Pension Protection Fund Consultation
Changes to Insolvency Scoring Methodology from 2021/22
Institute for Family Business Response

About the Institute for Family Business

The Institute for Family Business (IFB) is the UK's family business organisation, supporting and promoting the UK family-owned business sector through representation, thought leadership, analysis, events and networking.

We work closely with family firms to support them in growing enterprises for generations to come. A central part of our work is to provide educational resources and knowledge-sharing designed to support business owners and those who work in family business. We champion best practice within the family business community and help others to learn from these examples

Family Business and Pensions

Family business is the backbone of our economy, and the bedrock of our communities. In the UK, family firms generate a quarter of GDP and employ over thirteen million people. By their very nature family businesses take a long-term view, building on long-term stewardship of people and resources. Their commitment to passing a healthy business on to the next generation is locked into their corporate DNA.

The family business sector is extremely diverse. Family businesses come in all sizes and are found in all industries and communities across the UK. Whilst the majority of family firms are small or micro businesses, there are around 18,000 medium and large firms.

By their very nature, family businesses take a long-term view, built on long-term stewardship of people and resources. Family businesses have a long history of acting as responsible employers, and this includes their provision of pensions to their employees. Many firms now have significant pension scheme obligations, and family business owners are committed to ensuring that their business is able to meet these sustainably whilst also investing in growth for the future.

New Insolvency Risk Services

Question: Are there any specific improvements you can think of that would help make our new portal more user friendly or helpful?

Question: If you have used our customer support services, do you have any feedback?

On both these issues, we believe it is very early to be asking for feedback on these areas. It is likely most people have not looked at these in a great deal of detail. We believe the PPF should schedule an additional consultation or outreach to ask for specific feedback on this once more people have considered it in detail and more experiences to feed back.

Review of Insolvency Risk Methodology

Question: Do you have any comments in relation to the data changes made?

It's essential that how accounts are interpreted does not make a material difference to the way businesses are scored or charged. If a very prescriptive form or use of words is required it risks penalising the unadvised, rather than those businesses that are more at risk of insolvency. For example, 'unknown' to D&B does not mean necessarily mean 'unknown' to the company.

Question: Do you agree with the approach we propose to filling full/small accounts?

There are circumstances in which being scored on small company accounts scorecard does not accurately reflect the risk that a scheme poses to the PPF. We therefore believe it is important that this option continues to be provided.

However, these issues could be temporary in nature, possibly applying only to a single set of financial statements. We therefore believe that it is disproportionate for the PPF to require a company to continue to provide full accounting information and not be able to opt to return to simply providing small company accounts.

We also note that companies that prepare small accounts are generally by nature of their lower turnover the entities that are most likely to be impacted by additional administration costs. Furthermore, small companies are more likely to sponsor small pension schemes and hence the risk of such a policy leading to selection against the PPF is more limited than were similar options be offered to larger employers.

Question: Do you have any comments on the analysis we have done?

We are pleased to see the addition to the resilience to manipulation section which states that "it is undesirable for the model to inappropriately influence business decisions". We are concerned based on feedback from members that the PPF levy is impacting on business decisions and having a negative impact on business growth.

The analysis conducted considers the number of insolvencies but doesn't weight towards those insolvencies that have the biggest impact on the PPF (i.e. those which result in the largest claims). We believe this should be considered too.

Question: Do you have any comments on the recalibration carried out?

Rebalancing and recalibration is important, especially considering that businesses on scorecard three have likely been overcharged by 38%. However, we are concerned that the recalibration is in some cases leading to some counter-intuitive results, for example the degree to which creditor days are weighted in certain scorecards.

Question: do you agree with the proposed change to replace the mortgage age variable with cash by liabilities?

Question: Do you agree with the proposed change to cap creditor days at 60?

We are pleased to see the removal of the mortgage age variable, although we have concerns about the impact of replacing this with cash to current liabilities. Particularly in relation to the impact this could have on behaviour, and the impact it will have on decision making. For example, businesses could be penalised from using standard commercial cash sweeping arrangements within a group. The framework should be set in a way that doesn't influence business decision making, as included in the 'resilience to manipulation' section of the objectives for the model.

On Creditor Days, not all entities have creditors including holding companies. Creditor Days has always had its limitations, as particular sector (e.g. retail vs construction) have different approaches to financing working capital, leading to some businesses being under or overweighed and it should be reviewed.

Question: Do you agree with the scope of changes that we have investigated?
Question: Do you consider other changes should be investigated?
We do not believe that enough areas have been looked at when considering possible changes that could be made. The model looks almost entirely at financial measures. However, risk of failure and commercial scoring are not driven exclusively by those factors. The PPF should consider other factors and test those non-financial factors, including those that are used by D&B for other scoring.

Factors that should be considered include age of business, location of head office and size of scheme v. size of business. These are not radical changes, but would give a much fuller picture of a business and its ability to support its pension scheme.

Age of business should be included in the scorecard again. We understand that the age of directors' test was removed due to concerns about risk of manipulation. That is not possible with age of company. Businesses could provide the age of the business, which could then be verified by D&B. Similarly, location of head office is easily available information and not easy to manipulate.

Next Steps

Question: Are there any areas you think we should review in the levy framework for 2021/22?
The PPF should reconsult on its self sufficiency strategy. The PPF is now overfunded, and should consider the amount of money they now require to bring in through the Levy system.

Question: Do you agree with our approach to start live monthly scoring with D&B in April 2020?
No, we do not agree with that approach. An April 2020 start date for live scoring is too soon. A later date – for example September 2020 – should be used.

The consultation demonstrates that there will be a significant change in Levy payments for some groups. The PPF should consider phasing in the scoring, and apply a cap of some kind on the level of change that can be applied (perhaps a maximum increase of 100% in the next levy year). This will not make a significant difference to the amount of Levy being collected overall, but could have a significant impact on individual businesses.