meet in full the Realisable Recovery certified, having taken account of the likely impact of the immediate insolvency of all of the relevant employers."*

The 'Realisable Recovery' is a fixed sum which must be calculated in accordance with the PPF's specific requirements but effectively this is the amount that trustees are satisfied that they could claim under the guarantee in the event of insolvency. Trustees are free to certify the contingent asset for a different Realisable Recovery each levy year. Trustees are expected to take a sensible view each year of the guarantor's financial position and the pension plan funding position.

From 2015/16 the PPF will apply a formula which may result in a downgrading to a guarantor's levy band to take account of the amount guaranteed under the Type A guarantee. The adjustment will depend on the impact that providing the guarantee would have on the guarantor's level of gearing if called upon. An adjustment will not be made where the guarantor is the ultimate parent company and files consolidated accounts (otherwise there could be an element of double counting). Guarantees will only be taken into account where there is sufficient information to score the guarantor on the basis of its own financial statements.

According to the PPF, the changes to the certification of Type A contingent assets are not intended to require trustees to make any extra assessment of the employer covenant, as they reflect what trustees should already have been doing in previous levy years. However, many trustees will need covenant advice to support their certified Realisable Recovery sum.

Before giving the certification, trustees should take time to consider the new certification wording and, if they consider covenant advice is required, seek the necessary advice before the inevitable capacity crunch in March.

Type C

From 2015/16 the PPF will recognise surety bond arrangements as Type C (ii) contingent assets.

Asset Backed Contributions

For 2015/16, Asset Backed Contributions with any underlying asset type can be recognised for levy reduction purposes. The certification process is complicated and, in simple terms, involves trustees certifying the lower of the amount that they would reasonably expect to recover in an insolvency situation and the 'fair value' of the Asset Backed Contribution investment (normally as reported in the most recent scheme accounts). The valuation must be undertaken by appropriate professionals who will accept a duty of care to the PPF. Legal advice is required as part of the valuation and also in respect of the structure and enforceability of the Asset Backed Contribution. The PPF has issued guidance on this subject.

This is a new process and a number of professionals will need to be involved – we therefore recommend that trustees speak with their advisers at an early stage.

Mortgage Ages

The 'mortgage age' variable (which measures the age of the newest unsatisfied secured charge registered) is a feature of most of the insolvency risk scorecards and can have a material effect on an employer's insolvency risk score. The PPF considers that mortgage age is an important predictor of insolvency risk but accepts that this might not be true in respect of all mortgages or charges. The following charges are excludable:

- charges in favour of a pension scheme
- rent deposits[1]
- mortgage refinancing on equal or better terms where the borrowing has not increased
- "immaterial mortgages" (for more information on the immateriality thresholds see the PPF's Guidance relating to Mortgage Exclusions).

Following consultation, the PPF has also agreed that charges may be ignored for the mortgage age variable if either the employer has an external investment grade rating, or the employer is not credit rated but each other member of the employer's group that is credit rated has an external investment grade rating. The PPF will check that the certified investment grade rating remains correct as at 31 March 2015.

For a mortgage to be disregarded, an Officer's Certificate must be produced for each type of mortgage exclusion that applies. The certificates can be obtained from the PPF/Experian online portal. Employers should consult the Mortgage Exclusion Guidance issued by the PPF for more information. The relevant documentation must be supplied to Experian by 5pm on 31 March 2015 for a mortgage to be excluded. If the exclusion criteria are met, scores will be recalculated for all relevant monthly scores counting for 2015/16 averaging (October 2014 to March 2015).

Employers are advised to consider whether they have mortgages that can be excluded. The PPF's Mortgage Exclusion Guidance should be considered carefully and advice sought as necessary.

Further Risk Scoring Considerations

Companies with a large number of part time staff may be scored harshly under the new risk model. These companies can apply to have full-time equivalent staff numbers used in the risk calculations.

This requires action from the company.

Following consultation, changes have also been made to the way in which employers are allocated to one of the eight PPF scorecards for risk assessment. In particular, the entry conditions for the 'Large and Complex' scorecard are altered so as not to capture businesses that file abbreviated accounts or whose only subsidiaries are dormant.

Non-UK companies who are allocated to the Large and Complex scorecard by default can supply evidence which may allow them to be allocated to a different scorecard.

Last Man Standing Schemes

Trustees of schemes classified as 'last man standing' schemes on the scheme return will receive an email from the Pensions Regulator asking for confirmation to be supplied to the PPF, by 29 May 2015, that legal advice has been received on the status of the pension plan.

We recommend that trustees who have not yet obtained this advice should consider doing so before submitting the scheme return.

Key Deadlines

Item	Key date
Submit scheme returns on Exchange	By 5 p.m., 31 March 2015
Contingent Asset Certificates to be submitted on Exchange and with hard copy documents as necessary to PPF	By 5 p.m., 31 March 2015
Asset Backed Contribution Certificate to be supplied to PPF	By 5 p.m., 31 March 2015
Mortgage Exclusion Officers' Certificates and supporting evidence to be supplied to Experian	By 5 p.m., 31 March 2015
Deficit-Reduction Contributions Certificates to be submitted on Exchange	By 5 p.m., 30 April 2015
Confirmation of legal advice on 'last man standing' status to be supplied to PPF	By 29 May 2015
Certification of full block transfers to be completed on Exchange (or supplied to PPF in limited circumstances)	By 5 p.m., 30 June 2015

1. Experian is proactively identifying rental deposits from Companies House records. The employer should check the PPF/Experian online portal for evidence. If the employer is in any doubt that rental deposits have been identified, the relevant Officer's Certificate and paperwork should be completed and submitted to Experian.

Action

It is very important for trustees and employers to monitor the information held on the PPF/Experian online portal and to supply to Experian any accounting or other relevant information that may be missing from employer and pension plan records.

Employers and trustees wishing to apply for one of the levy reduction methods are encouraged to seek advice and take action well in advance of the deadlines.

More detail on all of the issues mentioned in this publication is contained on the 2015/16 levy determination page.

Further Information

For help and information please contact any of the partners listed or your usual contact in the Squire Patton Boggs pensions team.

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