

# Technical Briefing

No. 27



## PPF announces conclusions on the 2009/10 levy

In our technical briefing 26 we notified readers of the PPF's proposed details of the 2009/10 PPF levy. The Board of the PPF has now issued the final details. As expected, the final details are substantially unaltered from those proposed. Consequently the methodology and factors for calculating the 2009/10 levy are fixed.

Readers may recall from technical briefing 23 that the levy consists of the scheme based levy (SBL) and a risk based levy (RBL):

1. **SBL** = Protected liabilities (**L**) x levy multiplier (**m**)
2. **RBL** = Underfunding risk (**U**) x Insolvency risk (**P**) x 80% (**R**) x Scaling factor (**c**)

**m** has been fixed at 0.000162 (unchanged from 2008/09) and **c** at 2.22 (down from 3.77 in 2008/09). **L** will be calculated by the PPF in a prescribed manner based on information submitted on the Section 179 certificate (this had to be submitted on or before 31 March 2008). Similarly, **U** is based on assets and liabilities that are calculated by the PPF, also in a prescribed manner. **P** is based on the probability of the sponsoring employer defaulting in the next 12 months and was determined at 31 March 2008 based on the sponsoring employer's D&B rating at that time. Information submitted after this date will not affect **P**. This is the same D&B rating that will be used for the 2008/09 levy.

So, the 2009/10 PPF levy for each scheme can now be estimated with a reasonably level of accuracy based on the above fixed factors and methodology used by the PPF. There are however two main methods open to schemes and their sponsors to reduce the 2009/10 levy. This can be done by submitting either an actuarial certificate

for deficit reduction contributions (DRC) or a contingent asset certificate. However, these certificates can only be submitted in specific circumstances which are detailed below.

### Certificate for DRC

A sponsoring employer can reduce **U** in a scheme by paying additional contributions into its defined benefit scheme. This in turn would reduce the **RBL** that the scheme is liable for. These contributions need to be in addition to those already documented in the schedule of contributions.

Following receipt of these contributions the Scheme Actuary would be able to submit a certificate to the PPF that would be taken into account in determining the 2009/10 levy. This certificate must be submitted by **5pm on 7 April 2009**. The amount disclosed on the certificate would be added to the assets when calculating **U**. The amount that is added to the assets is equal to the total contributions paid by the Employer (including regular contributions as documented in the schedule of contributions) less the cost of benefits accruing over the period from the date of the last section 179 valuation and the date of the payment of the additional contributions.

### Contingent asset certificate

Contingent assets do not involve money or assets being transferred to the scheme, but rather affect **U** or **P** in the **RBL** formula. This is done by guarantees of some form from other parties. The fact that assets are not actually transferred to the scheme is the main advantage for sponsors over deficit reduction contributions. It does, however restrict the use of those assets.





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There are three types of contingent assets and these are discussed further below. Please note that certificates submitted for the 2008/09 levy year will need to be renewed if these contingent assets are still appropriate. Any certificate must be submitted by **5pm on 31 March 2009**.

**Type A** – guarantee from a parent company to the sponsoring employer.

This certificate is applicable for those schemes where the parent company is different from the participating employer(s). If the parent company to the participating employer(s) has a better D&B rating, this better D&B rating can be used to calculate the probability of insolvency if a type A certificate is in place. Exactly how this would affect the levy will depend on the form of the guarantee.

**Type B** – security over assets not belonging to the scheme.

The types of assets that can be considered for this certificate are (a) cash in a bank account, (b) real estate and (c) securities in which the scheme is permitted to invest (plus employer related assets). The guarantee can take various forms and the value of these contingent assets are dependant on that form. The guarantee could be:

- a) A fixed monetary sum with the value just equal to that monetary sum.
- b) The amount required to bring the PPF scheme funding level up to a specified percentage. The value of this guarantee equals the amount by which that the specified percentage of liabilities exceed the assets.
- c) The lower of (a) and (b). The value of this form of contingent asset is simply the lower of the value determined under (a) and (b).
- d) The aggregate PPF liability. The value of this would be determined as 140% of the protected liabilities less scheme assets.
- e) The lower of (a) and (d). The value of this is simply the lower of the value determined under (a) and (d).

In isolation this type of certificate would reduce **U** in the **RBL** formula above by the value of the contingent asset.

**Type C** – letter of credit or bank guarantee.

This form of contingent asset can be a letter of credit or a bank guarantee, in the event of insolvency of the sponsoring employer, for (i) a fixed amount or (ii) a fixed amount which reduces upon the making of contributions specified in this certificate. The value of this guarantee is equal to the fixed amount at 1 April 2008 and affects **U** in the same way as a type B certificate.

### **cprm commentary**

The 2009/10 PPF levy was intentionally specified well in advance of the applicable year to help trustees and sponsors manage their scheme finances by providing a bit more certainty. Implementing any of the above certificates requires submission by the specified deadlines in a very specific format. For contingent asset certificates, legal advice will be required, but this could be a viable opportunity for sponsoring employers to reduce the assessed risk to their schemes and hence reduce the PPF levy. As all the factors are now known in advance, it should be possible to estimate the levy due in 2009/10 and provide an analysis on how the results would be affected if any of the above options were to be put in place.