

Technical Briefing

No. 37



Insolvency Risk for 2011/12 PPF Levy

Introduction

On 29 January 2010 the Pension Protection Fund (PPF) issued a Consultation Policy Statement on how it will measure insolvency risk for the 2011/12 PPF Risk-Based levy with the intention to represent a fairer measure of insolvency risk, and in particular to reflect the current economic environment.

Revised D&B Scorecard Elements

The PPF have stated that the following changes are to be made to their methodology for calculating the 2011/12 PPF Risk-Based levy:

- Dun & Bradstreet (D&B) have been asked to obtain stronger evidence when employers seek to change their industry or geographic information to avoid manipulation in order to achieve a lower Failure Score.
- D&B are to introduce a Nationwide attribute for scoring the geographic location of a company to more accurately reflect the lower risk faced by companies with branches which are located within three or more regions.
- D&B are to exclude PPF-compliant contingent assets when considering whether charges on a company's asset have a negative effect on its insolvency risk.
- The Failure Score of a subsidiary company, whose parent company is considered to have a substantial risk of failure, will not be assessed higher than the score of the parent company. This measure will recognise the parental risk of the parent company on the subsidiary.

- Although D&B automatically collect accounting information filed at Companies House it has not actively sought audited accounts from charities and other non-commercial employers. Although 75% of charities have voluntarily provided audited accounts D&B intend to obtain financial data from the Charity Commission website in March 2010 for the 2011/12 PPF levy to increase fairness and mitigate the risk of weaker employers not volunteering this information.

Employers will only have up to 30 March 2010 to confirm the information held by D&B or provide additional information. In particular, employers may wish to contact D&B Customer Services (0870 850 6209) to check whether or not they have been classified as Nationwide for 2011/12. Employers will be unable to appeal to change their status after **30 March 2010** unless they have provided D&B with appropriate evidence before this deadline,

Revised D&B Scorecard

As part of a periodic review, D&B have updated their one year assumed probabilities of insolvency risk for UK companies to reflect the current economic environment.

As a result, the probability of insolvency associated with every Failure Score will be increased to reflect the observed increase of business failures in the UK during the current recession. In particular, the probabilities of failure for the lowest risk companies will be increased proportionately more than higher risk companies. This reflects recent observations that insolvency rates rise fastest for those with a very low chance of insolvency prior to the recession.





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The following table compares the one year assumed probabilities of insolvency risk for 2010/11 and 2011/12 at selected Failure Scores.

Failure Score	2010/11	2011/12
5	6.63%	7.58%
10	4.40%	4.68%
40	1.47%	1.65%
60	0.65%	1.00%
90	0.15%	0.28%
95	0.09%	0.18%
100	0.01%	0.03%

The table demonstrates that all one year probabilities of insolvency have increased and that the greatest proportionate increases are for those companies with the best Failure Scores. The probability of insolvency has doubled for a Failure Score of 95 and tripled for a Failure Score of 100.

Details of the total amount to be collected by the PPF and the levy-scaling factor will not be published until later on this year. Therefore it is not possible at this stage to assess the impact of the above changes on the 2011/12 Risk-Based levy.

CPRM Commentary

It is not surprising that the one year assumed probability of insolvency will be increased for all employers for the 2011/12 PPF Risk-Based levy to reflect higher observed rates of insolvency being experienced in the UK within a recessionary environment. What may come as more of a surprise is that the largest proportionate increases are to those employers who previously had the lowest perceived risk of failure.

These changes will increase the proportion of the aggregate levy to be met from schemes sponsored by stronger businesses (with higher D&B Failure Scores) and reduce the levy raised from schemes sponsored by weaker businesses (with lower D&B Failure Scores).

The changes being made to the D&B scorecard are aimed at more accurately identifying the insolvency risk posed to the PPF to make the distribution of levies fairer. The introduction of a Nationwide attribute to acknowledge the lower perceived risks associated with companies in three or more different regions is welcomed, which in turn will also reduce the possibility of inappropriate manipulation of scores based on company location.

Companies are reminded that they should ensure that the information held by D&B is both accurate and complete by **5pm on 30 March 2010**, the Measurement Date for the 2011/12 PPF levy. In particular, multi-regional companies should confirm with D&B that their status is correctly recorded as Nationwide so that they can benefit from the lower perceived insolvency risk associated with such companies.

Please contact your usual **cprm** consultant if you have any questions on the contents of this Technical Briefing or would like some additional information.

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