

5 Actuarial valuation as at 31 March 2011

Actuarial Valuation of the Pension Protection Fund

To: The Board of the Pension Protection Fund

From: Stephen Rice, Appointed Actuary

The actuarial valuation of the Pension Protection Fund as at 31 March 2011

1. Introduction

The Board of the Pension Protection Fund ('the Board') is required by paragraph 22 of schedule 5 to the Pensions Act 2004 to prepare a statement of accounts in respect of each financial year. Each statement of accounts must contain an actuarial valuation of the assets and liabilities of the Pension Protection Fund prepared and signed by the Appointed Actuary.

This is the sixth actuarial valuation of the Pension Protection Fund. The effective date of this valuation is 31 March 2011. The previous actuarial valuation was as at 31 March 2010, and the report on that valuation was dated 25 October 2010.

At its meeting on 26 April 2006 the Board appointed me to prepare the annual actuarial valuation of the assets and liabilities of the Pension Protection Fund. I intend my report to assist the Board with the preparation of the annual report and accounts as at 31 March 2011 and so I see the Board as the user of this report. As required by paragraph 22(5) of schedule 5 to the Pensions Act 2004, the Board will be sending a copy of this report, as part of the statement of accounts, to the Secretary of State and also to the Comptroller and Auditor General. No party, apart from the Board, the Secretary of State and the Comptroller and Auditor General, should rely on any part of this report.

This report does not contain advice on the funding of compensation payable from the Pension Protection Fund. In particular, the results of this valuation are not used in the determination of the levy. All the results in this report are outcomes of a valuation exercise involving the quantification of amounts for recording in the annual report and accounts.

In my view, while the Actuaries Code issued by the Actuarial Profession applies to the preparation of this report, there are no professional practice standards which directly apply. I have, however, prepared this report having regard to the principles in three Technical Actuarial Standards, namely TAS R (Reporting Actuarial Information), TAS D (Data) and TAS M (Modelling). This report should be considered alongside my supplementary report dated 25 October 2011. As my reports are prepared solely for the purpose of the Annual Report and Accounts of the Pension Protection Fund, I have not produced any projections of future accounting positions in either this or my supplementary report because the Board does not require them for its accounting disclosures.

2. Data

Individual member data was obtained from Capita (the administrators) in respect of former members of schemes for which the Board assumed responsibility on or before 31 March 2011 (although some membership data was missing in respect of one scheme because the full membership data had not been provided to Capita by this date). I have carried out some overall checks on this data for general reasonableness and to ensure that it is consistent with that used in the actuarial valuation at 31 March 2010. A summary of the data as at 31 March 2011 is as follows (figures in brackets are as at 31 March 2010):

Deferred pensioners

Sex	Number	Average age	Total Accrued Pension revalued to 31 March 2011 (uncapped) (£000s pa)
Male	31,395 (20,294)	49.4 (48.9)	116,863 (77,147)
Female	10,668 (5,134)	47.6 (46.9)	21,749 (10,406)
Total	42,063 (25,428)	48.9 (48.5)	138,612 (87,553)

Pensioners

Status	Sex	Number	Average age	Total Compensation at 31 March 2011 (capped where applicable) (£000s pa)
Members	Male	22,003 (14,325)	67.8 (67.8)	103,466 (64,814)
	Female	6,100 (3,145)	68.4 (69.6)	12,621 (6,541)
Depend-ants (excluding children)	Male	361 (183)	70.3 (72.3)	529 (319)
	Female	4,520 (3,039)	73.3 (73.9)	11,846 (7,589)
Children	Male	40 (38)	15.6 (17.3)	78 (80)
	Female	45 (45)	16.1 (17.0)	82 (84)
Total		33,069 (20,775)	68.6 (68.8)	128,622 (79,427)

Individuals who are in receipt of one tranche of compensation as well as being entitled to a further tranche of compensation beginning after 31 March 2011 are included in both tables.

In respect of the one scheme for which the individual membership data was not complete, a loading of 50 per cent was added to the calculated liabilities of the incomplete membership of that scheme. The loading was derived from an analysis of the grouped member data and liabilities provided in conjunction with the scheme's s143 valuation.

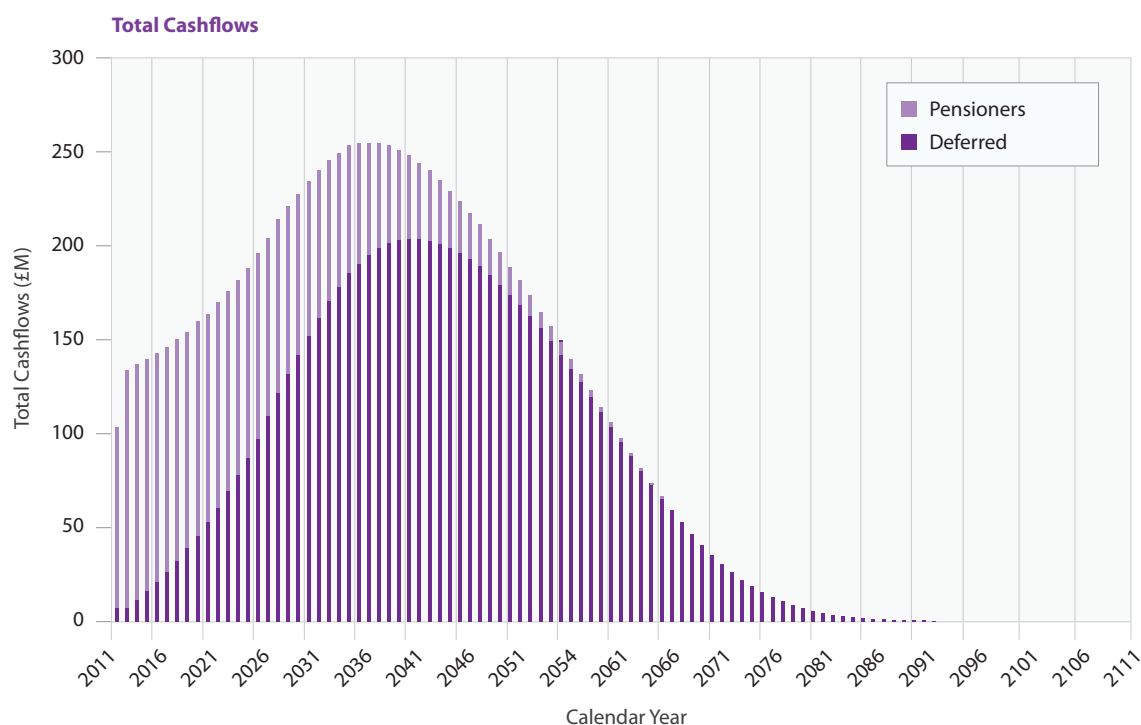
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3. Compensation

The compensation in respect of former members of schemes for which the Board assumed responsibility on or before 31 March 2011 has been determined in accordance with the provisions of Schedule 7 to the Pensions Act 2004 and consequent regulations. A summary of the compensation provisions is shown in Annex M1.

4. Method

In respect of each former member of schemes for which the Board assumed responsibility on or before 31 March 2011, the expected compensation cash flows for each future year are estimated. In estimating each yearly compensation cash flow for each former member, account is taken of the initial amount of compensation or accrued pension, mortality, the Normal Pension Age (NPA) for deferred members, compensation increases and the probability of survivors' compensation being paid. The expected cash flows are shown in the chart below (ignoring early retirement and commutation of annual compensation for a lump sum). Note that this cash flow projection takes no account of schemes for which the Board assumes responsibility after 31 March 2011.



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The resulting yearly compensation cash flows are discounted back to a present value at the valuation date, 31 March 2011, and summed to obtain the actuarial present value of each former member's liability.

The financial and demographic assumptions employed are described briefly in the next section of this report and set out more fully in Annex M2.

The sum of all former members' liabilities is the estimated sum required, based on the financial and demographic assumptions employed, to meet liabilities that have been transferred to the Board's responsibility.

5. Assumptions

In order to estimate future compensation cash flows, I have needed, in respect of the former members of schemes for which the Board assumed responsibility on or before 31 March 2011, to make assumptions about:

- annual increases in payment to that element of their compensation which accrued after 5 April 1997
- revaluation of compensation in deferment for those whose compensation does not begin to be paid until after the valuation date, 31 March 2011
- their future mortality and other demographic features, and
- whether the Secretary of State exercises his / her power under paragraph 30 of Schedule 7 of the Pensions Act 2004 to vary the 100 per cent level of compensation for those members in category 1 of Annex M1 and the 90 per cent level of compensation for those members in category 2 of Annex M1.

In order to determine the present value of the liabilities, I have needed to discount the compensation cash flows, estimated as described above, back to the valuation date, 31 March 2011.

The Appointed Actuary has responsibility for the assumptions used in the statutory valuation of the assets of the PPF and the transferred liabilities, which are the subject of this report. The Board has responsibility for the assumptions used to value the provisions for schemes forming the provisions, as well as contingent liabilities, which are the subject of my supplementary report. Since there is a large overlap in the two sets of assumptions, past practice has been to adopt the same assumptions, as far as possible, for both purposes, which are agreed by the Board.

In proposing the assumptions for the 2011 actuarial valuation, I have taken account of the Accounts Direction which is given by the Secretary of State for Work and Pensions with the approval of HM Treasury in accordance with Schedule 5, Part 4 of the Pensions Act 2004.

Under this direction, the Board is required to prepare accounts in compliance with:

- the accounting principles and disclosure requirements of the current edition of the Government Financial Reporting Manual (the 'FRm') issued by HM Treasury which is in force for the financial year for which the accounts are being prepared
- other guidance issued by HM Treasury in respect of accounts which are required to give a true and fair view, and
- the Framework document agreed with the Board of the Pension Protection Fund.

