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Dear Louise

## **EXPOSURE DRAFT: REPORTING ACTUARIAL INFORMATION**

I enclose my submission on the BAS's second exposure draft on *Reporting Actuarial Information*.

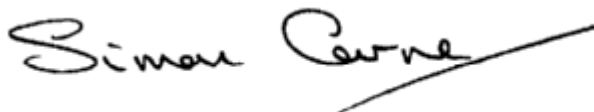
The major part of my paper focuses on Question 8, in which the BAS invites comments on the text of the exposure draft as a means of implementing the policy proposals. For the reasons set out in this submission, I have concluded that the text does not deliver the policies articulated by the BAS. (I have made no substantive comments on the policies themselves, which seem eminently sensible.) In brief:

- The definitions of *aggregate report* and *component report* do not mean what the BAS intends them to mean (see section 1) and the structure of the exposure draft forces the text into a confusing separation of topics (section 2).
- Part of the TAS's stated purpose is that readers should be able to judge the implications of a report, but there is nothing in the exposure draft which delivers this (section 3).
- The exposure draft has virtually eliminated the scope for judgement in implementing the principles, despite the stated policy which is the opposite (section 4). The approach to *materiality* and *proportionality* have the unintended effect of creating an additional disciplinary offence (sections 5 and 6) and the word *material* has two definitions, one of which doesn't always work (section 5).
- The substantive requirement for component reports will not, in practice, achieve the intended goal (see section 7) and the concept of *component reports* may even be redundant (see paragraph 7.9). The proposed approach to reports whose contents are prescribed by regulation is based on the mistaken belief that such reports are component reports, with the result that the exposure draft would require such reports to include inappropriate content (section 8).
- The requirements relating to misunderstandings by users are not complete (section 9).

I have also commented on the proposal to extend the scope of Generic TASs. I have explained that I believe some Reserved Work to be incompatible with TASs and that the inclusion, in scope, of work described as complying with TASs is redundant and outside the BAS's powers (section 11).

My responses to the BAS's eight questions are set out in the Appendix to my submission (see page 20).

Yours sincerely



Simon Carne

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# 1 THE DEFINITIONS OF “AGGREGATE” AND “COMPONENT” REPORTS

## Summary

- 1.1 The definitions of “aggregate report” and “component report” do not deliver the result that the BAS intends for these two terms and, as a result, the definition of “report” does not work either.

## Aggregate report

- 1.2 The first sentence of the definition of “aggregate report” says (paraphrasing):

For each decision taken by a user, [an aggregate report is] the set of all information given to a user in permanent form, material to that decision.

[See paragraph 1.10 for a demonstration that this is a valid paraphrasing.]

### *Why this fails to meet the BAS’s intention*

- 1.3 To see why this doesn’t meet the BAS’s intention, consider an actuarial valuation written up in a single document titled “Valuation Report” and which contains information relating to valuation methods and assumptions, as well as proposals based on the results of the ensuing calculations.
- 1.4 This single document presents information relating to a number of decisions (methods, assumptions and courses of action). But according to the definition, this single document is not one aggregate report; it is several, one for each of the separate decisions that the users will make. Not only that, but any extraneous content of the report, ie content that is not “material” to a decision, is not part of *any* aggregate report, even though it is contained in the document.
- 1.5 Bearing in mind, also, that the various decisions (methods, assumptions etc) will often depend on shared information, the proposed definition of “aggregate report” means that the single document in my example is a collection of overlapping, intertwining aggregate reports plus (possibly) extra material which is not part of any aggregate report.
- 1.6 A corollary to this is that the identification of any individual aggregate report within the document (for example for the purposes of a disciplinary tribunal) would not only be complicated; it would be a matter of judgement (and debate) as to which sentences belong in which aggregate report. This is clearly not what the BAS intends.

### *Cause of the problem: failure to separate definition from requirements*

- 1.7 The inclusion of the phrase “for each decision” was not an accident. It is clear from statements of the BAS in April 2008 (eg paragraph 8.2 of the first exposure draft and paragraph 11 of the accompanying Feedback) that information provided “for each decision” must be compliant with the TAS. This is important. But it is a *requirement* for an aggregate report, not a *definition*. Building requirements into a definition will not work.
- 1.8 Including the phrase “material to [the] decision” within the definition won’t work either. If the report is defined to be only the *material* information, it must follow that *immaterial* information is not part of the report. The requirement at C.4.6 (loosely, not to include immaterial information in an aggregate report if it gets in the way) is automatically met, simply because immaterial information is, by definition, excluded from all aggregate reports, notwithstanding that it might be in the same physical document and obscuring material content in that document.
- 1.9 To make the definition of “aggregate report” deliver the BAS’s intentions, it will need to be restructured, almost certainly so that it revolves around documents, not decisions or

materiality. Without a definition based on documents, I doubt the word “aggregate” can have its intended meaning (see also paragraph 1.25 below).

*Demonstration that my paraphrasing is correct*

1.10 In paragraph 1.2 above, I paraphrased the first sentence of the definition of “aggregate report”, because the actual sentence is complicated, depending, as it does, on a second defined term (“component report”) which is very long. To see that my paraphrasing is valid requires a parsing of the definitions, as follows:

- The first sentence in the definition of “aggregate report” is as follows:

“For each decision taken by a user in connection with work within the scope of this standard, the set of all component reports received by the user containing information material to that decision.” [Highlighting added]

- If we now replace the term “component report” with text from the definition of that term, shown in red below, we get the following

“For each decision taken by a user in connection with work within the scope of this standard, the set of all information which relates to work within the scope of this standard and which is given to a user in permanent form, [either] in hard copy or electronically, consist[ing] of tables, charts and other diagrammatic presentations as well as or instead of text, includ[ing] references to other documents, such as minutes of meetings or public documents received by the user containing information material to that decision.”

- We can now replace some of the words with dots, without changing the meaning, as follows:

“For each decision taken by a user ..., the set of all information ... given to a user in permanent form ... material to that decision.”

This is the paraphrasing I used above (without the dots).

**Component report**

1.11 The definition of “component report” also doesn’t appear to work. The main problem is, once again, the lack of a link to a document. There is also a second problem flowing from the inclusion of permissions within the definition.

