



ASSOCIATION OF PENSION LAWYERS

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Date 22 September 2009 Our Ref: HA/IXG/Z9996/00002

Your Ref

Dear Sir

**Association of Pension Lawyers Response to Consultation Paper – Pensions - June 2009**

You invited the Association of Pension Lawyers to comment on the Pensions: Consultation Paper published by the Board for Actuarial Standards in June 2009 on its draft Pensions Technical Actuarial Standard (TAS). The Chairman of the APL has asked the Legislative & Parliamentary Sub-Committee of the Association of Pension Lawyers to respond on the Pensions Consultation Paper on behalf of the APL.

The APL is an association of more than 1000 lawyers who practise pensions law in the UK, and our members include, most, if not all, of the legal practitioners in the field.

We work closely alongside actuaries and actuarial firms advising both employers and trustees of occupational pension schemes.

**1. Approach to Responding to Consultation Paper**

In responding we have focussed on three main areas;

1. as disinterested observers, whether the overall framework for professional standards proposed is suitable or may create any practical issues for the actuarial profession;
2. whether what is proposed conflicts in any way with pension legislation;
3. whether what is proposed could create practical problems for the relationship between pension lawyers, actuaries and their mutual clients.

We are not qualified to comment on technical actuarial issues such as discount factors. In such matters we would always defer to the actuarial profession.

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The paper is also not intended to constitute legal advice and no responsibility is accepted for any reliance placed on the answers to the questions raised in the papers or the description of the law applicable to actuaries. We assume that the Board for Actuarial Standards will be taking its own legal advice on any legal issues arising out of the adoption of the pensions TAS to the extent it considers appropriate.

Also ultimately it must be for the Board for Actuarial Standards to decide as a matter of policy what work should be within the pensions TAS under the terms of its remit

## **2. Division of Responsibility between the Board for Actuarial Standards and the Professional Oversight Board**

Our understanding from the Board for Actuarial Standards July 2008: Scope & Authority of Technical Standards is that, following the Morris Review of the Actuarial Profession published in March 2005, HM Treasury asked the Financial Reporting Council (FRC) to:

- (1) take on responsibility for setting technical actuarial standards ("TAS"). The FRS created an operating body (the Board for Actuarial Standards) to fulfil this obligation; and
- (2) take on responsibility for oversight of the UK Actuarial Profession. The FRC carries out this responsibility through a separate operating body, the Professional Oversight Board.

Our understanding from the Scope and Authority document is that the various Technical Actuarial Standards are developed in line with the Conceptual Framework for Actuarial Standards published by the Board for Actuarial Standards.

We also understand that the authority of BAS standards derives from the powers of the Institute and Faculty of Actuaries. Specifically the disciplinary schemes of the Actuarial Professional Bodies recognise the authority of BAS standards by providing that a departure from a BAS standard may amount to misconduct, rendering the actuary liable to disciplinary action.

Also the regulatory regimes for pensions and for insurance have recognised certain BAS standards for the purposes of the requirements imposed on the entities they regulate. For example:

- (1) under Regulation 1(2) the Personal Pension Schemes (Disclosure of Information) Regulations 1987 there are references to "relevant guidance" adopted or prepared by the Board for Actuarial Standards i.e. the Technical Memorandum TM1: Statutory Money Purchase Illustrations";
- (2) under Regulation 23(a) of the Occupational Pension Schemes (Contracting-out) Regulations 1996 in determining whether the pensions provided under the scheme are broadly equivalent to or better than those which would be provided under a reference scheme, the actuary must currently follow guidance note GN28 adopted or prepared, and from time to time revised, by the Board for Actuarial Standards;



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- (3) under the Occupational Pension Schemes (Disclosure of Information) Regulations 1996 there are references to "relevant guidance" in various places which are defined as guidance in the document entitled "Technical Memorandum TM1: Statutory Money Purchase Illustrations" that is adopted or prepared, and from time to time revised, by the Board for Actuarial Standards;
- (4) under the Occupational Pension Schemes (Employer Debt) Regulations 2005 certain calculations have to be carried out in accordance with BAS standards;
- (5) under regulation 15 of the Occupational Pension Schemes (Scheme Funding) Regulations 2005 when advising the trustees or managers of a scheme on any of the matters specified in section 230(1) of the 2004 Act, the actuary is required to have regard to the guidance note "Occupational Pension Schemes -scheme funding matters on which advice of actuary must be obtained" (GN49) adopted or prepared, and from time to time revised, by the Board for Actuarial Standards;
- (6) under Regulation 5(2) of the Occupational Pension Schemes (Modification of Schemes) Regulations 2006 the actuary is required to ensure that the calculation of the actuarial value of an affected member's subsisting rights is made in accordance with any guidance that is adopted or prepared, and from time to time revised, by the Board for Actuarial Standards which is current on the date that the actuarial equivalence statement is obtained by the trustees.

