

Mr Paul Seymour  
Chairman  
The Board for Actuarial Standards  
Aldwych House  
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LONDON  
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23 May 2008

Dear Paul

We welcome the opportunity to respond to the Consultation by the Board for Actuarial Standards (BAS) on the Exposure Drafts of:

- Conceptual Framework for Technical Actuarial Standards
- Scope & Authority of Technical Standards.

We support the content of the Exposure Drafts subject to the detailed comments set out in the attached Appendices, and subject to testing the working of the Framework as Standards are developed or revised in the months to come.

We therefore strongly suggest that BAS should deliberately leave the finalised draft Conceptual Framework as a working draft for a couple of years, whilst the first few standards are prepared, so that the Framework is not crystallised until experience has been obtained of applying it in practice.

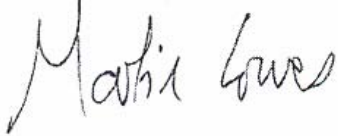
Also, we would encourage BAS to prioritise now its work on the development and updating of technical actuarial standards. There has been no progress on the standards applicable to pension schemes since BAS took responsibility for them 2 years ago. Swift action is now required. In particular, it is not acceptable that there should be no updating of pensions guidance to reflect changes in the legislative, economic and commercial environment before BAS is ready to issue a new format pensions TAS in 2010 – which means that there will effectively have been 4 years of inaction since BAS took responsibility for technical actuarial standards.

We note in this context that in paragraph 32 of the statement of Scope, BAS states that it liaises regularly with the Actuarial Profession regarding areas of practice for which new [and updated?] standards are required. We agree that this is important, and that BAS has received input from the Actuarial Profession. However, we also note that BAS has taken little if any action to date on the feedback it has received from the Actuarial Profession or from actuarial firms. BAS must now act rapidly on the feedback received.

We note BAS would welcome more responses to its Consultation Papers. We suggest that more responses would be likely if BAS issued shorter, better focused, and more accessible documents. We would also expect greater engagement when it is easier to see the real impact of BAS proposals; for example in relation to proposals for actual standards, or in relation to developments of the Conceptual Framework put forward alongside actual standards and including an explanation showing the impact on those standards.

Mr Paul Seymour  
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Yours sincerely

A handwritten signature in black ink that reads "Martin Lowes". The signature is written in a cursive style with a large initial 'M'.

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CPC/ML/JES/BAS Conceptual Framework Response  
Enclosure

## Appendix 1 – Conceptual Framework for Technical Actuarial Standards

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The strategic goal set out in paragraph 1.1 (and referred to in paragraph 2.2) implies that an entity should only be able to get a gold-plated report from an actuary, or nothing at all (but would be able to get a less comprehensive piece of work from a non-actuary). This doesn't reflect reality. Clients often want a "quick and dirty" answer, without all the bells and whistles required for it to be "complete". For example, a manager might ask: "If I was to ask you to advise on the impact of doing X, what might the ballpark impact be". Clearly, the full requirements should apply to the formal report if subsequently commissioned. They are not required for the initial scoping discussion intended only for the purpose of considering whether it is worth commissioning the work. The problem is that BAS seems to have a mindset, displayed in the exposure drafts of the Conceptual Framework, statement of Scope, and Reporting Actuarial Information, that "actuarial information" will always be a long report on the financial management of a financial institution. "Actuarial information" (however defined) covers a much wider spectrum than that, and the Conceptual Framework and statement of Scope (and subsequent Standards) must recognise this, and avoid imposing unnecessary requirements.

Whilst we understand the intent behind the *Uncertainty* precept, we have concerns about how it will be applied:

- Firstly, the giving of actuarial advice may take the form of a process incorporating many steps. Taking the process as a whole, we agree that the various elements contributing to the overall "uncertainty" should be communicated. However, Standards will need to be drafted carefully to avoid requiring duplicated or repetitive communication, and this is covered explicitly in Section 8 of the Exposure Draft of the proposed generic standard on Reporting Actuarial Information. The Conceptual Framework should similarly explicitly acknowledge that it is not necessary for each item of "actuarial information" in isolation to be complete in the sense discussed.
- Secondly, there are items of actuarial information which are calculated using assumptions that have been fixed previously (by legislation, by a regulator, or by the entity) which are not intended as input to any decisions to be taken by the entity. Paragraph 7.3 of the Exposure Draft of the proposed generic standard on Reporting Actuarial Information acknowledges this (although we believe these circumstances occur more widely than envisaged by that Exposure Draft). In these circumstances there is no benefit from a discussion of "Uncertainty" and this should be explicitly acknowledged by the Conceptual Framework. The Framework appears to take a view that "actuarial information" will always be a long report on the financial management of a financial institution. "Actuarial information" (however defined) covers a much wider spectrum than that, and the Framework (and subsequent Standards) must recognise this, and avoid imposing unnecessary requirements.
- Thirdly, clients should be free in most circumstances to request broad brush information that would not be regarded as "complete" (although "complete" information is required for significant decisions).