*The definition doesn’t actually specify what constitutes a component report*

1.12 The definition of “component report” begins:

“Information which relates to work within the scope of this standard and which is given to a user in permanent form. ... A component report may consist of tables, charts and other diagrammatic presentations ...”

1.13 So a chart printed on a single piece of paper is capable of being a component report. What about two pieces of paper with one chart each: is that one component report or two? What about 30 charts on 30 pieces of paper? It matters because each component report must include the purpose and addressee.

1.14 I am reasonably confident that, where a number of pieces of paper are bound together (either physically or in the electronic equivalent), the BAS intends that this should be *one* component report, but there is nothing in the proposed definition to support that.

*Including permissions within the definition*

- 1.15 The definition of “component report” includes several items expressed in the form of *permissions* (“A component report *may* ...”). Permissions (unlike requirements – see above) are not fatal to a definition if they are truly *part of* the definition. But problems arise when the permissions stray beyond that.
- 1.16 In this case, the definition tries to include five permissions:
- a) hard copy or electronic;
  - b) formal reports, emails etc;
  - c) tables, charts, diagrams as well as text;
  - d) references to other documents; and
  - e) part of one or more aggregate reports.
- 1.17 The first three of these permissions indicate that the definition is to be interpreted broadly and are therefore genuinely part of the definition. The fifth permission is actually nothing at all to do with the definition of component report. It tells us that aggregate reports may have components in common. It should be removed from the definition of component report.
- 1.18 The fourth permission is very strange: it gives permission to do something which is self-evidently permitted. Why would any reader of the TAS imagine that a (component) report would be prohibited from containing a cross-reference to another document? If that needs to be expressly permitted, does that mean there are other innocuous pieces of information that are *not* permitted?
- 1.19 I wonder whether the point intended to be made in the fourth permission is that the document cross-referred to automatically becomes a component report. If not, any material information in the document referred to would have to be repeated in one of the component reports, thereby negating the point of the cross-reference.

*The inclusion of draft reports within the definition*

- 1.20 The inclusion of draft reports within the definition of “component report” has consequences which I am sure the BAS did not intend.
- 1.21 If a draft report is, by definition, a component report – and, therefore, part of an aggregate report – it follows that material which was included within a draft, but omitted from the final version, is still part of the aggregate report. This has adverse repercussions for both the writer and the reader, because it means that:
- a) report writers who mistakenly leave something significant out of the final report will be able to claim they are not be in breach of the TAS if the information was in a draft;
  - b) material which is included in a draft, but later withdrawn, must be expressly contradicted in the aggregate report: deletion from the final version is not enough;
  - c) if the final report is copied to a second decision-maker, all the drafts must be copied across too.
- 1.22 I am sure the BAS intended none of these consequences. I suspect that the intention behind the definition was simply to cover the scenario where the report writer is not able to issue a final report before the decision is made (for example in the context of a takeover) and so tells the user(s) to rely on the final draft. I see no problem with this scenario, so long as the writer *expressly authorises* the user to rely on the draft. It is the

express authorisation (effectively a statement that the report can be read as if the word “draft” was deleted) which enables the draft report to be a component report.

- 1.23 This can be addressed in the TAS by including a *requirement* (not in the definition) that, if a report writer becomes aware that a draft report is to be relied on for a decision, the report writer must *either* give express clearance for the draft to be used in this way *or* tell the decision-maker(s) that the actuarial information is not yet complete. The TAS should also state that:
- a) a draft report which is *expressly authorised* in this way becomes a component report and is treated, for the purposes of the TAS, as if the word “draft” was not there; and
  - b) [as already addressed in paragraph C.2.4] it is the material available at the time of the decision (or, if different, the time when the report writer is told the decision will be made) which determines whether the TAS has been complied with; a report issued after the decision has been made does not contribute to compliance.

*Minor drafting error: copies of presentations*

- 1.24 The fifth line of the definition of “component report” refers to “copies of” presentations. It is a small point (and obviously a drafting slip), but none of the other reporting formats have to be copies, rather than originals, in order to be included in the definition.

**Fixing the definitions**

- 1.25 The definitions can be remedied fairly simply, as follows:

A **report** is a document, or a set of documents, containing actuarial information. An **aggregate report** is the complete set of documents, or the single document if there is only one. Where an aggregate report consists of more than one document, each individual document is called a **component report**. It follows from these definitions that where the TAS uses the word **report** on its own, it denotes either an aggregate report or a component report.

[If thought necessary, the following can be added.] The words “document” and “information” are to be interpreted as widely as their ordinary English meaning permits. Accordingly, documents include electronic versions as well as hard copies; presentations, emails and any other content formats. Information includes tables, charts and other diagrammatic presentations as well as text.

- 1.26 This is by no means the only way to construct the definitions. In particular, my construction above differs from the exposure draft’s construction by basing the definition of “component report” and “aggregate report” on the word “report”, not the other way around. I do this because “report” is being used by the BAS with its ordinary English meaning. That being so, I think lay readers of the TAS will find it very unhelpful that the exposure draft takes 161 words and two sub-definitions to define “report” only to end up with the ordinary English meaning of the word.

## **2 THE STRUCTURE OF THE TAS**

### **Summary**

- 2.1 At first sight, the exposure draft adopts a structure that appears to have an obviously identifiable logic, separating out completeness, relevance, transparency and comprehensibility. But, on analysis, this logic is illusory. The separation doesn’t actually work and (even if it did work) it is not helpful to report writers.
- 2.2 My comments focus on the 60% (approx) of the TAS which form sections C.3 onwards.

## The logic of the structure is invalid

2.3 The separation of the four sections C.3-C.6 (*Relevance, Completeness, Comprehensibility* and *Transparency*) works only if the four subjects are actually distinct from each other. In fact, they are closely overlapping and intertwining, with the result that requirements have been split across multiple headings in a manner that is difficult for the reader to follow.