In certain other sets of regulations there are also references to specific actuarial Guidance Notes. Also in various other regulations there (e.g. those relating to transfers) there used to be references to guidance issued by the BAS which have now been replaced.

A new Actuaries' Code has also recently been adopted to replace the existing Professional Conduct Standards applicable to members of the Institute and Faculty of Actuaries.

Given the split between responsibility for technical standards and ethical standards under the current system for regulation of the Actuarial Profession, the Actuaries' Code needs to mesh properly with any TAS issued by the Board for Actuarial Standards and address any issues which are outside the Board for Actuarial Standards' remit. If it is intended to lay down a higher standard of care in the pensions TAS for certain actuarial work, consideration needs to be given as to how this compares with the basic standard of care laid down for actuaries in the Actuaries' Code

We note that the Actuaries' Code operates by laying down certain high level principles for the Regulation of Actuaries and does not lay down detailed guidance about how actuaries are to operate in any given situation.

We note, however, that it does lay down a minimum standard of care for the profession. Principle 2 provides that



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- “2. **Competence and Care:** *Members will perform their professional duties competently and with care.*
- 2.1 *Members will consider who their advice and/or services are being provided to (their clients). In many cases it may be their employer.*
- 2.2 *Members will not act unless:*
- a) *they have an appropriate level of relevant knowledge and skill;*
  - b) *they are acting on the advice of an individual who has the appropriate level of relevant knowledge and skill and all interested parties are aware that this is the case; or*
  - c) *they are acting under the direct supervision of another member who is taking professional responsibility for their work.”*

In considering whether a higher standard of care is appropriate for certain work covered by the pensions TAS this must be the baseline. The view of the APL L&P Committee is that actuaries should not be performing any task (actuarial or non-actuarial such as giving investment advice or performing administration functions) unless the relevant person has the appropriate experience to perform this task. In this connection we would note that actuaries do perform many tasks which are not strictly actuarial in nature (including on occasions giving investment advice). If any task is performed by an actuary to a standard below that should be expected of a competent professional we would observe that this could bring the profession into disrepute.

We would observe as a preliminary issue that there is nothing in the Actuaries' Code which focuses on the fact that in certain circumstances the actuary will often be performing an expert role making expert determinations. We consider that it is important that either the Actuaries Code or the pension TAS addresses this issue.

This is not in our view the same as the distinction between Reserved and Non Reserved work. Often when performing Reserved Work the actuary will be performing an expert role. However, there is also a significant amount of work which falls within the proposed classification of Reserved Work which is effectively advisory in nature (see below)

### 3. Reliability Objective

We note that much of what is proposed in the Pensions Consultation Paper is designed to give effect to and flesh out the detail of the Reliability Objective set out in the Conceptual Framework for Technical Actuarial Standards issued by the Board for Actuarial Standards in July 2008. This is as follows:

*““Reliability Objective” means the objective that the users for whom a piece of actuarial information was created should be able to place a high degree of reliance on the information’s relevance, transparency of assumptions, completeness and comprehensibility, including the communication of any uncertainty inherent in the information.”*



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We would observe that on actuarial issues no one, apart from the profession itself under the oversight of the Board for Actuarial Standards, is really qualified to judge and question the appropriateness of the actuarial assumptions and methods adopted. Trustee and employer clients place significant reliance on advice from their actuaries. It is therefore important that they can rely on and understand this advice.

We note that in the Pensions Consultation Paper it is stated that

*"The primary purpose of the proposed TAS is to ensure that actuarial information gives the best possible support to those who use the information to make decisions based on it."*

We also note that you state elsewhere in the Pensions Consultation Paper that:

*"The overall purpose of all BAS standards is that the users for whom a piece of actuarial information was created should be able to place a high degree of reliance on the information's relevance, transparency of assumptions, completeness and comprehensibility, including the communication of any uncertainty inherent in the information. This is the BAS's Reliability Objective as set out in the Scope and Authority."*

*"We believe that the purpose of the pensions TAS should be to assist the achievement of the Reliability Objective by ensuring that in the performance of work within its scope:*

- (a) Trustees, other members of pension scheme governing bodies, sponsors and other users of actuarial information are provided with sufficient information, including information on risk and uncertainty, to enable them to make decisions which relate to the financing of the pension scheme or affect the benefits payable to members of the pension scheme; and*
- (b) Calculations which result in payments to or from pension schemes are accurate and carried out using methods that are fit for purpose.*

The APL fully supports the proposed purpose of the Pensions TAS. Given the difficulty non actuaries have in assessing actuarial advice it is very important that trustees and employers and other users of actuarial information are provided with sufficient information, including information on risk and uncertainty to enable them to make decisions which relate to the financing of the pension scheme. The approach is also consistent with the limited case law there is about the duties of actuaries when they are performing an advisory role (see below).