None of the above provides direction on the choice of assumptions made for the valuation. However, in taking account of these documents and the accounts direction, the Board is required to place a value on the provisions which is best estimate (ie is equally likely to overstate as to understate the actual value). This follows from IAS 37, which the Board is required to take into account in accordance with the FRm. As the same choices of assumptions are made as far as possible for this report as for valuing the provisions the value placed on liabilities of the PPF are also best estimate.

A full description of the assumptions made can be found in Annex M2.

I have also carried out a sensitivity analysis in which the effect on the assets and liabilities is shown by changes in certain key assumptions. The results of this analysis may be seen in the supplementary report which I have prepared concerning the provisions of the Pension Protection Fund as at 31 March 2011.

6. Value of assets

The value of the Pension Protection Fund assets is determined in accordance with regulations 2, 4 and 5 of the Pension Protection Fund (Valuation of the Assets and Liabilities of the Pension Protection Fund) Regulations 2006 (SI 2006 / 597).

I have adopted the value of the assets of the Fund as stated in the relevant accounts prepared by the Board for the financial period ending on 31 March 2011. I have not adopted either of the adjustments made available by regulations 4 and 5 as I considered that it was not appropriate to do so.

Accordingly I have taken the value of the assets of the Pension Protection Fund as at 31 March 2011 as £6,602,136,000. This includes £1,998,000 in respect of AVC assets that match AVC liabilities yet to be discharged.

This compares with £4,658,671,000 as at 31 March 2010.

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An analysis of the change in the value of the assets of the Fund between 31 March 2010 and 31 March 2011 is as follows:

	£000s
Value of assets at the start of the year (31 March 2010)	4,658,671
Assets for schemes entering the PPF during the year to 31 March 2011 (measured at their transfer dates)	1,025,682
Income from Pension Protection Levies	668,460
Compensation paid	(119,457)
Change in current assets (AVCs to be discharged)	1,074
Change in value of interest rate swaps and inflation swaps	91,445
Change in value of invested assets on account of changes in bond yields	47,508
Change in value of invested assets on account of other changes (excluding bond yields, interest rate swaps and inflation swaps) net of investment management expenses.	228,753
Value of assets at the end of the year (31 March 2011)	6,602,136

7. Value of liabilities

The value of the Pension Protection Fund liabilities is determined in accordance with regulation 3 of the Pension Protection Fund (Valuation of the Assets and Liabilities of the Pension Protection Fund) Regulations 2006 (SI 2006 / 597). This requires that:

- (a) the liabilities of the Pension Protection Fund shall be any sums or properties falling to be paid or transferred out of the Fund required to meet liabilities listed in section 173(3) of the Pensions Act 2004, and
- (b) the value of a liability shall be the present value of that liability at the valuation date.

The actuarial liabilities in respect of former members of schemes for which the Board assumed responsibility on or before 31 March 2011, on the assumptions described in section 5 and Annex M2, are summarised in the table below:

Type of member	£000s
Deferred pensioners	2,079,544
Pensioners	1,827,782
Administration expenses to be met from the Fund	75,000
Current liabilities (AVCs to be discharged)	1,998
Total	3,984,324

Accordingly I have taken the value of the liabilities of the Pension Protection Fund as at 31 March 2011 as £3,984,324,000.

This compares with £2,447,969,000 as at 31 March 2010.

An analysis of the change in the actuarial liabilities between 31 March 2010 and 31 March 2011 is as follows:

	£000s
Actuarial liabilities at the start of the year (31 March 2010)	2,447,969
Liabilities for schemes entering the PPF during the year to 31 March 2011 (measured at 31 March 2011)	1,490,685
Effect of passage of time on discounting	21,420
Actuarial (gain) / loss due to change in financial assumptions	107,111
Actuarial (gain) / loss due to changes in mortality assumptions	(46,929)
Actuarial (gain) / loss due to experience being different from what was assumed*	22,176
Change in expense allowance**	60,275
Compensation paid	(119,457)
Change in current liabilities (AVCs to be discharged)	1,074
Actuarial liabilities at the end of the year (31 March 2011)	3,984,324

* Mainly due to actual increases to pensions both in payment and in deferment being higher than assumed

** See section vii) of Annex M2 for a description of the changes incorporated for expenses

8. Conclusion

The balance sheet in respect of the assets and liabilities of the Pension Protection Fund determined in accordance with regulation SI 2006 / 597 is as follows:


	£000s
Assets	
The value of the Pension Protection Fund assets determined in accordance with the Pension Protection Fund (Valuation of the Assets and Liabilities of the Pension Protection Fund) Regulations 2006	6,602,136
Total assets	6,602,136
Liabilities	
The actuarial liabilities in respect of former members of schemes for which the Board assumed responsibility on or before 31 March 2011	3,907,326
Allowance for certain expenses that are met from the Pension Protection Fund	75,000
The remaining liabilities under Regulation 3 of the Pension Protection Fund (Valuation of the Assets and Liabilities of the Pension Protection Fund) Regulations 2006	1,998
Total liabilities	3,984,324
Excess of assets over liabilities – before provisions	2,617,812
Funding ratio (Assets / Liabilities) – before provisions	166%

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In respect of the Pension Protection Fund as at 31 March 2011, the value of the assets was £ 6,602,136,000 and the value of the liabilities (including those in respect of former members of schemes for which the Board assumed responsibility on or before 31 March 2011) was £ 3,984,324,000.

The excess of assets over liabilities of £ 2,617,812,000 in the Pension Protection Fund as at 31 March 2011 needs to be understood in the context of additional pension schemes that had entered into an assessment period, as defined in section 132 of the Pensions Act 2004, with effect from a date on or before 31 March 2011. Therefore, in addition to this formal report on the assets and liabilities, I have estimated provisions in respect of the assets, potential recoveries and liabilities of those schemes which, in the Board's judgement, are likely to be transferred into the Pension Protection Fund. These provisions are shown in my supplementary report to the Board dated 25 October 2011 and will be shown in the statement of accounts being prepared by the Board for the financial period ending on 31 March 2011.

I have also estimated contingent liabilities as at 31 March 2011, including those in respect of other pension schemes which, in the Board's judgement, may possibly be transferred into the Pension Protection Fund in the near future. These contingent liabilities are shown in my supplementary report to the Board dated 25 October 2011 and will be disclosed in footnotes to the statement of accounts prepared by the Board for the financial period ending on 31 March 2011.

Signed: 

Date: 25 October 2011

Name: Stephen Rice, Appointed Actuary

Job Title: Chief Actuary

Qualification: Fellow of the Institute of Actuaries

Employer: The Board of the Pension Protection Fund

Annex M1 Summary of compensation provided by the Pension Protection Fund

Broadly speaking, the Pension Protection Fund provides two levels of compensation:

1. For individuals who have reached their scheme's normal pension age before the assessment date or, irrespective of age, are in receipt of either a survivor's pension or a pension on the grounds of ill health, the Board pays from the Pension Protection Fund -- **100 per cent level of compensation**

In broad terms and in normal circumstances, this means a starting level of compensation that equates to 100% of the pension in payment immediately before the start of the assessment period, as defined in section 132 of the Pensions Act 2004. This is subject to a review of the rules of the scheme by the Board.

The part of this compensation that is derived from pensionable service on or after 6 April 1997 will, from 1 January 2012, be increased each year in line with the increase in the Consumer Prices Index ("CPI") capped at 2.5% and with a floor of 0%. Before this change, the increase was linked to increases in the Retail Prices Index ("RPI"). Primary legislation is planned for later this year in order to enable this change to be made.

2. For the majority of people aged below their scheme's normal pension age the Board pays from the Pension Protection Fund -- **90 per cent level of compensation.**

In broad terms and in normal circumstances, this means 90 per cent of the pension an individual had accrued immediately before the assessment date (subject to a review of the rules of the scheme by the Board) plus revaluation in line with the increase in the RPI between the assessment date and March 2011, and the increase in the CPI between March 2011 and the commencement of compensation payments, subject to a floor of 0 per cent over the whole period, and to a maximum increase of five per cent per annum for the whole period (2.5 per cent per annum for pension accrued on or after 6 April 2009). This compensation is subject to an overall cap, which from April 2011 equates to £33,219.36 per annum at age 65 (the cap is adjusted according to the age at which compensation comes into payment). This revaluation method is a change to previous years when revaluation was linked solely to increases in RPI. Regulations (SI 2011 / 554) requiring the use of CPI in determining revaluation after March 2011 were laid in March 2011.

Once compensation is in payment, the part that derives from pensionable service on or after 6 April 1997 is increased on 1 January each year in line with:

- for years 2011 and earlier, the increase in the RPI capped at 2.5 per cent and with a floor of 0 per cent, and
- for years 2012 and later, the increase in the CPI capped at 2.5 per cent and with a floor of 0 per cent.

Also, there is compensation for certain survivors.

Under the Pensions Act 2004, the Board has a duty to pay compensation on a basis that is no more or less favourable to a woman (or man) than it would be to a comparable man (or woman) in respect of pensionable service on or after 17 May 1990. In meeting this requirement, the Board must take into account any differences in scheme benefits that have arisen owing to differences in the calculation of Guaranteed Minimum Pensions (GMPs) for males and females. The Board has received legal advice confirming the existence of its duty to pay compensation on this basis. The Board has also carried out work on how it might implement equalisation of compensation for members whose schemes have already entered the PPF and on the probable costs of equalisation. These events have led the Board to conclude that it should establish a provision within its financial statements for the cost of equalisation on both the schemes that have transferred to the PPF and those schemes forming the provisions. Additionally a contingent liability is disclosed in respect of the cost of equalisation in respect of other contingent liabilities in the footnotes to the statement of accounts prepared by the Board for the financial period ending on 31 March 2011.

