PENSIONS AND
LIFETIME SAVINGS
ASSOCIATION

PENSION PROTECTION FUND CONSULTATION ON 2023/24 LEVY RULES: PLSA RESPONSE

10 NOVEMBER 2022

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ABOUT THE PENSIONS AND LIFETIME SAVINGS ASSOCIATION

The Pensions and Lifetime Savings Association is the voice of workplace pensions and savings. We represent pension schemes that together provide a retirement income to more than 30 million savers in the UK and invest more than £1.3 trillion in the UK and abroad. Our members also include asset managers, consultants, law firms, fintechs, and others who play an influential role in people's financial futures. We aim to help everyone achieve a better income in retirement.

Pensions and Lifetime Savings Association
24 Chiswell Street,
London,
EC1Y 4TY

T: 020 7601 1700
E: plsa@plsa.co.uk

www.plsa.co.uk

GENERAL COMMENTS

We are pleased to provide this submission in response to the PPF's consultation on the proposed changes to its 2023/24 Levy Rules (the **Rules**), which were released on 29 September 2022.

The PLSA and its members welcome the reduction in levy collection to £200m in 2023/24, representing an almost halving of the £390m levy amount collected in 2022/23.

The PLSA has previously called for a lower levy in response to increasingly high levels of PPF surplus over the years. As such, we support the PPF's recent announcement that it will significantly lower its levy.

We note the PPF's analysis that this reduction to the overall levy will result in around 96% of levy payers expecting to see a reduction in their risk-based levy from 2022/23 to 2023/24, with an expected average reduction of over 50%. This would be a welcome outcome for our DB members and for the industry in general.

Consultation response:

The PLSA and its members fully support the PPF's proposal to significantly reduce the levy amount to be collected in 2023/24 to £200m (down from £390m in 2022/23).

On the longer-term proposals, the PLSA again generally welcomes the intention to move to a simpler levy model, although we note that the move to greater reliance on a scheme-based rather than risk-based levy may raise some concerns that large, well-funded and well-run schemes may bear the bulk of the burden of future levies. As such, we believe it is important that the distributional effects can be demonstrated, even if overall levies are declining, thereby reducing the burden on schemes and employers. That said, the 'rebalancing' of the risk-based levy to emphasise underfunding with a reduced focus on employer insolvency seems sensible and would likely introduce greater predictability in future levies – making budgeting by schemes easier. We also recognise that some of the changes will require primary legislation and that the PPF is working closely with the DWP in this regard. We look forward to providing input into the legislative changes.

As a final overall comment, our members have raised with us the desire for a discussion at some point in the future around the use of the PPF's surplus (which, as noted, has reached almost £12 billion as at 31 March 2022) once all compensation payments have ceased, or are close to ceasing. While we appreciate that this is still some way off, there is a strong feeling by our members that a significant part of the PPF's funding has come from DB schemes and sponsoring employers (along with investment growth and recoveries). Therefore, while we recognise that there is a role for government to play in agreeing the final approach, we believe there is a valid argument that levy payers should have a significant influence on how excess funds are treated at the appropriate time (i.e. during the run-off stage).

We have provided further comments in our response on the specific changes proposed by the PPF on the various aspects of the Rules. These are discussed in the next section.

COMMENTS ON SPECIFIC CHANGES

1. Proposed changes to Levy Rates

As a general observation, we believe there is logic to not making significant changes to the Rules given they are well understood by the industry. In addition, we support the principle that schemes that pose more risk pay more levy; therefore we recognise that the Levy Rates need to rise for each of the ten bands.

That said, we are supportive of the proposed reduction to in the Levy Rates for levy bands 2–10, reducing the band-to-band increase. In our view, the proposal to halve the relative increases between each levy band (as outline in Table 1 of the PPF's Consultation document) will not only reduce the sensitivity of the levy to changes in insolvency risk across the full range of schemes, but it will also reduce the volatility where an employer moves between more than one levy band. We note for example that the difference between levy band 4 and 6 would be 44% under the proposed new Levy Rates (as compared to more than double under the current Levy Rates).