It needs to be recognised (as is touched upon in paragraph 10 of the Scope and Authority of Technical Standards), however, that the effect of imposing the Reliability Objective as a matter of professional conduct could impact on the standard of care expected of actuaries when performing their functions in both contract and negligence. In practice is likely to raise or set the standard by which actuaries may be judged in negligence and breach of contract actions.

In relation to claims for negligence an actuary is expected to exercise the standard of care and skill that a reasonably competent member of the profession professing to have the standard of care and skill he held himself out as having and exercised acting with ordinary care. The actuary will be judged



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by what is acceptable practice at the time (this principle was applied to actuaries in *NRG v Bacon & Woodrow* [2000] 08 PLBR (180). If the matter reaches court expert evidence can be called on what is acceptable actuarial practice at the time. Just because another actuary would have proposed a different set of assumptions does not make an actuary negligent. The traditional approach taken by the courts was that if the practice adopted was one that a responsible body of the actuarial profession would have followed he is not negligent (*Bolam v Friern Hospital Management Committee* [1957] 2 All ER 118).

The professional conduct requirements in the pensions TAS will be part of the requirements that **all** actuaries are required to comply with and will shape actuarial practice. Accordingly the pensions TAS may well raise and set the standard of care owed by the profession to their clients in relation to work subject to the pensions TAS.

#### **4 Scope of pensions TAS**

A key question you have asked in your consultation paper is what sort of work should be covered by the pensions TAS. As you recognise in your consultation paper it would be possible for this standard:

- (1) to apply only to "Reserved Work";
- (2) to all work of an actuarial nature whether "Reserved" or "Non-Reserved Work" but not non actuarial work carried out by actuaries (broadly this is the position you appear to be leaning towards in your consultation paper);
- (3) to all work carried out by actuaries including non actuarial work (actuaries often carry out significant work of a non actuarial nature in pensions).

The view of the APL L&P committee was that, as long as there is a minimum standard set down in the Actuaries Code in relation to all work carried out by actuaries, whether actuarial or non actuarial in nature, it is a policy decision as to the scope of the remaining work covered by the pensions TAS. On the one hand there are legitimate policy reasons for deciding that the higher standard of care laid down in the pensions TAS should only apply to work reserved by statute or the trust deed governing the pension scheme to be carried out by actuaries.

On the other hand there is a policy argument that the higher standard should apply to all work of an actuarial nature whether or not it falls with the definition of Reserved Work if the purpose of the pensions TAS is to ensure that there is general confidence in all work carried out by actuaries.

In reaching a decision on the scope of the work to be covered by the pensions TAS consideration does need to be given to extra cost this approach may impose on clients and whether it is always going to be appropriate for work to be carried out to the high level of accuracy required to comply with the Reliability Objective. For example in corporate transactions actuaries are often asked to express a view on the size of a deficit as part of a due diligence exercise on very limited information. If the Reliability Objective prevented the actuary advising the Buyer in this situation this would be unfortunate. Actuaries on occasion do need to be able to provide "back of the envelope" advice.



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Another common situation where there are often problems in practice is where an actuary is asked to certify a section 75 debt triggered by an employment cessation event where there is incomplete information available to give an accurate certification due to lack of information. If an actuary will not certify the debt (even if it is a certification of not more than £x) on the basis that such a certification is only possible under the Reliability Objective if all relevant information is available, this will not assist the operation of pension schemes in the UK. In other words care needs to be taken to ensure that a lack of flexibility in applying the Reliability Objective does not prevent practical solutions where there is no other way of resolving an issue. The experience of APL L&P Committee is that members of the actuarial profession have in the past been very reluctant to depart from the strict wording of a Guidance Note even when there are valid arguments for doing so.

It also needs to be recognised that pension schemes vary in size. If on policy grounds the same high standards are required for all actuarial valuation or certification work for all schemes the smaller schemes (which are less able to afford the cost involved) will have to pay to ensure that the actuary performs to this high standard. There may well be good policy reasons why there should be no distinction in the quality of work when performing a statutory valuation or certification role. However, it needs to be recognised that this may have cost implications for the pension industry.

A possible intermediate position may be to have the pensions TAS applying to all work of an actuarial nature but to give actuaries greater flexibility in departing from the standard where it is appropriate to do so in relation to non Reserved Work where a more limited scope of work is agreed with the client.