The Board has the power to alter the amount of the levy that it collects (up to the levy ceiling) to meet its liabilities. Additionally, under paragraphs 29 and 30 of Schedule 7 of the Pensions Act 2004, the Board:

- has the power to alter the rates of revaluation and indexation, and
- can recommend to the Secretary of State for Work per cent Pensions that the percentage of benefits paid as compensation is varied.

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Annex M2 Assumptions

a) Compensation levels

As for previous valuations of the Pension Protection Fund, I have continued to assume that the Secretary of State will not exercise her / his power under paragraph 29 of Schedule 7 of the Pensions Act 2004 to vary the 100 per cent level of compensation for those members in category 1 of Annex M1 and the 90 per cent level of compensation for those members in category 2 of Annex M1.

b) Financial assumptions

For the liabilities in respect of transferred schemes I have applied the same rationale in setting the financial assumptions as I did in my report as at 31 March 2010. I consider that it is still appropriate for the financial assumptions to vary according to the term of the particular cash flow being estimated and discounted.

i) Discount rates

I consider that a notional portfolio of assets consisting of cash plus appropriate zero-coupon interest rate swaps contracts and inflation swaps contracts plus gilt strips (or notional gilt strips) provides the best match to the Pension Protection Fund liability cash flows. Calculating the liabilities in this way represents a low-risk approach to the setting of the financial assumptions, in the sense that there should be a low risk of the notional assets being inadequate to pay the PPF members as at the valuation date their full compensation.

Under the terms of a zero-coupon interest rate swap contract with notional principal P and tenor (=duration) N, the Fund would at time N pay interest on P to the counterparty of the London Interbank Offered Rate ("LIBOR") while the counterparty would at the same time pay the Fund a fixed interest rate specified in the contract. Since around August 2008, zero coupon interest rate swap yields for longer tenors have been lower than the gilts strip (one with the individual cash flows stripped out of a gilt) yields at the same duration. It is therefore considered reasonable to construct a notional portfolio so that it contains gilts strips (or more often notional gilts strips) at longer durations and cash and swaps contracts at shorter durations.

Because it is difficult to earn close to LIBOR interest on cash, a deduction is made from the zero-coupon interest rate swap yields of 15 basis points at each term.

The discount rate for each term is therefore taken as the higher of the zero-coupon interest rate swaps yield less 15 basis points and the gilts strip yield.

A zero-coupon interest rate swaps yield curve as at 31 March 2011 was obtained from Insight Investment who constructed the curve by seeking indicative prices from investment banks.

A gilts strip yield curve as at 31 March 2011 was obtained from the UK Debt Management Office. This curve shows gilt strips yields at terms one year to 45 years inclusive. Yields at each of these terms are in respect of bonds with the closest nominal maturity to the indicated term. As the zero-coupon swaps curve and gilt strips curve both extend only as far as term 50 and 45 respectively, I have assumed that these curves remain flat from term 50 and 45 onwards.

In my opinion, the Pension Protection Fund's Statement of Investment Principles is consistent with this discount rate derivation, albeit that the Board takes some extra investment risk in the expectation of outperformance.

ii) Revaluation rates

I have assumed that the Board of the Pension Protection Fund will not exercise its power to amend the maximum revaluation rate of 5 per cent per annum (2.5 per cent per annum in respect of compensation which derives from service after 5 April 2009).

Future revaluations of deferred compensation are now linked to increases in the CPI rather than RPI, as for the previous valuation. In considering what assumption would be appropriate for future CPI increases, I have noted that at present there is almost no market in CPI swaps or indeed any other instruments from which CPI prices can reasonably be inferred. Such limited current market pricing information as is available from investment banks and insurance companies would suggest only a very small gap between CPI-linked prices and corresponding RPI-linked prices. I have therefore assumed, for this valuation, that there will be a zero gap between future CPI increases and future RPI increases. I have further assumed that the rate of future RPI increases, for the period from the valuation date to normal pension age, is determined from the RPI inflation swap curve (supplied as at 31 March 2011 by Insight Investment).

I am aware that there are other methods of deriving a CPI assumption and these include, for example, deducting a best estimate of the future gap between RPI and CPI from the market implied measure of RPI. I do not feel that this method is consistent with the setting of the other financial assumptions. Should a market develop, I expect that a gap will develop between RPI and CPI and I have shown the sensitivity of the balance sheet to there being a gap of 0.5 per cent. This may be seen in the supplementary report which I have prepared concerning the provisions of the PPF as at 31 March 2011.

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The maximum revaluation rate of 5 per cent per annum never applies, for any term, to compensation deriving from service before 6 April 2009. The maximum revaluation rate of 2.5 per cent per annum would apply, for every term, to compensation deriving from service after 5 April 2009. For ease of calculation this upper limit of 2.5 per cent per annum has been ignored. The consequent overstatement of liabilities is insignificant; a rough estimate of the overstatement is less than £500,000.

iii) Pension increase rates

I have assumed that the Board of the Pension Protection Fund will not exercise its power under paragraph 29 of Schedule 7 of the Pensions Act 2004 to amend the maximum annual increase rate of 2.5 per cent per annum, for compensation accrued after 5 April 1997.

As with revaluation, future increases to compensation will be linked to the increase in CPI rather than RPI. Assuming a zero gap between CPI and RPI, my assumption for pension increase rates is therefore derived in the same way as in my valuation report dated 31 March 2010 and this is set out below.

An LPI[0,2.5 per cent] inflation swap is an inflation swap which is subject to an annual floor of 0 per cent and an annual cap of 2.5 per cent. It is used to determine the level of increase that will apply in payment each year. The assumed rate of future post-1997 pension increases was determined from the LPI[0,2.5 per cent] inflation swap curve (supplied as at 31 March 2011 by Insight Investment for terms 5 to 30 years). As at 31 March 2011, it has not been possible to obtain data for terms one to four years because Insight Investment did not receive quotes for trading the LPI[0,2.5 per cent] inflation swap for these years on that day. Insight Investment was, however, able to generate notionally a curve for terms one to four years by assuming that the implied volatilities that can be derived from the more heavily traded LPI[0,3.0 per cent] inflation swap curve were applied to the RPI inflation swap curve. For terms beyond 50 years, I have assumed that the LPI[0,2.5 per cent] inflation swap curve remains flat.

The table below shows the annualised average term-dependent rates of discount, inflation and increases to pensions in payment over the given term. Figures shown in brackets are as at 31 March 2010

Term	Discount rate pa	RPI increase rate pa	Post 1997 pension increase rate pa
1	1.216% (0.893%)	4.115% (2.921%)	2.307% (2.029%)
2	1.730% (1.401%)	3.894% (3.087%)	2.223% (2.038%)
3	2.194% (1.945%)	3.667% (3.099%)	2.183% (2.037%)
4	2.572% (2.388%)	3.498% (3.125%)	2.152% (2.043%)
5	2.882% (2.750%)	3.398% (3.167%)	2.123% (2.035%)
10	3.969% (4.233%)	3.471% (3.466%)	2.145% (2.146%)
15	4.413% (4.666%)	3.614% (3.681%)	2.186% (2.202%)
20	4.638% (4.721%)	3.671% (3.784%)	2.213% (2.236%)
30	4.560% (4.709%)	3.707% (3.804%)	2.237% (2.268%)
40	4.410% (4.528%)	3.683% (3.770%)	2.226% (2.285%)
50	4.286% (4.456%)	3.680% (3.755%)	2.224% (2.286%)

Sources: Insight Investment
UK Debt Management Office (for discount rates with terms 8 years and over)

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c) Demographic assumptions

i) Mortality

The assumption for mortality is in two parts. The first part is the assumption about baseline mortality. This reflects the rate at which people have been dying in the recent past. The second part of the assumption is an estimate of how mortality rates will change over time. Taken together, these assumptions reflect my best estimate of the mortality that will be experienced by members of the PPF (ie it is my view that the assumption is equally likely to overstate as to understate actual experience).

• Baseline mortality

For the valuation as at 31 March 2010, standard tables produced by the Continuous Mortality Investigation (CMI) of the UK Actuarial Profession from the pensioner mortality experience of self-administered pension schemes (SAPS) were used as base tables. The table actually used for any particular member depended on:

- member status (ie deferred pensioner, pensioner, or dependant)
- sex, and
- amount of compensation.

I have concluded that there is a significant gain in precision if account is also taken of an additional factor; namely lifestyle, as proxied by post-code. Club Vita, a mortality analyst, by analysing a large amount of data from its members (including the PPF), has provided the PPF with 149 different mortality curves to apply to the transferred membership. These curves are based on mortality experienced over the period 2006-2008, and vary one from another according to member status, sex, amount of compensation and post-code.

• Allowance for changes in mortality over time

For the valuation as at 31 March 2010, I adopted the CMI-2009 mortality projection model which made available for the first time a different approach to projecting changes in mortality rates over time. As well as reflecting a change in methodology, the new model also incorporated new data on how mortality in England and Wales has changed in recent years.

This model was adopted in its core form, without advanced parameterisation, setting a long-term improvement rate of 1.5 per cent per annum for both men and women. I have seen no evidence to suggest that the long-term improvement rate should be changed from my assumption adopted last year.

Since the previous valuation, the CMI has updated the CMI-2009 model to take account of more up to date data. I have therefore adopted the CMI-2010 mortality projection model in its core form, without advanced parameterisation, setting a long term improvement rate of 1.5 per cent per annum for both men and women for this valuation. In standard notation, my assumption for men is denoted CMI_2010_M [1.5 per cent] and for women is denoted CMI_2010_F [1.5 per cent].

It should be recognised that there is a substantial element of subjectivity about mortality assumptions and that different actuaries will come to different conclusions. The appropriate mortality assumption for future valuations will be kept under review.