2.4 Consider the following two examples:

a) For any material calculation, the TAS requires an aggregate report to state:

- the *nature and objective* of the calculation;
- *methods* used to achieve the calculation's objective;
- specific *measure(s)* adopted in the calculation; and
- the *results* of the calculation and *what they represent*;

The first three requirements are set out in the *Completeness* section of the TAS (paragraph C.5.7) and the fourth appears *earlier* in the TAS under *Comprehensibility* (paragraph C.4.10). All four requirements relate to calculations. It is difficult to see why they are split across different sections and even more difficult to see why the last one (what the calculation *represents*) is regarded as a comprehensibility point if the first one (the *objective* of the calculation) is not.

b) For each material uncertainty, the TAS requires an aggregate report to state:

- the nature and extent of the uncertainty; and
- the assumptions used to address the uncertainty.

The first requirement is set out in the *Completeness* section of the TAS (paragraph C.5.1), but the second is left to much later, under *Transparency* (paragraph C.6.4). Again, it is difficult to see the reason for the separation.

2.5 These are just two examples; I could cite more.

## Unhelpful to report writers

2.6 Structuring the requirements section of the TAS around completeness etc is not helpful to the writer. It is not possible to plan or write a report by addressing the goals of completeness, comprehensibility etc in separate steps. A report writer starts with a set of inputs to the report (data, calculations, results, recommendations etc) and develops the report based on those inputs. The fact that completeness etc are overlapping and intertwining (as explained in paragraphs 2.3-2.5 above) exacerbates the problem.

2.7 It is, of course, quite right that the TAS begins (in the first paragraph) with a statement of the overall goal of completeness, comprehensibility etc. But thereafter the TAS really ought to follow a structure that will enable those who must comply with the TAS to relate the requirements to the world they are working in.

2.8 Because the TAS breaks up connected topics in the manner described in paragraphs 2.3-2.5 above, a report writer looking for the requirements relating to a particular topic (eg calculations) must search through all four sections C.3-C.6 (which is more than 50% of the TAS) to be sure to find the complete set of requirements for that one topic. If the TAS remains in the current structure, report writers will call for a "working version" of the TAS for use when writing reports – or else create their own.

- 2.9 The reporting TAS is unique amongst all the proposed BAS standards in that it addresses an aspect of actuarial work which has been identified, repeatedly, as being a weakness for actuaries which needs to be remedied. For example, the FRC, and before that the *Morris Review*, undertook research which reached this conclusion. Putting this a little more bluntly than most actuaries would like, the research says that actuaries have not been effective at communicating.
- 2.10 It is inevitable that the BAS's objectives will not be met in an effective manner if the structure of the TAS doesn't follow a logic which reflects how the inputs to an actuarial report should feature in the report. Addressing this point does not involve re-writing the requirements in the TAS; it simply involves re-sequencing them.

#### **False precedent**

- 2.11 In paragraph 3.9 of the Response section of the Exposure Draft, the BAS said TAS R "will inevitably create a precedent in terms of style and structure for later TASs". I see nothing inevitable about this at all.
- 2.12 As explained in the previous point (see paragraph 2.9 above), research shows that actuaries have not been effective at communicating. It is inevitable that the reporting TAS will not deliver the intended results if it is written in the same style, and with the same structure, as standards for work relating to areas in which actuaries are highly expert. The style and structure of TAS R needs to maximise the effectiveness of the TAS as a reporting standard and not try to set a precedent for other standards.

### **3 THE CENTRAL TENET OF THE TAS IS MISSING**

#### **Summary**

- 3.1 The TAS states that (part of) its purpose is to ensure that actuarial reports include sufficient information to enable the reader to judge the appropriateness and implications of the content. But there is nothing in the TAS which delivers this.

#### **Missing requirement**

- 3.2 It is a central tenet of actuarial communications, and has been for many years (via the PCS), that readers of actuarial reports should be able judge the appropriateness and the implications of the content.
- 3.3 The BAS's acceptance of this tenet is stated clearly in the exposure draft (see paragraph A.1.2) which states that "the purpose of this standard is to ... ensur[e] that ... sufficient information is included to enable users to understand the implications of the contents of the reports" (see also paragraph 4.13-4.14 of the Response section of the exposure draft). A very similar statement is articulated in the FRC's *Quality Framework* published earlier this year and in the first exposure draft of this TAS last year.
- 3.4 Despite all this, there isn't a single reference to "implications" in the current exposure draft other than in its purpose. None of the requirements address the issue. The closest the TAS gets is the requirement for sufficient information to judge the "relevance" of the report (paragraph C.3.1), which covers only a very limited aspect of the intended point.

### **4 THE USE OF JUDGEMENT HAS BEEN SEVERELY CURTAILED**

#### **Summary**

- 4.1 The exposure draft has reduced very significantly the scope for report writers to use judgement. It is clear from the supporting documents that the BAS did not intend this.

## Former Section 7

- 4.2 Paragraph 7.1 of the April 2008 exposure draft included the statement: “judgement is required ... in relation to the decision whether ... the principles should be applied.” The current exposure draft does not contain that statement or anything similar.
- 4.3 The point is exacerbated by a change in the wording used for the individual requirements which are derived from Section 7. Compare, for example, the following wording from paragraph 7.4 of the April 2008 exposure draft with its equivalent in paragraph C.5.7 of the current exposure draft:
- “The description of an actuarial calculation would ***not normally be complete unless*** the following ... have been disclosed ...” [Emphasis added]
- “An aggregate report ***shall include*** explanations of the following for any material calculations ... “[Emphasis added]
- 4.4 The current exposure draft expresses the point in terms which make it compulsory for the information to be reported, rather than allowing for the possibility that the information might not always be needed. I believe that 15 of the 25 requirements in the current exposure draft originate from Section 7 and have all had the judgemental element removed in similar fashion.

## The point goes wider than Section 7

- 4.5 It is not just the 15 requirements from the former Section 7 which have lost the element of judgement. In the first exposure draft, the compulsory element was confined to just four principles. Everything else was commentary or explanation relating to those principles. The significance of this was confirmed by paragraph 9.2 which told us that the way in which the four principles were to be applied was a matter of judgement.
- 4.6 In the current exposure draft, the statement from paragraph 9.2 has been dropped and the four principles have lost their separate identity. The four former principles are now presented in exactly the same way as the other 21 requirements, with the language allowing no element of judgement. This is a hugely significant change. Whereas, before, nothing was compulsory unless it was necessary in order to satisfy one or more of the four principles, now all 25 requirements attract equal compulsion.