### **5 Different Roles of Actuaries in different situations**

One issue the APL L&P Committee would recommend that the Actuarial Standards Board gives some further consideration. Is to whether the approach it takes in the draft Pensions TAS is going to be appropriate, without some modification, to situations where an actuary performs a non advisory role. In particular there does not appear to be any recognition in the Actuaries Code or the pensions TAS at present that actuaries perform a number of roles.

It functions an actuary performs is going to differ depending on the role the actuary is required to perform by statute or the trust documentation or by contract. It may be useful to distinguish between the role of the actuary:

- (1) as expert- making an expert determination for the purpose of legislation or under the trust deed or rules – where the actuary him or herself makes the decision;
- (2) as advisor to either or both of the trustees and employer where the trustee and/or the employer is making a decision on the advice or after consulting the actuary; and
- (3) actuary as negotiator acting for either the trustees or employer;
- (4) as advisor in non actuarial matters e.g. investment and administrative matters.

In relation to the first situation, it is the actuary himself making the decision within the constraints of the relevant legislation (e.g. if there is a prudential requirement or the calculation must be carried out on a



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best estimate basis). Often, but not always, in the first situation the actuary will be performing Reserved Work. In the second situation and third situation some other person is making the decision and the actuary is acting as adviser to that person.

The Reliability Objective is most relevant to the second of these situations where some other person is making the decision.

**Expert Determination Roles**

Examples of situations of where an actuary might perform an expert determination role might include:

- (a) **LGPS Regular Funding Valuations** - under the Local Government Pension Scheme where the actuary is required to determine at each regular valuation the regular ongoing contribution rate necessary to fund the benefits and any adjustments to that rate for an individual employer. Unlike the position under the statutory funding requirements of the Pensions Act 2004, there is no requirement that the assumptions and methods used for funding the LGPS should be calculated on a "prudent basis" like the assumptions in a private sector occupational pension scheme. Accordingly the funding assumptions used are often significantly weaker than those used in private sector schemes. The actuary in this situation has a very wide discretion;
- (b) **LGPS Rates and Adjustment Certificates** - where the LGPS actuary has to determine any capital contribution required under the rates and adjustment certificate when an admission body ceases to participate in the LGPS (this has implications for the remaining employers and the admission body that ceases to participate);
- (c) **Statutory Funding Valuations where Actuary determines** – in cases where the trust deed and rules of a private sector occupational pension scheme provide that the actuary alone determines the funding basis and the level of contributions the normal requirements of the statutory funding regime under the Pensions Act 2004 are modified. The employer and trustees now have to agree the funding basis and level of contributions. However, the actuary's certificate must state that the rates shown in any such rates forming part of the schedule of contributions are not lower than the rates he would have provided for if he, rather than the trustees or managers of the scheme, had the responsibility of preparing or revising the schedule, the statement of funding principles and any recovery plan (paragraph 9(5) of Schedule 2 to the Occupational Pension Schemes (Scheme Funding) Regulations 2005);
- (d) **Actuary performs other functions under the trust deed** – there are many other schemes where the actuary is required to perform a specific function or make a decision itself under the trust deed and rules or under the relevant legislation e.g. certifying amendments as reasonable or fair. This is effectively an expert decision making role rather than an advisory role where the trustees and/or employer make a decision on the advice of the actuary;
- (e) **Independent actuary making default determination in sale or acquisition** – many sale and purchase agreements provide for bulk transfers or a funding deficit to be calculated by the



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Seller's actuary and agreed by the Buyer's Actuary but in default of agreement to be determined by an independent actuary acting as expert;

- (f) **Certifications required by statute** – in many situations actuaries are required to give certifications for example that the certificate required under section 226 of the Pensions Act 2004 that:
- a. the schedule of contributions is consistent with the statement of funding principles, and
  - b. the rates shown in the schedule are such that-
    - i. where the statutory funding objective was not met on the effective date of the last actuarial valuation, the statutory funding objective can be expected to be met by the end of the period specified in the recovery plan, or
    - ii. where the statutory funding objective was met on the effective date of the last actuarial valuation, the statutory funding objective can be expected to continue to be met for the period for which the schedule is to be in force.

The role of the actuary in giving the certificate differs from the role of actuary in giving advice to the trustees on the statutory funding requirements. There are likely to be a wide range of assumptions that the actuary could advise the trustees could meet the statutory funding requirements which could still be certified

- (g) actuaries are also sometimes asked to give expert evidence to the Court in relation to negligence cases against other actuaries; and the calculation of loss in employment disputes. The actuary as expert in this situation owes specific duties to the Court not to the party instructing him. There used to be a GN (GN24) which dealt with this situation. We note, however, that this has now been replaced by an information and assistance note on the Actuary as Expert Witness.