• Life expectancies implied by the mortality assumptions

The following table illustrates the range of cohort life expectancies of pensioners aged 65 on 31 March 2011 and non-pensioners from age 65 aged 40 on 31 March 2011 (based on the mortality assumptions being used for this valuation). Cohort life expectancies are based on the age-specific mortality rates allowing for projected changes in mortality. The figures in brackets show the cohort life expectancies based on the assumptions adopted in my valuation as at 31 March 2010. One source of the difference between the 2010 and 2011 expectations of life is due to an additional year's worth of mortality improvements in the 2011 figures. As a result of using post code analysis in the baseline mortality assumption, there are significantly more mortality curves used in this valuation than in the previous valuation. This gives a wider range of life expectancy than would have been seen last year.

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Men

Membership group	Minimum life expectancy in years	Maximum life expectancy in years	Range of life expectancies, in years, within which 75% of all accrued annual compensation lies	Average life expectancy in years (weighted by annual compensation)
Pensioners:				
- Members	17.2 (19.9)	25.9 (24.1)	20.1-24.3 (21.6-24.1)	21.5 (21.6)
- Dependants	16.0 (19.9)	20.9 (24.1)	19.5-20.9 (19.9-19.9)	19.5 (19.9)
Male Non-pensioners:				
- Members	20.4 (23.0)	28.8 (27.0)	23.1-26.1 (24.5-27.0)	24.4 (24.5)
- Dependants	19.1 (23.0)	24.0 (27.0)	22.6-24.0 (24.5-27.0)	22.6 (24.5)

Women

Membership group	Minimum life expectancy in years	Maximum life expectancy in years	Range of life expectancies, in years, within which 75% of all accrued compensation lies	Average life expectancy in years (weighted by annual compensation)
Pensioners:				
- Members	20.0 (23.4)	26.4 (25.1)	22.7-25.6 (23.4-24.0)	23.9 (24.0)
- Dependants	16.2 (22.6)	27.4 (25.4)	21.7-25.7 (22.6-23.8)	23.8 (23.8)
Non-pensioners:				
- Members	23.2 (26.5)	29.3 (28.1)	25.9-28.6 (27.0-27.0)	27.0 (27.0)
- Dependants	20.0 (25.8)	30.2 (28.3)	25.0-27.8 (27.0-27.0)	26.2 (27.0)

ii) Commutation

No allowance is made for commutation of compensation. Even though estimated cash flows would be affected by making allowances, nonetheless these member options are roughly cost-neutral in that the value of the liabilities is roughly the same whether or not a member commutes pension for cash. The factors used to determine the amount of compensation given up for cash are assumed to change over time (being reviewed at least annually) in order to maintain this cost-neutral position.

iii) Early retirement

No allowance is made for early retirement. Even though estimated cash flows would be affected by making allowances, nonetheless these member options are roughly cost-neutral in that the value of the liabilities is roughly the same whether or not a member retires early. The factors used to determine the reduction in compensation on early retirement are assumed to change over time (being reviewed at least annually) in order to maintain this cost neutral position.

iv) Proportion married

For pensioners:

Where there is provision for survivor pensions for relevant partners an assumption consistent with 90 per cent (males) or 80 per cent (females) at normal pension age.

Where there is no provision for survivor pensions for relevant partners other than legal spouses an assumption consistent with 80 per cent (males) or 70 per cent (females) at normal pension age.

For deferred pensioners:

Where there is provision for survivor pensions for relevant partners an assumption, at the assumed date of retirement or earlier death, of 90 per cent (males) or 80 per cent (females).

Where there is no provision for survivor pensions for relevant partners other than legal spouses an assumption, at the assumed date of retirement or earlier death, of 80 per cent (males) or 70 per cent (females).

These are standard assumptions normally considered appropriate by actuaries measuring liabilities of UK pension funds.

5 Actuarial valuation as at 31 March 2011

v) Age difference between member and dependant

Females assumed to be 3 years younger than males.

This is a standard assumption normally considered appropriate by actuaries measuring liabilities of UK pension funds.

vi) Children's pensions

No specific additional allowance is included for prospective children's pensions. Children's pensions already in payment are assumed to cease in accordance with the compensation entitlement with no allowance for mortality prior to cessation.

vii) Expenses

Since 1 April 2008, certain administration expenses are being met from the Pension Protection Fund rather than from the Administration Fund as happened before that date. Since 1 April 2011 certain other expenses are also being met from the Pension Protection Fund rather than the Administration Fund.

An allowance equal to 1.9 per cent of the value of the liabilities in respect of former members of schemes that have transferred into the Pension Protection Fund before 1 April 2011 has been made in respect of the future cost of expenses to be met from the Pension Protection Fund. This has been derived from a calculation of the present value of the expected future expenses that will be incurred in respect of these members. This calculation was based on the budgeted expenses to be incurred by the Pension Protection Fund in the three years following the valuation date. This compares to an allowance of 0.6 per cent in the previous year's valuation.

5 Actuarial valuation as at 31 March 2011

Actuary's supplementary report as at 31 March 2011

To: The Board of the Pension Protection Fund

From: Stephen Rice, Chief Actuary to the Board of the Pension Protection Fund

Actuarial liabilities, provisions and contingent liabilities of the Pension Protection Fund as at 31 March 2011

1. Introduction

The Board of the Pension Protection Fund ("the Board") is required by paragraph 22 of schedule 5 to the Pensions Act 2004 to prepare a statement of accounts in respect of each financial year. Each statement of accounts must contain an actuarial valuation of the assets and liabilities of the Pension Protection Fund. This actuarial valuation is set out in my report to the Board dated 25 October 2011.

The statement of accounts also contains provisions and discloses contingent liabilities that require actuarial estimation. This report contains these estimates. It also contains actuarial balance sheets for the Pension Protection Fund showing actuarial liabilities and provisions in comparison with the corresponding assets. The Board is responsible for the accounting policies, and this report has been prepared within the framework which it has determined. Although I have not been explicitly commissioned to provide this report, I have, nevertheless, prepared it for the Board and I intend my report to assist the Board with the preparation of the Annual Report and Accounts as at 31 March 2011. I therefore see the Board as the user of this report and no other party should rely on any part of this report.

This report does not contain advice on the funding of compensation payable from the Pension Protection Fund. In particular, the results of this valuation are not used in the determination of the levy. All the results in this report are outcomes of a valuation exercise involving the quantification of amounts for recording in the Annual Report and Accounts.

In my view, while the Actuaries Code issued by the Actuarial Profession applies to the preparation of this report, there are no professional practice standards which directly apply. I have, however, prepared this report having regard to the principles in three Technical Actuarial Standards, namely TAS R (Reporting Actuarial Information), TAS D (Data) and TAS M (Modelling). This report should be considered alongside my report to the Board dated 25 October 2011. As my reports are prepared solely for the purpose of the Annual Report and Accounts of the Pension Protection Fund, I have not produced any projections of future accounting positions in this report because the Board does not require them for its accounting disclosures.

2. Provisions

Under International Accounting Standard 37 (IAS 37) of the International Accounting Standards Board a provision should be recognised when:

- an entity has a present obligation (legal or constructive) as a result of a past event
- it is probable that a transfer of economic benefits will be required to settle the obligation, and
- a reliable estimate can be made of the amount of the obligation.

The application of this requirement in the accounting standard to the Board's statement of accounts as at 31 March 2011 is set out in Annex S1.

3. Contingent liabilities

Under IAS 37, a contingent liability is not recognised as a liability because it is either:

- a possible obligation (it has not yet been confirmed whether there is an obligation that could lead to a transfer of economic benefits), or
- a present obligation that does not meet the recognition criteria in IAS 37 (ie it is not probable that a transfer of economic benefits will be required to settle the obligation, or a sufficiently reliable estimate of the amount of the obligation cannot be made).

A contingent liability should, however, be disclosed if the possibility of an outflow of economic benefit to settle an obligation is more than remote. The application of this requirement in the accounting standard to the Board's statement of accounts for the financial period ending on 31 March 2011 is set out in Annex S2.

The definitions of contingent liabilities are specified by the Board and I have calculated the values accordingly. However, it should be noted that claims arising after 31 March 2011 could arise from sources other than those described in the definitions for the contingent liabilities. For the avoidance of doubt, the contingent liabilities are not meant to represent the expected claims in the coming year.

4. Data

The data used for this valuation is summarised in Annex S3.

5. Compensation provided by the Pension Protection Fund

The compensation provided by the Pension Protection Fund is summarised in Annex M1 of my report to the Board dated 25 October 2011.

5 Actuarial valuation as at 31 March 2011

6. Assumptions

The assumptions used to calculate the actuarial liabilities are set out in full in Annex M2 of my report to the Board dated 25 October 2011.

The set of assumptions used in order to calculate the provisions and contingent liabilities as at 31 March 2011 are in most respects the same as those used to calculate the actuarial liabilities. The differences are shown in Annex S4.

We have performed a sensitivity analysis by amending the valuation basis in key areas. The assumptions adopted for the sensitivity analysis are shown in Annex S5.

To determine whether a provision is required for a scheme it is necessary to determine whether as at the insolvency date the value of the assets was less than the amount of Protected Liabilities (see Annex S1). The assumptions to determine this are derived from market conditions at the date of calculation following the published guidance on undertaking a valuation in accordance with section 179 of the Pensions Act 2004. This guidance is available on the Pension Protection Fund web-site;

www.pensionprotectionfund.org.uk/TechnicalGuidance/Pages/ValuationGuidance.aspx

7. Method to calculate the actuarial liabilities, provisions and contingent liabilities

a) Actuarial liabilities

The method of calculating the actuarial liabilities is set out in my report to the Board dated 25 October 2011

b) Provisions

The method of calculating the provisions varied according to the data that the Board was holding about the scheme as at 30 April 2011.