We therefore agree that there is merit in the PPF taking steps now to soften the scale of increases from band to band, in order to facilitate the objective of moving to a simpler levy in the future while, at the same time, reducing the amount of levy the PPF collects in future years.

Consultation response:

The PLSA supports the PPF's proposal to reduce the cliff-edges between the levy bands so that a small movement in insolvency risk has a lower impact on scheme's levy bills.

Note: We make no comment on whether the proposed changes to the Levy Rates will in fact result in the envisaged £60m reduction to the 2023/24 levy collection.

2. Proposed reduction of Levy Scaling Factor and Scheme-based Levy Multiplier

We note that nearly 40% of DB schemes are sufficiently well funded such that they only pay the scheme-based levy, and that the changes to the Levy Rates alone will not deliver the overall reduction needed to the amount of levy collected in 2023/24. Therefore, consistent with the PPF's policy intent for the scheme-based levy to make up a larger proportion of an overall smaller levy, we support the proposal to reduce levies across the universe of levy payers by:

- reducing the Levy Scaling Factor (LSF) from 0.48 in 2022/23 down to 0.37 in 2023/24 (representing a 23% reduction), and
- reducing the Scheme-based Levy Multiplier (SLM) from 0.000021 in 2022/23 down to 0.000019 in 2023/24 (representing a 10% reduction).

In supporting these reductions, the PLSA appreciates that almost all eligible schemes (with the exception of some idiosyncratic cases) will see a reduction in their levy bills in 2023/24.

> **Consultation response:**
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> The PLSA supports the PPF's proposal to reduce the Levy Scaling Factor (LSF) and the Scheme-based Levy Multiplier (SLM), as outlined in the Consultation document.

Note: As with the Levy Rates, we make no comment on whether the proposed reduction in the LSF and SLM will result in the envisaged £60m reduction to the 2023/24 levy collection.

3. Proposal to update the stress factors

Off the back of the joint consultation with The Pensions Regulator (TPR) last year on updated asset categorisation, the PPF is proposing to update its asset and liability stress factors, with the main being to apply one asset stress for all quoted equities at –16%, thereby bringing down the stress previously applied to UK equities from –19%. There are also other changes being proposed, including updated stress factors for fixed interest and inflation-linked bonds, as well as stress factors for newly introduced asset classes such as Diversified Growth Funds (DGFs), Absolute Return Funds (ARFs) and private debt.

We note the PPF's assertion that it does not expect the updated stress factors to materially impact the total amount of levy expected to be collected, albeit individual schemes with a greater allocation to certain types of assets may be more impacted (some positively and some negatively).

The PLSA is broadly supportive of the PPF's proposals with respect to the updated stress factors, particularly the reduction in the negative stress applying to UK equites, which will bring it into line with other quoted equity classes.

We note that the asset stresses generally have been reduced where the asset class was previously used (so stressed assets will be higher) and we welcome this change as it will lead to a reduction in risk-based levies. We also believe the changes to the asset split information are appropriate, given TPR is collecting this information.

> **Consultation response:**
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> The PLSA broadly supports the PPF's proposals with respect to the updated stress factors, particularly the move to apply one asset stress (–16%) for all quoted equities.
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> We also support the proposed changes to the asset split information shown in Table 2 of the Consultation document, to align with the new asset class data being collected by TPR.

It should be noted that a number of our members are still considering the full impact of all the updated stresses on particular asset classes within their schemes, and would welcome further discussions on this in the future, once they have completed their internal reviews.

However, a few uncertainties have been raised with us – for example, the PPF refers to adjusting "certain individual stresses to allow for diversification" benefits, and we agree that they should, but it is not clear that that is what has occurred. The PPF has stated that adjustments have been made to some non-equity asset classes, but it is unclear why some have not been adjusted.

A number of our members have advised the PLSA that they are continuing to work closely with their investment specialists to determine the impact of the updated stresses. Some members will likely reflect their views directly to the PPF in their own responses to the consultation, while others may provide us with further feedback upon the completion of their internal reviews. We will of course convey any further comments we receive from our members on the likely impact of the updated stress factors to the PPF for consideration.

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