***Actuary advisory roles***

Examples of advisory roles include

- (a) **Pensions Act 2004 Advisory Obligations** - under the Pensions Act 2004 the trustees or managers must obtain the advice of the actuary before doing any of the following-
- a. making any decision as to the methods and assumptions to be used in calculating the scheme's technical provisions (see section 222(4));
  - b. preparing or revising the statement of funding principles (see section 223);
  - c. preparing or revising a recovery plan (see section 226);
  - d. preparing or revising the schedule of contributions (see section 227);



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- e. modifying the scheme as regards the future accrual of benefits under section 229(2).
- (b) Many trust deeds will provide that amount of any bulk transfer or actuarial factors and many other matters should be determined by the trustees and/or employer on the advice of or after consulting the actuary;
- (c) Where employers instruct their own actuaries to give a second opinion on the approach taken by the scheme actuary in relation to setting the technical provisions. This type of work blurs into a negotiation role (see below). We would note that in our experience when actuaries are instructed on negotiations on scheme funding they take a negotiating stance on behalf of their respective clients.

***Negotiation Roles in relation to actuarial matters***

Negotiation roles include;

- (a) Advising Sellers and Buyers in relation to sales and acquisitions of companies or on bulk transfers following a sale;
- (b) Advising trustees and employers on actuarial issues in connection with negotiations on the amount of any payment necessary to address a detriment on a Type A event. Usually forensic accountants and lawyers will also be instructed;
- (c) Advising trustees in negotiations about the level of prudence and/or lengths of recovery plans where the employer instructs his own actuary.

***Non Actuarial Work***

In the experience of the APL actuarial advice or advice from the firm where the actuary works is often sought on a wide range of matters relating to occupational pension schemes including:

- (a) Investment advice;
- (b) The preparation of explanatory literature relating to the scheme;
- (c) Administrative issues.

***Cases on the duty of the Actuary***

There is limited case law on the duties of the Actuary. However, what case law there is, does indicate that the actuary's duties differ depending on the role(s) he is asked to perform. We have included some details of the relevant case law in the Appendix to this letter by way of background information.

The following broad principles may (in the view of the author) be extracted from existing case law:

- (1) An actuary's duty under an occupational pension scheme will depend on the particular functions the actuary is required to perform under the trust deed and rules as modified or



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constrained by any relevant statutory provisions. These duties may constrain the actuarial valuation methods or approach the actuary can adopt;

- (2) If there is doubt about the meaning of the rules a Court would expect legal advice to be taken;
- (3) To the extent that the trust deed and rules places obligations on the actuary that are not precisely governed by the rules or statute, for example where the actuary has to determine, certify or approve something under the rules, the actuary is under a duty to attempt to achieve the greatest practicable degree of fairness between the various persons interested;
- (4) If the trustees have to decide something "on the advice of the actuary" or "after consulting the actuary" the actuary's duty is arguably to give the trustees sufficient information to enable the trustees to make an informed decision on the issue;
- (5) While there is no direct case law on point, arguably a similar approach to (4) should be taken where an employer is required to make a decision in relation to an occupational pension scheme on the advice of the actuary.

The Reliability Objective has most relevance to the role of actuary as adviser rather than expert.

We would note that, in our experience, even when an actuary is performing an expert role, the expert determination the actuary arrives at is often influenced by the views of the trustees if the trustees are client. We would query whether the actuary should be influenced at all in this situation by the client's wishes given the case law on the actuaries' duties. The actuary's duty is to act as expert not adviser.

This issue is not currently addressed explicitly in the Actuaries' Code. We would recommend that it is addressed either in the Code or the pensions TAS

**Duties of Actuaries in law can be affected by who they are acting for and the role they are performing**

The role of the actuary and duties to third parties under contract or negligence will also be influenced by who they are acting for and whether a third party is independently advised. What is unusual is that actuaries can owe duties to a wide range of third parties. For example:

- (1) actuaries generally owe concurrent duties in contract and tort (e.g. negligence) to the trustees or the sponsoring employer instructing them in relation to the performance of their work. In other words they can be sued by the person instructing them both for breach of contract or the tort of negligence for the same mistake. Actuaries can also owe fiduciary duties to a client and can be liable for breach of fiduciary duties they owe to a client e.g. failing to recognise a conflict;
- (2) actuaries may also owe duties of care in negligence to the sponsoring employer in relation to funding/investment advice given to the trustees as it is reasonably foreseeable that the employer may rely on this advice. However, if there is a potential conflict between the employer's interest and the trustees' interests and the employer instructs its own actuary this



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should normally be sufficient to negate any duty of care. The duty can also be affected by the contractual terms of engagement and the basis it is agreed that any advice or information to the trustees is made available to the employer;

- (3) actuaries may owe duties of care to members in negligence in relation to funding advice or calculations of transfer values or benefit calculations they carry out for the trustees;
- (4) actuaries could be liable for breach of statutory duty in addition to any claim in negligence.