## The limited treatment of judgement in the current exposure draft

- 4.7 The current exposure draft tells us *how* to apply judgement (“in a reasoned and justifiable manner” – see paragraph C.2.8) and gives some examples of the need for judgement (not all of them valid – see paragraph 4.8(b) below). But none of this does the job of paragraphs 7.1 or 9.2 of the first exposure draft, which told us that, so long as the four principles are complied with, everything else in the standard was merely indicative of steps which are *likely* to deliver compliance, rather than compulsory.
- 4.8 Moreover, the five examples (set out in paragraph C.2.9) which the BAS says require judgement add very little:
- a) Two of the examples (*materiality* and *proportionality*) merely reiterate what has been stated elsewhere, ie that the standard does not extend to matters which are either trivial or excessive. Neither of these examples permits a report writer to judge that, as a matter of principle, a particular requirement is not applicable to a particular report.
  - b) A third example in paragraph C.2.9 asserts that judgement is required in relation to who the *users* of a report are. This is not a valid example. Whilst it is true that a report writer cannot know in advance who might be given a copy of the report, this uncertainty is not addressed by the writer using their *judgement* to speculate who

those people might be. The writer of the report makes a statement of who is intended to rely on it (paragraph C.3.3 *requires* the writer to do that) and then applies judgement to determine the content of the report in the light of the stated users, not the other way around.

[As an aside, and not something that is necessary for the foregoing argument, I note that deciding who may be a user of the report is actually a matter for the commissioners of the report, taking into account any relevant legislation or regulation, not the writer. The report writer is free to decide whether to accept instructions or to reject them (and to negotiate over the content of the instructions before making that decision). But the report writer does not retain the final say over the instructions, nor over who the users will be – certainly not for work within the scope of this TAS.]

- c) That leaves two examples (the *extent* of a piece of work and the possible *obscuring* of information). Whatever these two examples are telling us, they don't reinstate the freedom to use judgement that was lost when paragraphs 7.1 and 9.2 were deleted.

### **This is not what the BAS intended**

- 4.9 It is quite plain that the BAS did not intend this reduction in judgement. Paragraphs 1.3 and 3.10 of the Response section of the exposure draft tell us:

- 1.3 [The BAS] believe[s] that it is in the nature of principle-based standards that they require judgement to be exercised by those complying with them ...

- 3.10 It is far from our intention to encourage a “tick box” approach ... and we believe that the overall effect of the [exposure draft] will be a move in the opposite direction. Although there may be some superficial resemblance to rules, the proposed content of the TAS is firmly based on principles. Moreover, complying with the requirements (which are expressed in terms of principles) will require the exercise of judgement. We hope that the extent of such judgement is now clearer.

### **The problem lies with the execution, not the policy**

- 4.10 I demonstrated above that, so far as the requirements are concerned, the scope for judgement has been virtually annihilated. I also pointed out that the four principles have ceased to be separately identified and now have the same status as simple rules such as: reports must state who the addressee is; state any TASs complied with; state the meaning of any [ambiguous] terms; include a comparison with the previous report; and many more. Contrary to the quote from paragraph 3.10 above, these examples are not “expressed in terms of principles.”
- 4.11 To be absolutely clear about this: I do not object to the inclusion of (some) rules in a TAS. I accept entirely the BAS's statement in paragraph 2.6 of the Conceptual Framework that TASs will “not exclude specific rules, where appropriate”. Neither do I object to the ideas behind the 25 requirements in the exposure draft.
- 4.12 My point is that, whereas the BAS says in the Response section that judgement is maintained or increased, the draft TAS achieves the opposite. The first exposure draft expressly highlighted the principles, and included extensive permission for report writers to use judgement in applying them. But, in the current exposure draft, the freedom to use judgement has all but been reduced to materiality and proportionality.

## 5 MATERIALITY

### Summary

- 5.1 The definition of “material” contains two sentences, but they aren’t consistent with each other or with the definition in the *Scope & Authority* document.

### Two definitions where one will do

- 5.2 In the current exposure draft, the definition of “material” uses one formulation for the definition of “material departure” and a different formulation for everything else:

- a) “A **departure** from this standard is material if, at the time the work is performed, the effect of the departure could influence the decisions to be taken by the users ...” [Emphasis altered]
- b) “**Assumptions, calculations and other matters** are material if they result in information whose disclosure or misstatement could influence the decisions or understanding of users.” [Emphasis altered]

- 5.3 Why do we need a different definition of “material” when it is applied to something other than a departure (and why were assumptions and calculations listed as special cases)? What is wrong with applying the first definition across the board:

“[Something] is material if, at the time the work is performed, the effect of the [something] could influence the decisions to be taken by the intended users of the work product.”

- 5.4 Not only is definition (b) superfluous, it makes no sense in some instances of “material”. For example, the exposure draft refers “material information” (paragraph C.2.3) and material uncertainty (paragraph C.5.1). Try plugging “information” or “uncertainty” into definition (b) and it doesn’t work: the words “they result in information whose” need to be replaced by “their”. The approach illustrated in definition (a) would work in all cases.

### Incorrect words added to the first definition

- 5.5 In the current exposure draft, the definition of “material departure” introduces extra words that were not present in the *Scope & Authority* (or the *Modelling* consultation). The extra words have unintended consequences.

- 5.6 Previously, the definition referred only to matters which could influence users’ decisions. The revised definition refers not only to the users’ decision, but also “the users’ understanding of the information on which decisions are based.”

- 5.7 Although it is clearly not the BAS’s intention, adding these words to the definition means that a *satisfactory* explanation has the potential to be misconduct, merely because it wasn’t the *best* explanation. This results from the following analysis.

- 5.8 If an explanation can be improved on (in the sense of improving the users’ understanding), the difference between the two explanations is, under the BAS’s proposed definition (but not under mine), “material information.” It follows that, if the best explanation is given orally, but only a satisfactory explanation is put in writing, material information conveyed orally has not been confirmed in a report, contrary to paragraph C.2.6. This is almost certainly not the only adverse consequence.

- 5.9 The extra words should be deleted from the definition of “material”. I share the BAS’s goal of seeking to improve the users understanding of actuarial information, but the comprehensibility requirements are sufficient to deal with explanations that do not meet the minimum acceptable standard. A piece of information should not be regarded as “material” for disciplinary purposes if it cannot affect a user’s decision.