1. Updated asset value information (as at 31 December 2010 or later) and recent membership data

This information was obtained from certain schemes classified as 'material schemes'. These are schemes which:

- (i) satisfy the definition of a provision as set out in annex S1
- (ii) are sufficiently large. (Starting with the largest scheme by liability, the Board had a target that at least 75 per cent of the total liabilities and provisions of the Pension Protection Fund should be made up of material schemes and schemes which have already transferred to the Pension Protection Fund), and

(iii) actually did provide membership data and updated asset information.

For these schemes, the asset value at 31 March 2011 was determined by rolling forward the updated asset value and making an adjustment for benefits paid between the "as at date" of the assets and 31 March 2011. The liability was determined by generating future cash flows of PPF compensation for the members and discounting to 31 March 2011 using the assumptions set out in annex S4 of this report. No allowance was made for membership movements between the "as at" date of the membership and 31 March 2011 as the majority of data was provided as at or close to 31 March 2011.

Material schemes and schemes which have already transferred to the PPF account for 85 per cent of the total liabilities and provisions, as compared with the target of 75 per cent.

2. A section 143 valuation or a section 179 valuation, but not updated assets and membership data

- A section 143 or 179 valuation was rolled forward to the insolvency date and used as a proxy for a section 143 valuation to determine whether the scheme was in deficit at the insolvency date and therefore whether it should be included in the provisions.
- If the scheme was to be included in the provisions, the resulting section 179 valuation was then rolled forward to 31 March 2011 on the valuation basis using the same methodology.

The methodology consistent with that to be applied for the calculation of levy in the financial year 1 April 2010 to 31 March 2011 was used to roll the s143 / s179 valuation results forward to 31 March 2011, at the same time changing the valuation assumptions to those described in annex S4. The 2010/11 methodology is available in the Pension Protection Levy section of the Pension Protection Fund web-site at:

www.pensionprotectionfund.org.uk/DocumentLibrary/Documents/1011_determination_appendix_transformation.pdf

5 Actuarial valuation as at 31 March 2011

3. A Minimum Funding Requirement (MFR) valuation, but not updated assets and membership data, nor a section 143 valuation nor a section 179 valuation.

The MFR valuation was initially transformed to a section 179 valuation (guidance version G3/A3) at the MFR valuation date using a methodology consistent with that available in the Pension Protection Levy section of the Pension Protection Fund website at

www.pensionprotectionfund.org.uk/DocumentLibrary/Documents/1011_determination_appendix_MFR.pdf

- The resulting section 179 valuation was rolled forward to the insolvency date and used as a proxy for a section 143 valuation to determine whether the scheme was in deficit at the insolvency date and therefore whether it should be included in the provisions.
- If the scheme was to be included in the provisions, the resulting section 179 valuation was then rolled forward to 31 March 2011 on the valuation basis using the same methodology.

4. No updated assets and membership information, nor a section 143 valuation, nor a section 179 valuation, nor a MFR valuation.

It was assumed that the scheme was in deficit at the insolvency date and that the scheme's provision was estimated as the median provision for schemes where data was available.

For all non-material schemes, where information relating to income and outgo was forthcoming, this information was used to provide a more precise estimate of the scheme assets and liabilities as at 31 March 2011 than was available solely using the roll-forward methodology.

In addition to the above, a provision is being set up in this valuation for the cost of equalising compensation that is unequal on account of inequalities in Guaranteed Minimum Pensions (GMPs) accrued between 17 May 1990 and 5 April 1997. This provision is to cover the cost of equalisation both on the liabilities of schemes that have already transferred to the PPF and the liabilities of schemes which contribute to the provisions. Under the Pensions Act 2004, the Board has a duty to pay compensation on a basis that is no more or less favourable to a woman (or man) than it would be to a comparable man (or woman) in respect of pensionable service on or after 17 May 1990, and this includes equalisation for GMPs.

The Board has considered legal advice on how exactly compensation should be equalised to allow for the difference in the GMP formula for UK pension schemes. Loadings have been calculated to apply to compensation payable from Normal Pension Age 60 to 65 inclusive for men and women separately in respect of transferred schemes. These calculations use assumptions that I believe to be appropriate for schemes that have transferred into the PPF. In addition, a loading was calculated for transferred schemes equal to the expected arrears of compensation due to these inequalities in GMPs. A single loading was applied to the liabilities forming the provisions and contingent liabilities equal to the equivalent single loading that would give the total loading applied to transferred schemes. A separate provision has then been set up equal to the cost of equalising compensation for GMPs. Overall, the provision is 2.4 per cent of the actuarial liabilities and liabilities of schemes forming the provisions. This is a weakening of the provision compared to that allowed for in my previous report (three per cent) which takes account of the latest information available. A number of assumptions have gone into the calculation of this provision and some sensitivities to the result have been carried out. By looking at a number of extreme scenarios, I conclude that the impact of equalising compensation for GMPs should be between 2.0 per cent and 3.4 per cent of liabilities and provisions.

c) Contingent liabilities

The method adopted for contingent liabilities was identical to that for provisions where the Board was in possession of a section 179 valuation, except that no additional information was sought. This was the same method as adopted last year.

8. Results of the calculations

The results of the calculations of the actuarial liabilities, provisions and contingent liabilities are set out in Annex S6. We also show the results as at 31 March 2010 using the assumptions set out in the Annual Report and Accounts as at 31 March 2010.

It is my opinion that the data collection processes and calculation methods described in section 7 have resulted in calculations that represent a reasonable estimate of provisions and contingent liabilities in aggregate for the Pension Protection Fund. I recognise that the use of summary data and roll-forward methodologies inevitably introduce approximations into the calculations, but I consider they remain appropriate for calculating aggregate provisions and contingent liabilities for the purposes of this supplementary report.

5 Actuarial valuation as at 31 March 2011

9. Actuarial Balance Sheets

Annex S7 sets out the actuarial balance sheets for the Pension Protection Fund as at 31 March 2011, including the liabilities of the schemes forming the provisions. For this purpose the liabilities are taken to be:

(a) the present value of the liabilities of the Pension Protection Fund to pay sums or transfer property, as required under section 173(3) of the Pensions Act 2004. This includes the liabilities in respect of compensation to members of schemes for which the Board has assumed responsibility. The total value is taken as £3,984,324,000, the same figure as was used in my actuarial valuation report of 25 October 2011

(b) my estimate of the present value of the liabilities of the schemes forming the provisions, as set out in Annex S6 of this report, which amounts to £9,072,227,000, and

(c) my estimate of the present value of the cost of equalising compensation that is unequal on account of inequalities in GMPs, which amounts to £308,989,000.

Accordingly, I have taken the liabilities of the Pension Protection Fund as at 31 March 2011 as £13,365,541,000

In the actuarial balance sheets for the Pension Protection Fund as at 31 March 2011, the assets are:


(a) the value of the Pension Protection Fund assets determined in accordance with regulations 2, 4 and 5 of the Pension Protection Fund (Valuation of the Assets and Liabilities of the Pension Protection Fund) Regulations 2006 (SI 2006/597). This value is taken as £6,602,136,000, the same figure as was used in my actuarial valuation report of 25 October 2011, and

(b) the sum of the estimated values of the assets in the schemes that generated the provisions described in section 2 of this report, plus any anticipated recoveries estimated on a prudent basis (£399,447,000). This figure amounts to £7,440,997,000.

Accordingly I have taken the value of the assets of the Pension Protection Fund as at 31 March 2011 as £14,043,133,000.

10. Reconciliation of the change in the funding position

Annex S8 shows a reconciliation of the opening and closing net funding position in the actuarial balance sheet for the Pension Protection Fund, including the schemes that generate the provisions.

Signed: 

Date: 25 October 2011

Name: Stephen Rice, Appointed Actuary

Job Title: Chief Actuary

Qualification: Fellow of the Institute of Actuaries

Employer: The Board of the Pension Protection Fund

5 Actuarial valuation as at 31 March 2011

Annex S1 Provisions in the Statement of Accounts for the financial period ending on 31 March 2011

The statement of accounts as at 31 March 2011 contains provisions in respect of eligible schemes as defined in section 126 of the Pensions Act 2004 in relation to which:

- an insolvency event notice under section 120 of the Pensions Act 2004 had been received by the Board from an insolvency practitioner on or before 30 April 2011
- the Board had not stated on or before 30 April 2011 that the insolvency event was not a qualifying insolvency event
- the insolvency date was on or before 31 March 2011
- a withdrawal notice under section 122(2)(b) of the Pensions Act 2004 had not been received on or before 30 April 2011 (and, in the Board's judgement, is unlikely to be received) from the insolvency practitioner, and
- as at the insolvency date, the value of the assets was, in the Board's judgement (if the scheme had not yet transferred to the PPF), likely to have been less than the amount of the Protected Liabilities as defined in section 131 of the Pensions Act 2004 (determined on the section 179 basis as at the insolvency date).

Schemes which had, in the Board's judgement, a surplus of assets over the value of the Protected Liabilities at the insolvency date, but which may ultimately enter the PPF have been considered. A provision might be appropriate if there are a significant number of schemes in this position. I do not consider that this is so.

In addition, the position of schemes which, as a result of the valuation process set out in S3, have a surplus of assets over the estimated value of the Protected Liabilities at the valuation date, and therefore contribute a negative amount to the provisions, has also been considered. It might be appropriate to offset some of this negative provision if there are a significant number of schemes in this position because some of these schemes may not ultimately enter the PPF. Again, I do not consider that this is so.