Again it may be useful if there could be some recognition of the different duties owed to different persons in the pensions TAS as it is only obliquely addressed in the current Actuaries' Code. All the Code says is that "*Members will consider who their advice and/or services are provided to (their clients)*" and also that "*Members will not allow bias, conflict of interest, or the undue influence of others to override their professional judgment*".

We are not sure to what extent there will still be direct reference to compliance with the pensions TAS in pensions legislation once the new pensions TAS is adopted. This is an issue which needs to be considered when looking at the replacement of any of the existing GNs which are referred to in the legislation with the new pensions TAS.

Yours sincerely

Ian Greenstreet

For and on behalf of the APL Legislative and Parliamentary Committee



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## APPENDIX 1

(The summary of the relevant case law relevant to actuaries has been prepared by the author of this letter. The analysis of the cases is not intended to be a definitive summary of the law and other members of the APL may have differing views on these cases. Nevertheless the author hopes that the summary may be of assistance in relation to the consultation paper)

### 1. Actuary's Primary Duty to Follow the Trust Deed and Rules

The actuary's primary duty (like the trustees) is to follow the trust deed and rules. Any actuarial method or approach needs to be consistent with the wording of the trust deed and rules governing the scheme.

There have been a couple of cases where it has been held that the use of the "aggregate method" (which values the liabilities of the scheme for past and future service of members against the assets actually held, together with the discounted value of future contributions) was not compatible with a rule which required the actuary to certify the surplus or deficit following an actuarial valuation (*Hillsdown plc v Pensions Ombudsman and others* [1997] 1 All ER 862 at pages 887-889 and also *Stevens & others v Bell & others* [2001] PLR 99). The actuary could not use the "aggregate method" of valuation under the relevant rule as effectively it would give the employer the benefit of a past service surplus against future service obligations.

The author notes that the Actuaries' Code already recognises that it may be appropriate for clients to take legal advice.

### 2. Need to Take Legal Advice if There is Doubt about Meaning of the Rules

Actuaries also need to be careful when forming a view on what the rules mean in given circumstances without the benefit of legal advice. The Courts confirmed in the case of *Mettoy Pension Ltd v Evans* [1991] 2 All ER at 541 that it was manifestly right that:

*"...the rights of beneficiaries under a pension scheme depended first and foremost on the correct construction of the scheme documents which was a legal matter and not one on which they (the actuaries) were competent to testify..."*

It must be prudent to obtain legal advice where there is uncertainty about the meaning of a rule.

Again the author notes that the Actuaries' Code already recognises that it may be appropriate for clients to take legal advice.

### 3. Actuary's Duties When Performing a Valuation, Certification or Arbitration Role

The leading case on actuaries' duties is *Re George Newnes Group Pension Fund* (1969) *Journal of Institute of Actuaries*, Vol 98, Pt 3, Page 251. This case concerned the take-over by IPC of the George Newnes group of companies and the subsequent wind-up of the pension schemes. Employees were given the option of transferring their benefits to a replacement IPC scheme or having their benefits secured by annuities. Under the wind-up rule the terms and conditions of any transfer had to be approved by the actuary provided that the actuary should not approve terms and conditions which together or separately in his opinion:

- (a) Directly or substantially prejudiced the rights or interests of any member of the scheme at the dissolution date; or



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- (b) Fail to make adequate provision to secure the future payment to such persons as were at the dissolution date in receipt of pensions under the scheme, of the full amount of such pensions.

The IPC actuary unsuccessfully argued that the valuation method and assumptions used by the George Newnes actuary was not appropriate as it did not make allowance for future service when calculating wind-up benefits.

In this case the judge said:

*"The function of an actuary, in advising how a pension scheme of this kind should be dealt with on the determination of the Scheme, is to achieve the greatest practicable degree of fairness between the various persons interested under the scheme consistent with the rules governing the scheme. He cannot ignore or contravene those rules, and in the pursuit of fairness he may also have to pay regard to the spirit of those rules in respects which are not controlled by their express terms or necessary implication, but consistently with the rules, he must do his best to achieve as fair a distribution of benefits as the size of the available fund, the character of the Scheme and the circumstances of the contributors make possible".*

The judge also recognised that there was considerable scope for differences of opinion and judgement amongst actuaries and one actuary may very possibly reach a conclusion that differed from the conclusion of another actuary on the same facts. The court:

*"...should be very slow to criticize or seek to control the exercise of any discretion or judgement reposed in or required of any expert of this kind in exercise of a function of this character."*

It was also said that, where a discretion of this type is reposed in an expert, the burden of proof rests on the party who criticises the decision of the expert to show that the expert has acted fraudulently or for some improper motive or has been guilty of a mistake of a substantial character or has materially misdirected himself.