## 6 PROPORTIONALITY

### Summary

- 6.1 The exposure draft makes it a disciplinary offence to include disproportionate content in a report. But supporting documents suggest the BAS intended only that proportionality should impose a limit on the requirements of a standard, not create a new offence.

### Details

- 6.2 The proposal in the current exposure draft is that a disproportionate report should be a disciplinary offence. The wording proposed in the ConDoc says, in effect: "A report must not be disproportionate" (see paragraph 6.4 below for the actual wording). The equivalent proposal in the previous exposure draft was very different. The wording said, in effect: "If this standard pushes you towards anything disproportionate, reign it in so that the content is proportionate."
- 6.3 These are obviously two quite different proposals. In its *Conceptual Framework*, the BAS indicated that it would pursue the initial proposal.
- 6.4 The precise wording used in the current exposure draft and in the previous one are as follows:
- In the current exposure draft, the proposed proportionality principle begins with the words "An aggregate report shall be proportionate to ..." (paragraph C.2.11), ie a report must not be disproportionate.
  - In the previous exposure draft, the proposal contained some crucial extra words which I highlight here in italics: "The information *provided in compliance with this standard* ... should be proportionate to ..." (paragraph 4.1(d)). It is the inclusion of the italicised words which gives this the meaning: "If this standard pushes you towards something disproportionate, reign it in so that it becomes proportionate."
- 6.5 I should add that the wording of the previous exposure draft was not quite right either, because it said, in effect "... reign it in, or be guilty of a disciplinary offence." The wording should probably be adjusted so that it says: "... you *may* reign it in." Without this adjustment, the TAS will sandwich report writers between the requirement to include specified information and a limit on just how much information might be included before it becomes a disciplinary offence.

## 7 THE REQUIREMENT RELATING TO COMPONENT REPORTS

### Summary

- 7.1 The requirement for each component report to include a statement of its purpose and addressees is not a practical way of achieving the BAS's intended goal.

### The objective of the requirement

- 7.2 Paragraph C.3.2 suggests that an aggregate report *may* need to include an indication of its component reports, whilst the paragraph C.3.3 makes it *compulsory* for a component report to include a statement of its purpose and its addressees. As a purely practical matter, and for the reasons explained below, I think the compulsion and the permission are the wrong way around.
- 7.3 Given that the exposure draft permits a component report to be, for example, an email, the requirement to include the purpose and the addressees means that, in practice, the writer will typically need to have anticipated that the email was going to be a component

report – and yet the writer persisted in presenting it as an email, rather than putting it in an attachment to an email and presenting it accordingly.

- 7.4 If the BAS intends that the writer must recognise a document as a component report *at the time of writing it*, the permission to present it as an email serves no purpose. It is only if the BAS's intention is to permit a report writer to adopt an *earlier* email as a component report that the point has any force and any practical merit.

#### **The requirement is effective only if it attaches to the aggregate report**

- 7.5 If the real intent is to allow earlier documents (including emails) to be adopted as part of a report, the practical reality is that it will be the *aggregate* report which identifies the purpose and addressees of the components it adopts and not each individual component. In other words, the second sentence of paragraph C.3.3 should be deleted and the compulsion inserted in paragraph C.3.2, relating to aggregate reports, not components (eg “an aggregate report shall identify each of its component reports and indicate their purpose”).

- 7.6 As a minimum, the aggregate report needs to list, in its final component, all the other components, so that users can make sure that they have received the complete report. Given all the permissions granted by the exposure draft (not least the permission to treat emails as a component), the BAS seems to be content that the final component report might be nothing more than a reading list of all the component reports, in which case the list of components should identify the order in which they are intended to be read.

- 7.7 A more conventional approach would be for the final component to be the report “proper” with cross references to earlier documents, if any, included at the point where they fit into the overall message (with the purpose behind the cross reference made clear).

#### **Status of documents that are cross-referenced in a report**

- 7.8 This all links back to the point I alluded to earlier (see paragraph 1.19 above) regarding the status of documents cross-referenced in a report. If an aggregate report refers to material information contained in another document, *without* repeating that information, the practical reality is that the report writer must intend the cross-referenced document be treated as part of the aggregate report in order to satisfy paragraph C.2.3. If paragraphs C.3.2 and C.3.3 are amended as I proposed above, there need be no problem with that.

#### **Making this all so much simpler**

- 7.9 If we step back from the minutiae of components, aggregates etc, I can't help but wonder whether “component reports” ever needed to be defined. There is only one requirement in the exposure draft which relates to the content of a component report and I have explained immediately above why, on practical grounds, that requirement should be replaced by a requirement for the aggregate report.

## **8 REPORTS PRESCRIBED BY REGULATION**

### **Summary**

- 8.1 Paragraph 3.39 of the Response section of the exposure draft appears to suggest that reports whose contents are prescribed by regulation are component reports. This is not correct. The consequence of this is that the exposure draft would appear to require such reports to include inappropriate content.

## The source of the confusion

- 8.2 In the Response section, the BAS refers to comments received to the effect that difficulties may be encountered complying with TAS R in the case of reports whose contents are prescribed by regulation. This point was actually dealt with in the first exposure draft in paragraph 7.3 which identified such reports as a special case and proposed (in effect) an exemption.
- 8.3 In the current exposure draft, the exemption has been removed and, instead, the BAS has attempted to deal with the point by saying (in paragraphs 3.38-3.39 of the Response section) that the TAS “places few requirements on the contents of individual documents”. This is true only if the individual document is a component report and not an aggregate report – which is not the case, as the following paragraphs demonstrate.

### *Examples*

- 8.4 By way of example, the first exposure draft cited the actuarial valuations required under s143 and s179 of The Pensions Act 2004 in connection with the Pension Protection Fund. For these reports to be only component reports, not aggregate reports, there would have to be other components which make up the aggregate and there aren't.
- 8.5 But one doesn't have to rely on specific examples from current legislation. Where statute or regulation prescribes that a single report be produced, that report will be an aggregate report unless the report writer chooses to write a non-statutory report alongside it. If the statutory report does not comply with the requirements of the TAS (for aggregate reports), the voluntary report will have to do so. This doesn't meet the problem highlighted by commentators (and by the first exposure draft) which is that some statutes call for a report to be written in circumstances where the TAS is simply not applicable.