In addition to the above provisions I considered those schemes where a s143 valuation had been completed by the trustees and this showed an excess of assets over Protected Liabilities. These schemes did not, therefore, transfer into the PPF. There is a possibility that some of these schemes will return to the PPF within six months of the s143 valuation being signed

off (for instance if the trustees obtained a buy-out quote that showed a deficit of assets compared with the Protected Liabilities). Of these schemes, it was considered that it was probable one of these schemes would obtain a buy-out quote that showed a deficit of assets compared with the Protected Liabilities. This scheme is expected to have a small surplus which is not material and has therefore been ignored. However, one further scheme has been included as a provision where the s143 valuation shows an excess of assets over Protected Liabilities although the s143 valuation has not yet been finalised. This is because we have information that indicates the scheme will not be able to obtain a buy-out quote that shows an excess of assets over Protected Liabilities.

Additionally, an allowance for insolvency events that occurred on or before 31 March 2011 that have yet to be reported has also been made. This takes the form of an 'IBNR reserve' (Incurred But Not Reported reserve) which is determined by estimating the number of schemes where a claim has been incurred but not reported. This is calculated as a percentage addition to the number of schemes which have been reported and included as provisions. This percentage has been determined from an analysis of the average time lag between insolvency event occurrence and notification of such an event to the Board (via a section 120 notice) with consideration of the proportion of events resulting in a claim, as shown in the following table:

Number of months between insolvency event and Board receipt of S120 notice	Cumulative proportion of notifications received by each point in time
0	56%
1	87%
2	91%
6	96%
9	97%
12	98%
18	99%
37	100%

For this estimated number of schemes where a claim is yet to be reported, the provision is based on the median provision of schemes where a claim has been reported.

Additionally, we monitored the movement of the funding position in respect of schemes forming the provisions from 30 April 2011 to 25 October 2011 and our figures include the observed changes of sufficient materiality.

5 Actuarial valuation as at 31 March 2011

Annex S2 Contingent liabilities in the Statement of Accounts for the financial period ending on 31 March 2011

Five types of contingent liabilities are disclosed in footnotes to the statement of accounts. The definitions are the same as last year.

1. Type 1 contingent liabilities are in respect of eligible schemes as defined in section 126 of the Pensions Act 2004 in relation to which:

- an insolvency event notice under section 120 of the Pensions Act 2004 had been received by the Board from an insolvency practitioner on or before 30 April 2011
- the Board had stated on or before 30 April 2011 that the insolvency event was a qualifying insolvency event
- the insolvency date was on or after 1 April 2011
- a withdrawal notice under section 122(2)(b) of the Pensions Act 2004 had not been received on or before 30 April 2011 (and, in the Board's judgement, is unlikely to be received) from the insolvency practitioner, and
- as at the insolvency date, the value of the assets was, in the Board's judgement, likely to have been less than the amount of the Protected Liabilities as defined in section 131 of the Pensions Act 2004.

2. Type 2 contingent liabilities are in respect of eligible schemes in relation to which:

- an insolvency event notice under section 120 of the Pensions Act 2004 was received by the Board from an insolvency practitioner on or before 30 April 2011
- the Board had stated on or before 30 April 2011 that the insolvency event was NOT a qualifying insolvency event
- in the Board's judgement, a subsequent insolvency event, which will be a qualifying insolvency event, is likely, and
- as at 31 March 2011, the value of the assets was, in the Board's judgement, likely to have been less than the amount of the Protected Liabilities, as defined in section 131 of the Pensions Act 2004.

3. Type 3 contingent liabilities are in respect of eligible schemes in relation to which:

- in the Board's judgement, as at 30 April 2011, no insolvency event has taken place, but the Board is nonetheless expecting to receive an insolvency event notice under section 120 of the Pensions Act 2004 from an insolvency practitioner in the future, and
- the Board has sufficient data about the scheme to be able to make an estimate of a contingent liability.

4. Type 4 contingent liabilities are in respect of schemes where:

- the Dun & Bradstreet failure scores are available to the Board and, based on the data available as at 30 April 2011, the score corresponding to the weighted insolvency probability of the scheme's participating employers was less than 10 (which means the probability of insolvency over the next year was greater than 4.68 per cent), and
- the Board in its view had sufficient information as at 30 April 2011 about the scheme to enable the funding level as at 31 March 2011 to be estimated, and
- as at 31 March 2011, the value of the assets was, in the Board's judgement, likely to have been less than the amount of the Protected Liabilities as defined in section 131 of the Pensions Act 2004.

Out of a population of around 6,500 schemes considered, 160 had a failure score of less than 10 associated with them. Of these 160 schemes, 103 were in deficit.

There is the potential to have a slight overlap with the IBNR reserve referred to in Annex S1. In the context of the total contingent liabilities I would expect the overlap to be trivial.

Type 4 contingent liabilities exclude any scheme already within the provisions or other categories of contingent liabilities.

It should be noted that in practice the schemes contributing to the type 4 contingent liabilities often changes considerably from one year to the next.

5. Type 5 contingent liabilities are in respect of the cost of equalising compensation that is unequal on account of inequalities in Guaranteed Minimum Pensions (GMPs) accrued between 17 May 1990 and 5 April 1997.

Under the Pensions Act 2004, the Board has a duty to pay compensation on a basis that is no more or less favourable to a woman (or man) than it would be to a comparable man (or woman) in respect of pensionable service on or after 17 May 1990.

A contingent liability has therefore been established for the cost of equalising compensation in respect of contingent liability types 1 to 4 above.

5 Actuarial valuation as at 31 March 2011

Annex S3 Data

a) Data in respect of former members of schemes that were transferred to the Board on or before 31 March 2011

This data was shown in my report to the Board dated 25 October 2011.

b) Data in respect of provisions and contingent liabilities

There are 314 schemes which contribute to the provisions figure in the statement of accounts for the financial period ending on 31 March 2011 (and a further eight schemes included via the IBNR estimate); liabilities in respect of another 55 schemes have not been recognised (ie not included in the provisions) because the value of their assets was, in the Board's judgement, likely to have exceeded the amount of the Protected Liabilities at their insolvency date. For Type 1 contingent liabilities this recognition test was also undertaken at the insolvency date. For Type 2, Type 3 and Type 4 contingent liabilities the recognition test assessment was undertaken at the valuation date since a qualifying insolvency event had not occurred.

A database is maintained for schemes forming the provisions. Data used to identify these schemes is obtained from information sent to the PPF on an employer's insolvency. This data is updated when new information arises. For instance, when a claim is rejected by the PPF, the database is updated to reflect this information and the scheme is no longer included in the provisions calculations. In addition, the data used to place a value on the schemes forming the provisions is updated to allow for new information received by the PPF. We start off with data in relation to a s179 or MFR valuation which we already hold for the purposes of invoicing for levies, but as schemes near the end of their assessment period we will obtain a s143 valuation and the data from this will substitute any previous data held once there is confidence in the results of the s143 valuation. In other cases, for instance material schemes, the PPF will actively seek additional information from trustees so as to supplement or replace the data previously held on its database where it feels this will provide a more accurate valuation.

For contingent liabilities, identification is either through the same database as is used for schemes forming the provisions (type 1 contingent liabilities) or from information that the PPF has gathered from other sources (such as Dun & Bradstreet, negotiations with companies and information submitted by the Pensions Regulator). The data used to place a value on these liabilities is taken from the information we hold for levy invoicing purposes. A database is not maintained over time for these schemes. A separate identification of contingent liabilities is made each year for the Annual Report and Accounts and the latest data available is used in the valuation.

The numbers of schemes contributing to the various types of provisions and contingent liabilities are given in the following table:

Liability		Number of schemes recognised	Number of pensioners*	Number of deferred pensioners*
Provision	2011	314 (369 in total)**	72,148	112,454
	2010	317 (376 in total)	74,896	116,124
Provision - IBNR	2011	8 (8 in total)	n/a	n/a
	2010	6 (6 in total)	n/a	n/a
Type 1 contingent liability	2011	1 (2 in total)	235	229
	2010	8 (8 in total)	579	1,074
Type 2 contingent liability	2011	2 (2 in total)	120	168
	2010	4 (4 in total)	253	591
Type 3 contingent liability	2011	10 (10 in total)	6,795	9,356
	2010	12 (17 in total)	3,470	5,277
Type 4 contingent liability	2011	103 (160 in total)	25,297	58,662
	2010	107 (157 in total)	15,254	35,290

* Data in respect of recognised schemes only.

** As at 31 March 2011 we have sought to recognise all segregated parts of schemes as separate schemes. This is the same treatment as was adopted at 31 March 2010.

The valuation of the liabilities of material schemes forming the provisions has been undertaken using membership data, in some cases grouped by age and gender. The valuation of the liabilities of all other schemes forming the provisions and contingent liabilities has not been undertaken using member-by-member data as we do not hold this data. Instead the historic valuation results available for the schemes have been used and rolled forward on a global basis. As such the valuation will not be as accurate as one undertaken using individual membership data for each scheme. This approach, while perhaps inappropriate for valuation purposes for some schemes on an individual basis, in aggregate is, in my opinion, acceptable for estimating provisions and contingent liabilities. Generally there is no reason to doubt the quality of the information provided within a particular scheme's valuation report. It is important, however, to note that any errors contained within the original scheme valuation will carry through to this valuation.

Because of the lack of uniformity of data summaries in individual schemes' valuation reports, it has not been possible to provide any other summary data about schemes in the various liability categories.

As we do not hold member-by-member data for all the schemes forming the provisions, we have not been able to indicate the incidence of cash flows relating to the schemes forming the provisions. However, when collecting data for material schemes we obtained information relating to the pensions in payment and deferred pensions by age band and this indicated that the shape of the cash flows for schemes forming the provisions is not dissimilar to that for transferred schemes.