In a later case the Court was asked to consider whether a "past service reserve" method was an appropriate way of valuing the amount of the fund that should be transferred on a partial wind-up to a replacement scheme (Imperial Foods Ltd's Pension Scheme ([1986] 2 All ER 802 at 812). The purchaser had argued that a share of fund should have been transferred. Mr Walton J said:

*"I accept entirely the principle enunciated by Buckley J in Re George Newnes Group Pension Fund (1969) 98 J Inst of Actuaries 251 that the function of an actuary in any situation which is not governed precisely by the provisions of the trust deed is to achieve the greatest possible degree of fairness between the various persons interested under the scheme".*



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In that case the judge was not willing to make any finding that a "past service reserve" method was a more appropriate method of determining the share of the fund to be transferred on a partial wind-up compared with another method but merely that the decision to use a past service reserve method was such that a competent actuary fully acquainted with the facts could have adopted that method. Accordingly the court would not interfere.

The courts have taken a similar approach in later cases and are generally very reluctant to interfere with an exercise of actuarial judgement or an actuarial certification unless the method adopted by the actuary is not consistent with the wording of the rules.

Other cases show that the courts are generally supportive of actuaries performing the role of arbiter in very difficult situations. In the case of *Stevens v Bell* [2001] PLR 99, under clause 11(b) of the scheme documentation the managing trustee had to come up with a scheme for dealing with the "disposal surplus" but any such scheme had to be agreed by the employer or, in default of agreement, referred to a Fellow of the Institute of Actuaries and then come into effect subject to such amendments as the actuary shall direct. It was said that;

*"Moreover, I do not accept that an actuary experienced in pension scheme matters would not be a suitable arbiter. It may be that another professional might have been used, but an actuary (who could be the Scheme Actuary) could, in my judgement be expected to be capable of deciding fairly between rival contentions, even if the scope of the matters the subject of the disagreement is wide."*

In the case of *National Grid Co plc v Laws* [1997] OPLR 207, where again the actuary had to certify the arrangements for disposing of surplus, it was said that there was much to commend the interpretation that the actuary's certificate was a warrant of fairness not merely a certificate of technical correctness.

#### **4. Actuary's Certifications and Valuations are Difficult to Attack**

The cases also demonstrate that the courts are very reluctant to overturn an actuarial certificate or valuation made under the rules of an occupational pension scheme. The Courts will rarely look behind an actuarial certificate.

#### **5. Actuaries Duties Where Role is to Advise Trustees**

The cases discussed in the previous sections concern situations where the actuary has to perform an expert valuation or certification role or approve something under the trust deed and rules.

The actuary's duties are arguably different in cases where it is the trustees acting on, or having regard to, the advice of the actuary exercise a power or discretion under the trust deed. In these cases it is the trustees, not the actuary, who are primarily responsible for ensuring that proper consideration is given to the interests of the different categories of members affected by the



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exercise of the power or discretion. The trustees will owe fiduciary duties to the members in exercising these powers.

In one case there was an issue in the first instance court hearing about whether a decision to transfer part of a fund on a disposal had been made under the correct rule (the partial wind-up rule or the bulk transfer rule) (*Stannard v Fisons Pension Trust Limited* [1992] IRLR 28). Under the partial wind-up rule the trustees had to decide broadly what part of the assets of the fund had to be appropriated for the benefit of the employees after consulting the actuary. Under the bulk transfer rule broadly, the trustees had to transfer monies or other assets representing the members' interests in the Fund, as advised by the actuary.

On appeal the Court decided that it did not matter which rule had been used as the effect of the two rules was the same. The trustees had discretion under both and should be seeking to act fairly between the transferring and non-transferring members. Under the second rule the trustees were not merely rubber-stamping the advice of the actuary – they still had discretion, even though it said that the trustees had to transfer monies representing the interests of the members "as advised by the actuary". The judge said:

*"To give properly informed consideration to the discretion they [ i.e. the trustees] had to exercise, they needed also to know the relevance of the value of the fund to the problem at hand in relation to actuarial principles and the implications of their decision on future contributions. That information the actuaries could have given them (and in my view should have given them) since it was the actuaries' duty to put the trustees in a position, so far as the actuaries could, to make a properly informed decision".*

So the role of actuaries in a situation where it is the trustees, not the actuary, that is making the decision, seems to be to *"...put the trustees in a position, so far as the actuaries could, to make a properly informed decision..."*.

It is therefore arguable that in this type of situation an actuary should not be giving his client a single "right" answer. If, as invariably is the case, there are a range of reasonable actuarial approaches that could be adopted while acting consistently with the rules the actuary should arguably be setting these out (albeit with appropriate recommendations) so that the trustees can give properly informed consideration to the matter.