### *Pension funding reports*

- 8.6 Paragraphs 3.38-3.39 do not specify which reports under the Pensions Act were being referred to. It has been suggested to me by a member of the BAS that the statutory funding valuation reports fall within the ambit of the paragraphs, ie that the BAS believes statutory funding valuation reports are merely component, not aggregate, reports. Again, I think this is mistaken, although this time the analysis is more complex.
- 8.7 The statutory funding valuation, required under s224 of the Pensions Act 2004, is one of a series of pieces of information which the actuary is required to provide for pension schemes. Others are the advice required under s230 of the Act. But as much as this may suggest that the funding valuation is only a component report, that still isn't correct:
- a) The funding valuation report must, by statute, be provided to the employer as well as to the trustees, whereas the s230 advice is for the trustees only (unless they wish to disclose it to the employer). So, even if the funding valuation report could be viewed as a component in the hands of the trustees, it is an aggregate report so far as the employer is concerned.
  - b) Moreover, even if the Act had been worded so that the s224 funding report and the s230 advice had the same users, the first and second exposure drafts both state that the requirements of the TAS need to be met in relation to *each separate decision*. The s230 advice relates to a series of decisions which are distinct and separable from the statutory valuation report. For example, the valuation method and assumptions must each be decided before the valuation report can be finalised.

## The practical issue at the heart of the confusion

- 8.8 There is a danger that, by trying to include the statutory funding valuation along with the s143 and s179 reports in the ambit of paragraphs 3.38-3.39, the BAS is losing sight of

the practical point at the heart of this issue. In the case of s143 and s179 reports, the point (accepted by the BAS) is that the full TAS is not generally applicable, whereas, in relation to the s 224 statutory funding reports, it would drive a coach and horses through the BAS's intentions if these reports were exempt. The reasoning is as follows:

- a) The s143 and s179 valuations are required by the PPF for their own use. The PPF knows quite well why the legislation requires it to receive these reports and the PPF does not need the calculations to be accompanied by the various explanations that the BAS intends report writers to include when communicating actuarial information to trustees of occupational pension schemes. Accordingly, many of the requirements in the proposed TAS do not apply to these two statutory reports (and others like them) and the TAS should not try to apply them.
- b) The opposite is the case for the statutory funding valuation (and other reports addressed to entities themselves). If the statutory funding valuation of occupational pension schemes were exempt from the requirements applicable to an *aggregate* report, pension schemes might never receive some of the information which the exposure draft says should be provided generically.

Examples of information that would cease to be required are the requirements of paragraphs C.5.15 and C.5.18, relating to comparison of calculations with last time and the projection of expected results next time, and the requirements of paragraphs C.5.1 and C.5.4, relating to uncertainty.

### **The way forward**

- 8.9 As indicated above, most statutory reports require the full rigours of the TAS to be applied, but some do not. The reports to which the TAS is *not* applicable are likely to be reports which conform to a statutory template that allows the report writer (and those instructing the report writer) little or no judgement over the content. In relation to those reports, there needs to be a mechanism for exemption from the full rigours of the TAS. But, as also noted above, the concept of component reports does not deliver that exemption, because statutory reports which tightly prescribe the content are, by their very nature, unlikely to be component reports.

## **9 MISUNDERSTANDINGS BY USERS**

### **Summary**

- 9.1 In paragraph C.4.4, which addresses misunderstandings by users, the second sentence seems to be redundant and the first sentence is incomplete.

### **The second sentence is redundant**

- 9.2 The second sentence of paragraph C.4.4 is redundant, because everything it says is already in the first sentence. If the BAS is aware of the redundancy and was seeking to clarify the meaning, the second sentence should begin with words such as "It follows from this requirement that ..." (and the second sentence re-located outside the box).
- 9.3 If the BAS does not recognise the redundancy, I offer the following simple proof. The second sentence differs from the first only by the addition of the words "aggregate" and "component" in front of the word "report". But since "report" includes, by definition, both types of report, the requirement in the second sentence must be a subset of the requirement in the first sentence. It is impossible to construct a scenario which triggers the requirement in the second sentence, without also triggering the first sentence.

## The paragraph is incomplete

- 9.4 It is clear from paragraph C.4.4 that, if a person responsible for a component report becomes aware of a misunderstanding in that component, the exposure draft requires the responsible person to provide an explanation. But it is not clear what the rule is if a person responsible for Component A becomes aware of a misunderstanding relating to Component B of the same aggregate report but which is the responsibility of someone else. It is not clear whether the paragraph requires nothing to happen or it requires the person becoming aware of the problem to make the necessary correction.
- 9.5 I doubt that the BAS intended nothing to happen. But neither it is appropriate for the TAS to demand that the person responsible for Component A must provide explanations relating to Component B. At most, the person responsible for Component A should notify someone responsible for Component B.
- 9.6 There are at least two reasons why the person responsible for Component A should not be required to provide the explanation themselves. The first reason is that one member of the team may be given authority for writing a component report relating to (say) data, but may have no authority (or competence) to write about other matters. Clearly, in these circumstances, the person who took responsibility for the data component should do no more than pass on the evidence of the misunderstanding, rather than being required by the TAS to step in and communicate with the user about a matter that they have no responsibility for (and possibly no competence to address).
- 9.7 A second reason is that there may be a multiplicity of component reports (C, D, E etc), each potentially having separate authors who become aware, simultaneously, of the user's misunderstanding. The correction needs to be a single co-ordinated affair and not a flurry of corrections from one team member after another.
- 9.8 If, therefore, the BAS's intention is that writers of component reports need to take action if they see a *different* component being misunderstood, there needs to be a new sentence to the effect that:

“If a person responsible for a **component report** becomes aware of any evidence of another **component report** within the same **aggregate report** not being understood by any **user**, they shall notify either the person responsible for the other **component report** or a person responsible for the **aggregate report**.”