5 Actuarial valuation as at 31 March 2011

Annex S4 Assumptions

a) Actuarial liabilities

The assumptions adopted were described in my report to the Board dated 25 October 2011

b) Basis adopted for Provisions and Contingent liabilities

1. Discount, inflation and pension increase rates

For the Provisions represented by material schemes we have used the term-dependent rates as described in Annex M2). For the Provisions represented by non-material schemes and Contingent liabilities it is not possible to use term-dependent rates as we do not have individual member data to be able to project cash flows. We have therefore made assumptions about the following:

- discount rate in deferment (net of revaluation increases in deferment – see Annex M1 for a description of these increases)
- discount rate in payment for non-increasing compensation for current pensioners
- discount rate in payment for non-increasing compensation for future pensioners
- discount rate in payment for increasing compensation for current pensioners (net of increases in payment – see Annex M1 for a description of these increases), and
- discount rate in payment for increasing compensation for future pensioners (net of increases in payment – see Annex M1 for a description of these increases).

These financial assumptions have been derived from the term-dependent rates shown in Annex M2. This has been done by assuming that cash flows for provisions will follow the same shape as cash flows for the Pension Protection Fund liabilities.

Single rates of discount, inflation and pension increases were determined so that the present values placed on each of the cash flows for pensioners and deferred pensioners was equal to the present value determined using term-dependent rates. These single rates of discount, inflation and pension increase were then used to determine the net discount rate as set out in the following table. The figures in brackets are those as at 31 March 2010.

Net discount rate	% pa
In deferment	0.8 (0.9)
In payment for non-increasing compensation for current pensioners	4.1 (4.4)
In payment for non-increasing compensation for deferred pensioners	4.4 (4.6)
In payment for increasing compensation for current pensioners	1.9 (2.1)
In payment for increasing compensation for deferred pensioners	2.2 (2.2)

2. Mortality

There is no evidence to suggest that my assumption for the base mortality or long term mortality improvement used in my previous report should change, other than to adopt the latest update to CMI 2009 model for mortality improvements. The mortality baseline in respect of a member is, therefore, S1PMA (men) and S1PFA (women) with future changes in line with CMI_2010_M [1.50 per cent] and CMI_2010_F [1.50 per cent] for men and women respectively. For the member's dependant, the baseline is S1DFA (female dependants) and S1PMA (male dependants) with future changes in line with CMI_2010_F [1.50 per cent] and CMI_2010_M [1.50 per cent] for female and male dependants respectively. These baseline tables and future projections have been issued by the CMI.

Because the liabilities of non-material schemes' provisions and contingent liabilities are calculated by rolling forward the results of an earlier valuation, it is not possible to use the chosen assumptions precisely. Instead, all members of non-material schemes are assumed to be male and their dependants assumed to be female. Ratios of annuity values using male mortality are therefore used in the transformation of the valuation result. This straightforward and tractable approach is fit for purpose since men comprise the majority of pension scheme liabilities.

The possibility of scheme-specific mortality was considered for large schemes satisfying the following definition:

- Liabilities at the section 179 (or section 143) valuation date were at least £200 million on the section 179 (or section 143) basis.

Scheme-specific mortality was adopted where the Board had evidence that future mortality for large schemes as defined above was likely to be significantly different from the assumptions set out in the first paragraph. In consequence, in respect of one large scheme where in my opinion there is evidence that mortality is likely to prove significantly heavier than that described above, I have reduced the liability by assuming that the probability of death at each age will be 110 per cent of that used for all other schemes in assessment.

5 Actuarial valuation as at 31 March 2011

3. Proportion Married

80 per cent of members are assumed to be married or to have a relevant partner. Again, because the liabilities are calculated by rolling forward the results of an earlier valuation it is not possible to use sex-specific proportions married.

4. Age difference between member and dependant

Females assumed to be three years younger than males.

5. Children's pensions

No specific allowance.

6. Expenses

Allowance has been made for expenses incurred by the trustees prior to transfer into the Pension Protection Fund. Allowance has also been made for certain expenses incurred after transfer to the Pension Protection Fund, in respect of schemes which are likely to transfer to the Pension Protection Fund (see Annex M2 of my report to the Board dated 25 October 2011 for an explanation of the additional expenses that are to be met from the Fund with effect from 1 April 2011). These allowances amount to 1.1 per cent of the total provisions over and above the standard expenses allowances under the section 179 valuation methodology.

5 Actuarial valuation as at 31 March 2011

Annex S5 Sensitivity analysis

Results have been calculated on the basis described in annex S4. However, the future is never certain, and a wide range of factors could affect the future finances of the PPF. It is possible to capture some measure of how different possible outcomes for these factors affect the PPF by showing different valuation results using different values for the assumptions set out in annexes M2 and S4. For instance, if recipients of PPF compensation were to live longer than expected, the cash flows out of the PPF would rise, other things being equal. The risks that such a change pose to the PPF can be investigated by showing the results of the PPF valuation modified to reflect different assumptions about mortality rates and longevity. Conversely, if the values of (non-bond) assets held as investments by the PPF and schemes in assessment were to rise by 10 per cent, there would be more assets to meet liabilities, which, other things being equal, would be unchanged.

The scenarios considered are as follows:

Scenario 1: Assumptions based purely on the swaps curve at 31 March 2011 but with a deduction of 15 basis points at each term.

Scenario 2: Assumptions based purely on the gilts curve at 31 March 2011.

Under scenarios 1 and 2 the effect of the basis change is on the actuarial liabilities and on the liabilities forming the provisions. For the avoidance of doubt, scenario 1 assumes that the discount rates used for the 31 March 2010 valuation applied as at 31 March 2011.

Scenario 3: Assumes nominal yields increase by 0.5 per cent.

Scenario 4: Assumes nominal yields decrease by 0.5 per cent.

Scenario 5: Assumes that inflation increases by 0.5 per cent at each term.

Scenario 6: Assumes that inflation decreases by 0.5 per cent at each term.

In scenarios 3 to 6, we have looked at the effect on the invested assets and assets in respect of schemes forming the provisions as well as the effect on the liabilities.

Scenario 7: Assumes that increases in the Consumer Prices Index will be 0.5 per cent lower than increases in the Retail Prices Index, (ie assuming that a market had developed in CPI and that it was priced at 0.5 per cent below RPI).

Scenario 8: Assumes that the probability of death in each year of age is 90 per cent of that used in the main basis. Liabilities change by a similar order of magnitude in the opposite direction if the probability of death in each year is 110 per cent of that used in the main basis.

Scenario 9: Assumes that the long term projection in mortality improvement is increased by 0.5 per cent to 2.0 per cent per annum. Liabilities change by a similar order of magnitude in the opposite direction of the rate is decreased by 0.5 per cent to 1.0 per cent per annum.

Scenario 10: Assumes non-bond type assets decrease by 10 per cent at 31 March 2011. Assets change by a similar order of magnitude in the opposite direction if these assets are assumed to increase by 10 per cent.

Scenario 11: Assumes that the age difference between men and women decreases by one year so that men will be two years older than their spouse or partner. Liabilities change by a similar order of magnitude in the opposite direction if the age difference increases by one year.

Scenario 12: Assumes that the proportion of married members increases by 5 per cent. Liabilities move by a similar order of magnitude in the opposite direction if the proportion married decreases by 5 per cent.

Scenario 13: Assumptions based on s143 entry valuation basis (effective 1 April 2011).

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A summary of the assumptions is shown below:

	Main Basis	Scenario 1	Scenario 2	Scenario 3	Scenario 4	Scenario 5	Scenario 6
Discount rate in deferment	0.8%	0.4%	0.8%	1.3%	0.3%	0.3%	1.3%
Discount rate in payment for non-increasing compensation for current pensioners	4.1%	3.9%	4.1%	4.6%	3.6%	4.1%	4.1%
Discount rate in payment for non-increasing compensation for future pensioners	4.4%	4.0%	4.4%	4.9%	3.9%	4.4%	4.4%
Discount rate in payment for increasing compensation for current pensioners	1.9%	1.6%	1.9%	2.4%	1.4%	1.8%	2.0%
Discount rate in payment for increasing compensation for future pensioners	2.2%	1.7%	2.1%	2.6%	1.7%	2.1%	2.2%
Non bond assets	Market value	Market value	Market value	Market value	Market value	Market value	Market value
Age difference (male age less female age)	3 years	3 years	3 years	3 years	3 years	3 years	3 years
Proportion married	As in Annexes S4 and M4	As in Annexes S4 and M4	As in Annexes S4 and M4	As in Annexes S4 and M4	As in Annexes S4 and M4	As in Annexes S4 and M4	As in Annexes S4 and M4
Mortality	As in Annexes S4 and M4	As in Annexes S4 and M4	As in Annexes S4 and M4	As in Annexes S4 and M4	As in Annexes S4 and M4	As in Annexes S4 and M4	As in Annexes S4 and M4

	Scenario 7	Scenario 8	Scenario 9	Scenario 10	Scenario 11	Scenario 12	Scenario 13
Discount rate in deferment	1.3%	0.8%	0.8%	0.8%	0.8%	0.8%	0.4%
Discount rate in payment for non-increasing compensation for current pensioners	4.1%	4.1%	4.1%	4.1%	4.1%	4.1%	4.6%
Discount rate in payment for non-increasing compensation for future pensioners	4.4%	4.4%	4.4%	4.4%	4.4%	4.4%	4.6%
Discount rate in payment for increasing compensation for current pensioners	2.0%	1.9%	1.9%	1.9%	1.9%	1.9%	2.1%
Discount rate in payment for increasing compensation for future pensioners	2.2%	2.2%	2.2%	2.2%	2.2%	2.2%	2.1%
Non bond assets	Market value	Market value	Market value	Fall by 10%	Market value	Market value	Market value
Age difference (male age less female age)	3 years	3 years	3 years	3 years	2 years	3 years	3 years
Proportion married	As in Annexes S4 and M4	As in Annexes S4 and M4	As in Annexes S4 and M4	As in Annexes S4 and M4	As in Annexes S4 and M4	As in Annexes S4 and M4 plus 5%	As in s143 guidance (A6)
Mortality	As in Annexes S4 and M4	10% reduction in death rates	2.0% long term mortality improvement	As in Annexes S4 and M4	As in Annexes S4 and M4	As in Annexes S4 and M4	As in s143 guidance (A6)

5 Actuarial valuation as at 31 March 2011

Annex S6 Calculation results

a) Calculation of actuarial liabilities for members who have transferred into the Pension Protection Fund

The actuarial liabilities in respect of former members of schemes for which the Board assumed responsibility on or before 31 March 2011 plus a sum required to meet the remaining liabilities under Regulation 3 of the Pension Protection Fund (Valuation of the Assets and Liabilities of the Pension Protection Fund) Regulations 2006 amount to £3,984,324,000.

b) Calculation of provisions

322 schemes were considered in relation to the provisions in the statement of accounts for the financial period ending on 31 March 2011, yielding the following estimated provisions (a comparison is shown with the equivalent figures from the 2010 Report per cent Accounts using the assumptions described in that report).