BAS comments in its Analysis of the Responses to its Consultation on a Reporting Standard that respondents who were concerned over how the proposals would apply to compound advice processes and repeat reports had not read correctly what BAS proposed on these. We do not accept BAS's reaction on this point. Whilst BAS may intend a more proportionate approach, as now set out in the Appendix to that Analysis, the words in the original consultation paper on the Conceptual Framework and Reporting Standard and now in the exposure draft of the Conceptual Framework cannot naturally be interpreted in the way that BAS claim. An Appendix to a feedback document that BAS itself states will have no authority cannot over-ride the apparently more onerous requirements of the Conceptual Framework. The Conceptual Framework needs to state explicitly – along the lines now included in the Exposure Draft on Reporting Actuarial Information - how it applies to compound processes (or equivalently how it defines "actuarial information") and to repeat reports.

The statement in 3.15 that "Management of risk is for managers of the entity" is too sweeping. Even if BAS does not have a role in managing risk, other regulators may have such a role.

We disagree with the statement in 3.18 that the precept of Consistency does not call for the liabilities to be quantified at the current market value whenever the assets are valued in that way. BAS appears here to be falling into the trap of confusing *valuation* and *planning* of which it accuses others of falling into in the discussion of *Liabilities* (precept 1). If the quantification of the liabilities is not the current market value of liabilities, then the quantum is a target asset value, not a value of liabilities that can be regarded as consistent with the market value of assets. If BAS is to have any hope of changing practice in how *planning* measures are communicated, the Framework needs to be consistent in following this distinction.

We disagree strongly with the suggestion in 3.27 that incorporating a margin within the result can avoid a misleading presentation of the entity's financial position. In fact, incorporating a margin within the result will create a biased estimate, which will be positively misleading. We do however agree that widening the range of possible results to reflect data limitations may be appropriate.

The use of the word "risk" in the heading to 3.38 to 3.42 is inconsistent with the distinction between risk and uncertainty in the discussion of the 3<sup>rd</sup> precept in 3.12 to 3.14.

We do not think that assumptions "address" risk as stated in 3.39 – a better word might be "reflect", though we do not agree that there is a 1:1 correspondence between risks and assumptions. The level of assumed new business is an assumption, but it in no way quantifies the possibility or impact of the risk, which is that levels of new business are lower than assumed. We think that paragraphs 3.38 to 3.42 fail to distinguish clearly between the expected or assumed outcome and the quantification of the extent and impact of different out-turns.

Chapter 4 should state that the scope of TASs is limited to actuaries (except where explicitly agreed by the commissioning entity and another adviser).

Paragraph 4.20 implies that TASs apply for example to a non-UK actuary calculating pension cost in respect of a non-UK pension plan for consolidation into the financial statements of a UK parent company (to which UK law applies). BAS does not have any such authority.

We would welcome clarification in the final Conceptual Framework as to whether BAS standards will apply to UK actuaries advising non-UK entities (such as advising on the funding of an off-shore pension scheme). We note that such entities may well cover UK beneficiaries, that such work is covered by current Guidance Notes, and that if BAS standards do not apply, then there may be no other applicable technical actuarial standards or guidance.

The exception for materiality in 5.9 should be incorporated into the drafting in 5.1, which is otherwise contradicted by the first sentence of 5.9. (It is not possible to interpret as encompassing immateriality the limited exceptions applying only in rare cases that are referred to in 5.1.)

In paragraph 5.9, we suggest that the criteria for each departure should be clarified as being "in the reasonable opinion of the actuary" as otherwise it is not clear who is deciding whether the exception applies (for example the client).

In A.7, whilst it is true that the calculated transfer value of a pension is available to the member to apply in a transaction (a transfer to an alternative vehicle), the method of calculation reflects the "planning" approach, as it is derived as the amount of assets the scheme expects to require to provide the promised benefit (or such higher amount as the trustees of the scheme choose to offer).