- 9.9 If, as I suggested in paragraph 7.9 above, the term “component report” is deemed to be redundant, the above sentence is easily amended, for example:

“If a person responsible for part of a **report** becomes aware of any evidence of a different part of the report (ie a part which they are not responsible for) not being understood by any **user**, they shall notify a person responsible for the **report**.”

## A drafting slip

- 9.10 In the first sentence, the *second* reference to “a report” needs to say “that report”. As currently drafted, anyone who ever takes responsibility for a single report under the TAS will be forevermore required to correct any misunderstandings in any TAS R report that they ever come across, regardless of who wrote the misunderstood report – including (as currently drafted) reports written by actuaries from another firm!

## 10 MINOR CORRECTIONS OF THE TAS

### Definition of “user”

- 10.1 The term “user” is defined in a manner which restricts its meaning to *intended* users. Although the definition works, in the sense that the requirements of the TAS do, indeed, relate to *intended* users, readers of the TAS will not necessarily spot this at the first time of reading or remember it on future occasions when the TAS is read.
- 10.2 The distinction between users and intended users is particularly important in relation to paragraph C.4.4 relating to the requirement for the report writer to correct misunderstandings by *any* user – meaning any *intended* user.
- 10.3 The meaning would be clearer if the TAS referred to “intended user” on each occasion where the word “intended” is significant, with the definition of “user” amended by deleting the word “intended”. [Alternatively, the defined term could be “intended user” and the definition left as it is.]

### Assumptions underlying the TAS

- 10.4 Paragraph A.1.3 says: “This standard makes few assumptions about the way in which reporting takes place”, but the TAS does not disclose what those assumptions are. If the TAS depends on some assumptions about the way in which reporting takes place, report writers (and users) need to be told what those assumptions are, so that they can identify reports which do not fit the assumptions.
- 10.5 But I doubt that the BAS has, in fact, made any such assumptions. I think it is more likely that the BAS means “imposes few requirements”, rather than “makes few assumptions”, and those requirements are, of course, set out in Section C of the exposure draft.
- 10.6 To remove any doubt, I suggest the paragraph be amended in one of the following ways:
- a) change “few assumptions” to “no assumptions”; or
  - b) change “makes few assumptions about ” to “imposes few requirements on”; or
  - c) retain the words “makes few assumptions” and spell out what those assumptions are.

## 11 THE SCOPE OF GENERIC TASs

### Summary

- 11.1 The proposal to extend the scope of Generic TASs to include Reserved Work is incompatible with the terms in which some Reserved Work is specified. The proposal to extend the scope to work which is described as complying with TASs creates a strange anomaly.

### The extension of the scope to include Reserved Work

- 11.2 The definition of Reserved Work includes work reserved to actuaries by contract or other private legal obligation. Since the BAS does not know what might be the content of such private obligations, there is no way for the BAS to know what work might be required to comply and whether compliance is appropriate. One example of Reserved Work for which the TAS R would be inapplicable is *expert determination* in circumstances which call for a report without any reasons included.

### *Expert determination*

- 11.3 Expert determination is a form of dispute resolution. It has a lot in common with arbitration (someone is appointed to resolve the dispute having gathered appropriate information about it) and, to a layman, the two forms of dispute resolution may seem very similar. But, as a matter of law, it is well-established that the two are different. One particular difference is that expert determiners are not required to give reasons unless the terms of their appointment demand it: appointments may specify that the expert shall *not* give reasons. Famously, some determinations are no longer than a single sentence.
- 11.4 To anyone unfamiliar with this form of dispute resolution, the idea that a dispute might be resolved without the parties being told the reasons may seem undesirable. But no disputant is ever forced to accept such a situation: expert determination is always voluntary on the part of those in dispute. There are several reasons why the parties may not want to be told how or why the expert determiner reached their decision. These range from cost savings to a desire for finality. It is extremely difficult to “appeal” an expert’s determination and even more so if the decision has been given without reasons.
- 11.5 It needs to be borne in mind, also, that the decision to resolve a dispute by expert determination may be taken before the expert is appointed, for example when a contract is first drawn up between parties. The contract will specify from the outset that, if a dispute arises, it shall be referred to an expert to determine. By the time an actuary is approached to determine a dispute, the terms of the appointment may already be locked in. If the parties had wanted to lock the expert into a decision compliant with BAS standards, they were free to do that when they set the terms.

### *Other non-statutory cases*

- 11.6 The relationship between expert determination and TAS R is one just one example. There may be other types of work outside the knowledge of the BAS which are incompatible with one or more of the Generic TASs.
- 11.7 I am sure the BAS recognises that it has no authority to interfere in the freedom of parties, who are not themselves actuaries, to enter into an agreement to appoint an actuary to carry out a piece of work or the terms on which they make that appointment.

### *Work reserved by statute*

- 11.8 One option would be to limit the scope of the TAS to work reserved by statute or by regulation, so as to avoid the problems described above. But we have already seen that there are examples of statutory reports for which TAS R is not applicable (see section 8 above).
- 11.9 Since statutes (unlike private contracts) are a matter of public record, it would probably achieve the BAS’s goal more effectively, if the BAS expressly identified the statutorily reserved work which is to be included in the scope of Generic TASs, rather than embracing all such work and trying to create exemptions within the Generic TASs.

### **The extension of scope to work which is described as complying with TASs**

- 11.10 The BAS has proposed that if a person carrying out actuarial work says the TASs have been complied with, the Generic TASs should apply to the work, even if the TASs are not otherwise applicable. This is not appropriate, for the following reasons.
- 11.11 First, if a piece of work complies, voluntarily, with Generic TASs and is described by the person executing the work as compliant, there is little point in the BAS making that statement a trigger for the TASs to be compulsory. The work already complies and nothing is achieved.

11.12 The only possible effect of extending the scope in this way is to make it an offence to say that TAS(s) have been complied with when (either by accident or by design) they haven't. This duplicates the disciplinary system of the Actuarial Profession, is outside the BAS's powers and may cause actuaries and others to believe, wrongly, that misleading statements are not an offence unless they have been expressly banned.

11.13 More specifically:

- a) *Duplication*: The definition of "misconduct" in the Actuarial Profession's disciplinary scheme quite clearly embraces the making of a misleading statement, such as a statement that a piece of work complies with TAS(s) when it doesn't. Moreover, the disciplinary scheme is sufficiently flexible that it can distinguish between a deliberately false statement (ie a lie), which is an ethical issue, and a statement made in error, which is a competence issue.