The table below shows the estimated assets held at 31 March 2011 in the 322 schemes forming the provisions. It also shows the outstanding anticipated recoveries, the resulting total assets and estimated funding position in respect of those 322 schemes.

<i>All amounts in £000s</i>	31 March 2011	31 March 2010
Assets excluding anticipated recoveries	7,041,550	7,331,853
Anticipated recoveries	399,447	266,927
Total assets	7,440,997	7,598,780
Provisions	9,381,217	9,415,529
Excess of liabilities over assets	1,940,220	1,816,749

The liabilities recognised as provisions are the present value of the liabilities calculated at each valuation date on the relevant basis.

The provision assets have decreased by £157,783,000 and this can be reconciled as follows:

	£m
Assets as at 31 March 2010	7,599
New schemes coming into assessment	1,394
Schemes accepted into the PPF (assets as at the Transfer Date)	(1,025)
Change in schemes' assets on account of known benefits paid out	(408)
Claims no longer considered probable (exits or schemes estimated to be in surplus at their assessment date)	(307)
Claims now considered probable (schemes estimated to be in deficit at their assessment date)	358
Change in schemes' assets on account of other changes (including updated valuation information, changes in recoveries and investment returns)	(170)
	(158)
Assets as at 31 March 2011	7,441

The provision liabilities have decreased by £34,313,000 and this can be reconciled as follows:

	£m
Provision liabilities at 31 March 2010	9,415
New schemes coming into assessment	1,767
Schemes accepted into the PPF (liabilities as at the Transfer Date)	(1,490)
Claims no longer considered probable (exits or schemes estimated to be in surplus as at their assessment date)	(324)
Claims now considered probable (schemes estimated to be in deficit as at their assessment date)	410
Effect of passage of time on discounting	200
Change in schemes' liabilities on account of change in financial assumptions	190
Change in mortality assumptions	31
Change in schemes' liabilities on account of known benefits paid out	(408)
Change in allowance for equalisation of GMPs*	(52)
Change in schemes' liabilities on account of updated valuation information	(463)
Change in allowance for future expenses**	105
	(34)
Provision liabilities at 31 March 2011	9,381

* see section 7(b) of this supplementary report for an explanation of the change in allowance for equalisation of GMPs

** refer to 6. of annex S4 for an explanation of change in expenses

5 Actuarial valuation as at 31 March 2011

c) Calculation of contingent liabilities

The estimated amounts for the various types of contingent liabilities were as follows (a comparison is shown with the equivalent figures from the 2010 Report per cent Accounts under the Main Assumptions basis as described in that report):

Type of contingent liability <i>All amounts in £000s</i>	Estimated scheme funding positions / GMP equalisation costs (for type 5 contingent liabilities) as at 31 March 2011	Estimated scheme funding positions / GMP equalisation costs (for type 5 contingent liabilities) as at 31 March 2010
1	4,388	34,373
2	5,937	8,585
3	227,578	155,385
4	982,161	621,893
5	141,147	115,301
Total	1,361,211	935,537

The liabilities recognised as contingent liabilities are the present value of the deficit calculated at each valuation date on the relevant basis.

Shown below are the total assets and total liabilities that correspond to the above deficits (contingent liabilities). A comparison is shown with the equivalent figures from the 2010 Report per cent Accounts under the Main Assumptions basis.

Type of contingent liability <i>All amounts in £000s</i>	31 March 2011 Assets	31 March 2011 Liabilities	31 March 2010 Assets	31 March 2010 Liabilities
1	25,643*	30,031	65,201*	99,574
2	10,517	16,454	50,871	59,456
3	810,819	1,038,397	398,437	553,822
4	3,814,081	4,796,242	2,508,622	3,130,515
5	N/A	141,147	N/A	115,301
Total	4,661,060	6,022,271	3,023,131	3,958,668

* at this stage it is too early to assess whether any recovery is available for this type of contingent liability so none has been assumed

5 Actuarial valuation as at 31 March 2011

Annex S7 Actuarial balance sheet

On the main 31 March 2011 basis the Pension Protection Fund actuarial balance sheet is as follows:

Assets	<i>£000s</i>
The value of the Pension Protection Fund assets determined in accordance with the Pension Protection Fund (Valuation of the Assets and Liabilities of the Pension Protection Fund) Regulations 2006	6,602,136
The sum of the estimated values of the assets in the schemes that generated the provisions, plus any anticipated recoveries*	7,440,997 **
Total assets	14,043,133
Liabilities	<i>£000s</i>
The present value of the liabilities of the Pension Protection Fund to pay sums or transfer property as required under section 173(3) of the Pensions Act 2004	3,984,324
The present value of the liabilities of the schemes forming the provisions (inclusive of the cost of equalisation for GMP for both the Pension Protection Fund liabilities and the provision liabilities)	9,381,217
Total liabilities	13,365,541
Excess of assets over liabilities	677,592
Funding Ratio (Assets / liabilities)	105.1%

* Inclusive of an allowance for IBNR (scheme assets of £30,040,000 and liabilities of £37,093,000)

** Inclusive of anticipated recoveries of £399,447,000

I have also calculated the actuarial liabilities and the liabilities of the schemes forming the provisions using the bases set out in Annex S5.

5 Actuarial valuation as at 31 March 2011

The balance sheet on the various scenarios (as described in the section on sensitivity analysis in Annex S5) is as follows

<i>All amounts in £m</i>	Main Basis	Scenario 1 2011 Swaps less 15 basis points	Scenario 2 2011 gilts	Scenario 3 2011 Nominal plus 0.5%	Scenario 4 2011 Nominal less 0.5%	Scenario 5 2011 Inflation plus 0.5%	Scenario 6 2011 Inflation less 0.5%
Assets							
The value of the Pension Protection Fund assets	6,602	6,602	6,602	5,994	7,211	6,808	6,396
The values of the assets in the schemes that generated the provisions	7,441*	7,441*	7,441*	6,920*	7,962*	7,732*	7,149*
Total assets	14,043	14,043	14,043	12,914	15,173	14,540	13,545
Liabilities							
The present value of the liabilities of the Pension Protection Fund	3,984	4,262	3,983	3,649	4,354	4,122	3,841
The present value of the liabilities of the schemes forming the provisions	9,381	10,034	9,399	8,630	10,251	9,741	9,048
Total liabilities	13,365	14,296	13,382	12,279	14,605	13,863	12,889
Excess of assets over liabilities	678	(253)	661	635	568	677	656
Funding Ratio (Assets / liabilities)	105%	98%	105%	105%	104%	105%	105%

<i>All amounts in £m</i>	Scenario 7 CPI is 0.5% lower than RPI	Scenario 8 10% reduction in death rates	Scenario 9 Long term mortality improve- ment plus 0.5%	Scenario 10 Non bond type assets fall by 10%	Scenario 11 Age difference reduced by 1 year	Scenario 12 Proportion married increased by 5%	Scenario 13 S143 basis
Assets							
The value of the Pension Protection Fund assets	6,602	6,602	6,602	6,462	6,602	6,602	6,602
The values of the assets in the schemes that generated the provisions	7,441*	7,441*	7,441*	7,252*	7,441*	7,441*	7,441
Total assets	14,043	14,043	14,043	13,714	14,043	14,043	14,043
Liabilities							
The present value of the liabilities of the Pension Protection Fund	3,841	4,085	4,069	3,984	3,958	4,000	4,131
The present value of the liabilities of the schemes forming the provisions	9,048	9,621	9,586	9,381	9,344	9,429	9,487
Total liabilities	12,889	13,706	13,655	13,365	13,302	13,429	13,618
Excess of assets over liabilities	1,154	337	388	349	741	614	425
Funding Ratio (Assets / liabilities)	109%	102%	103%	103%	106%	105%	103%

*Inclusive of anticipated recoveries of £399m

None of these scenarios should be interpreted as upper or lower bounds of the range of reasonable estimates which might be made.

5 Actuarial valuation as at 31 March 2011

Annex S8 Comparison with the funding position as at 31 March 2010

Under IAS 37 a reconciliation is required of the opening and closing net funding position on the actuarial balance sheet, including schemes that generate the provisions. I show this as a table below:

Reconciling item	£m
Excess of assets over liabilities on the actuarial balance sheet at 31 March 2010	394
Change in actuarial liabilities (this is further broken down in section 7 of my report on the actuarial valuation of the Pension Protection Fund)	(1,536)
Change in liabilities for schemes forming the Provisions (this is further broken down in Annex S6)	34
Change in Pension Protection Fund assets (this is further broken down in section 6 of my report on the actuarial valuation of the Pension Protection Fund)	1,944
Change in assets for schemes forming the provisions (this is further broken down in Annex S6)	(158)
Excess of assets over liabilities on the actuarial balance sheet at 31 March 2011	678

The overall impact on the PPF liabilities and the provision liabilities as a result of the change in mortality assumptions for 2011 was a reduction in liability of £30m.

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