In A.9, it is unhelpful for BAS to hard code into what is intended to be a long-lived document a criticism of actuaries. In any case, the comment can only be applied to some actuaries, and should be directed much wider than actuaries – it is the government (not actuaries) that have used the word in legislation over many years, leaving actuaries with little choice but to follow the language imposed on them by government. It is also inappropriate, given BAS's own inability to distinguish consistently

between “valuation” and “planning”, e.g. in paragraph 3.18 and A.7. Further, BAS acknowledges in 3.5 that amounts described as “values” but which are not “fair value” or “market value” are used regularly in other disciplines.

## Appendix 2 – Scope & Authority of Technical Standards

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The title should be amended to “Scope & Authority of Technical Actuarial Standards”.

As noted in connection with Chapter 4 of the Conceptual Framework (see Appendix 1), this document should state explicitly that the scope of TASs is limited to actuaries (except where explicitly agreed by the commissioning entity and another adviser). The implicit comment in paragraph 12 is not sufficient.

Again as noted in connection with paragraph 4.20 of the Conceptual Framework (see Appendix 1), paragraph 13 implies that TASs apply for example to a non-UK actuary calculating pension cost in respect of a non-UK pension plan for consolidation into the financial statements of a UK parent company (to which UK law applies). BAS does not have any such authority.

As noted above in relation to the Conceptual Framework, we would welcome clarification in the final statement as to whether BAS standards will apply to UK actuaries advising non-UK entities (eg advising on the funding of an off-shore pension scheme). We note that such entities may well cover UK beneficiaries, that such work is covered by current Guidance Notes, and that if BAS standards do not apply, then there would often be no other applicable technical actuarial standards or guidance.

BAS’s Consultation Paper on the Structure of New BAS Standards states categorically that a number of existing GNs only contain interpretation of legislation, and are therefore out of scope of Technical Standards. Firstly, there is nothing in the Exposure Draft of “Scope & Authority of Technical Standards” saying that such requirements are out of scope of Technical Standards. Secondly, we believe that in order to meet its objectives, BAS will need to include subject matter on interpretation in an actuarial context of legal requirements. Thirdly, the fact that the “Structure” consultation paper can so confidently rely on something that it is in fact not in the “Scope” exposure draft illustrates why the Conceptual Framework and “Scope” should sit for a while as drafts (albeit in final form) whilst the first tranche of Technical Standards are developed, to allow scope for them to be fine tuned in the light of lessons learned from developing actual Standards.

Whilst it is not obvious from the text of this document (in particular from the text of the Schedule), the separate Consultation on the Structure of New BAS Standards suggests that the Pensions Technical Actuarial Standard will cover essentially all advice that relates to the funding and management of a defined benefit pension scheme, rather than just to specified advice. We do not believe that it will be possible to draft generic standards that apply to such a wide range of advice. We do not accept the proposed solution to this problem set out in paragraph 7 of the Analysis of Responses to the Consultation Paper on a Reporting Standard – that if a piece of information is not relevant to a particular report it should be omitted. This suggestion merely turns the generic “standard” into a menu of items that the report writer could consider mentioning, which is not what we would regard as a “standard.”

We note that in paragraph 24 the scope for departures from a TAS are very narrowly drawn, which means that BAS will have to work hard to make sure that each TAS is completely up to date at all times, which is giving itself a tough challenge.

Also, the definitions of Reliability Objective and of paragraph 24 together mean that in any area covered by a TAS, the entity can only get a gold-plated report from an actuary, or nothing at all (but would be able to get a less comprehensive piece of work from a non-actuary). This doesn’t reflect reality. Clients often want a “quick and dirty” answer, without all the bells and whistles required for compliance with the Reliability Objective. This is of concern because, as noted above, it appears that BAS intends to apply the Pensions Technical Actuarial Standard to essentially all advice that relates to the funding and management of a defined benefit pension scheme, rather than just to specified advice. For example, a manager might ask: “If I was to ask you to advise on the impact of doing X, what might the ballpark impact be”. Clearly, the full requirements should apply to the formal report if

subsequently commissioned. They are not required for the initial scoping discussion intended only for the purpose of considering whether it is worth commissioning the work. The problem is that BAS seems to have a mindset, displayed in the exposure drafts of the Conceptual Framework, statement of Scope, and Reporting Actuarial Information, that “actuarial information” will always be a long report on the financial management of a financial institution. “Actuarial information” (however defined) covers a much wider spectrum than that, and the Conceptual Framework and statement of Scope (and subsequent Standards) must recognise this, and avoid imposing unnecessary requirements.