The BAS's proposal is a much blunter instrument than that, because it relates only to technical compliance, and serves no extra purpose.

- b) *Ultra Vires*: The powers of the BAS are limited by the *Memorandum of Understanding* with the Actuarial Profession. Essentially, the power is limited to making technical standards. Arguably, the BAS also has powers in relation to ethical issues, but this applies at most if the Profession has failed to address the issue in question and that manifestly doesn't apply here.

The proposed increase in scope does not create an additional technical standard, nor does it (despite all appearances) extend the scope of any technical standards. The proposed extension only bites in the event that a false statement is made about a piece of work. The effect of the proposal is not to cause the TAS to be applied – it is too late for that – it merely creates an offence (if one didn't already exist) of having made a false statement. That is not within the BAS's remit.

- c) *Anomaly*: The particular false statement brought into play by this proposal is just one of many false statements that might potentially be made. Consider the following:

- an actuary says that adopting the recommendations in their report will enable the entity to comply with regulations, when in fact the recommendations will not achieve compliance;
- an actuary says they have used a particular valuation method or measure, when in fact the stated method or measure is not the one which was used;
- an actuary says that the result of their calculations is to arrive at a particular amount (£809m, say) when in fact the calculations arrive at a different figure (£908m, perhaps);
- an actuary says a TAS has been complied with when in fact it has not.

Each of the above statements is false. Each has the power to mislead the user of the actuarial information. Each one could be anything from a deliberate lie, to incompetence on the part of the person doing (or reviewing) the work, or just an innocent typing/transcription error. And each has the potential to be disastrous or it may prove to be innocuous.

What is it about the fourth statement that means that it needs the BAS to make a rule declaring it as misconduct when the other three have no express rule to that effect? Creating such a rule through the mechanism of the *Scope & Authority* – or, rather, *appearing* to create such a rule – creates with it the risk that readers of the *Scope & Authority* are misled into thinking the other three statements are not capable of being misconduct, when in fact they are.

## **A RESPONSES TO THE BAS's EIGHT QUESTIONS**

### **1 Proposed additions to the Schedule of the BAS's Scope & Authority**

A.1 I consider the proposed additions to the Schedule of the BAS's *Scope & Authority* to be misconceived. The reasons underlying my conclusion are set out in Section 11 of this submission.

### **2 Proposed commencement date for TAS R**

A.2 I have no comment on this proposal.

### **3 The definitions of "aggregate report" and "component report"**

A.3 The definitions of "aggregate report" and "component report" do not deliver the result that I believe the BAS intends for these two terms and, as a result, the definition of "report" does not work either. The reasons underlying my conclusion are set out in Section 1 of this submission.

A.4 Moreover, having considered the proposed requirements for component reports, I have doubts about whether the term "component report" even needs a definition – see paragraph 7.9 of this submission.

### **4 The likely effects of the introduction of TAS R**

A.5 It is an inevitable corollary of my comments in the body of this submission that the exposure draft, in its current form, will not deliver the goals articulated by the BAS in paragraphs 1.8-1.12 of the Response section of the exposure draft, nor will it have the impact envisaged by the BAS in paragraphs 3.40-3.46.

A.6 Notwithstanding my gloomy assessment of the likely outcome of the current exposure draft, I am largely in support of the goals articulated by the BAS and in broad agreement that the impact of the Reporting TAS ought to be as envisaged by the BAS.

### **5 Whether the long term costs will be justified by the benefits to the users**

A.7 I have no doubt that, if the benefits articulated by the BAS could be achieved, it would more than justify the long term costs. Indeed, I rather suspect that the costs would be only short term costs of adjustment (and perhaps training). Thereafter, the costs should be somewhere between zero and negligible.

A.8 But it is an inevitable corollary of my comments in the body of this submission that the exposure draft, in its current form, will not deliver the benefits articulated by the BAS (or anything close to the articulated benefits). I would have to conclude, therefore, that any costs, whether short term or long term, could not be justified.

### **6 The proposal that TAS R should override GNs in the event of a conflict**

A.9 In light of my comments in the body of this submission, I have not considered this question.

### **7 The proposed additional requirements described in paragraphs 4.8-4.18**

A.10 My comments on each of the additional proposals are as follows:

- *"Application" (oral information)*: This is an essential requirement. As noted by the BAS in paragraph 4.8, it is not, in fact, new.
- *"Relevance" (events after the effective date)*: This is an excellent suggestion.

- “*Comprehensibility*” (*descriptions of terms which are not uniquely defined*): The proposal in C.4.8 is an eminently sensible extension of the corresponding proposal in the first exposure draft – but the examples in C.4.9 confuse the point.

There is a world of difference between terms like “central estimate”, for which there appears to be more than one definition in common actuarial use, and a term such as “prudence” for which there is only one meaning, albeit a meaning which spans a range, not a point. In many circumstances, trying to define “prudence” is likely to be unhelpful and not something which, on a proper reading, is required by C.4.8.

For example, the Pensions Act 2004 requires assumptions to be “prudent”, but does not say *how* prudent or offer any definition of the term. A scheme actuary who expresses the view that a particular assumption meets the statutory requirement for prudence would be most unwise to try to explain what the term means and paragraph C.4.9 is misguided in suggesting that C.4.8 requires the actuary to do so.

- “*Completeness*” (*disclosure of cash flows and project results*): The disclosure of at least some information relating to cash flows continues to be controversial amongst some actuaries. As much as I understand why the proposal generates this concern, I am confident that, in time, those who have not yet been convinced will come to realise that the proposal is sufficiently flexible that compliance will not have any of the adverse consequences which the objectors fear.
- “*Transparency*” (*differences between assumptions*): I don’t understand this proposal. If it is intended to address a situation where a piece of work includes, for example, some assumptions which are prudent and some which are best estimates, that would seem to be covered by the requirement to explain the rationale for each (material) assumption.

## **8 The text of the exposure draft as a means of implementing the policy proposals**

- A.11 It will be plain from my comments in the body of this submission that there are many respects in which I have concluded that the text of the exposure draft does not implement the policy proposals.