The author would note that this approach is reflected in the Reliability Objective proposed by the Board for Actuarial Standards.

**6. Actuary's Duty When Advising the Principal Employer how to Exercise a Power under the Rules**

The author of this letter has not been able to locate any cases which have considered the duties of an actuary advising a principal employer where the principal employer has power to determine the level of contributions or the size of a bulk transfer on the advice of the actuary. Generally it is submitted that in these cases the principle employer will not hold the power in a fiduciary capacity but only subject to the implied duty of good faith not to break down the relationship of trust and confidence that exists between the employer and the pension scheme



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members (*Imperial Group Pension Trust v Imperial Tobacco* [1991] 2 All ER 597). This is not the same thing as acting reasonably and the principal employer will be able to have regard to its own financial interests in so far as this is consistent with the implied duty of good faith.

In these circumstances, by analogy to the position in relation to trustees, the duty of the actuary under the rules should be to put the principal employer in a position where it can make an informed decision.



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## APPENDIX 2

### Response to Questions Asked in Board for Actuarial Standards Pension Consultation Paper

1. **Question 1** – Will the proposed purpose of the pensions TAS that is set out in paragraph 2.3 help to ensure that users of actuarial information can place a high degree of reliance on its relevance, transparency of assumptions, completeness and comprehensibility?

**APL Response - Yes** - the stated purpose of the pensions TAS is consistent with, and expands on, the Reliability Objective as set out in the Scope and Authority.

As mentioned in the covering letter to this Appendix, however, the APL would note that the role of the actuary will differ depending on the nature of the task the actuary is obliged to perform e.g. an expert determination role; an advisory role or a negotiation role. The Reliability Objective appears to be primarily focussed on the role of the actuary as adviser where some other person has to make a decision on the basis of the advice of the actuary.

Where an actuary is performing an expert determination role it is still important that calculations are accurate and are carried out using methods that are fit for purpose and assumptions are transparent, complete and comprehensible, including any communication of uncertainty but it will be the actuary making the decision.

In the experience of the APL there can sometimes be confusion within the actuarial profession about precisely which role the actuary is performing. When performing the role of expert the actuary is sometimes influenced by the wishes of its client where there are a range of possible approaches that could be taken. On the basis of current case law, while the actuary can listen to the various stakeholders, the actuary should be seeking to achieve the greatest degree of fairness between the various stakeholders when making such a determination.

2. **Question 2** – Do respondents agree that all Reserved Work concerning occupational pension schemes should be within the scope of the pensions TAS? (paragraphs 4.2 to 4.7)

**APL Response – Yes we agree** – The APL L&P Committee agree that there are good policy arguments for applying the pensions TAS to Reserved Work. Given the reliance placed on it, and the difficulty of non actuaries in understanding actuarial issues employers, trustees and beneficiaries should have the confidence that it will be carried out to a high standard.

As mentioned in the covering letter good arguments can also be put forward why the pension TAS should apply to all actuarial work (both Reserved and non Reserved work). It is arguable that actuarial work which is vital to the effective operation of UK Business (e.g. actuarial advice in relation to corporate transactions) should not be subject to a lower standard of care than Reserved Work. The counter-argument against extending the TAS to non Reserved Work is that it may result in work being carried out to a higher standard (at a higher cost) than would otherwise be appropriate.



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It is important that the pensions TAS should not prevent actuaries giving views based on limited information or clients instructing actuaries to give them high level advice to establish whether an issue is likely to be material in relation to a transaction. For example it may not matter whether the funding deficit is £1 million or £5 million in an acquisition where the purchase price is £1 billion. On occasions clients may wish to limit the scope of the actuary's work although clients would expect the work within the limited scope to be performed to a high standard.

There are also going to be situations where the relevant information needed to perform work to the high standard of accuracy required under the new Reliability Objective may not be available.

It also needs to be appreciated that not all pension schemes are multi-billion schemes and applying the pensions TAS to non Reserved Work may impose additional costs on employers and trustees where from a policy view it may not be appropriate to do so.

**Question 3** – do respondents agree with our intention that pensions TAS should apply to work in connection with occupational pension schemes which is almost always carried out by an actuary and which is used to make important financial decisions or which might affect the level of benefits payable to the members (paragraph 4.11)

**APL Response –See above and covering letter for a discussion of these issues.**

3. **Question 4** – Should the pensions TAS cover the non-Reserved Work listed in paragraph 4.26?
- 4.26(a) updates to scheme funding information used to make or support financial decisions by governing bodies on contribution requirements, investment strategy and rule changes – **APL Response –See above;**
  - 4.26(b) actuarial information provided to employers or scheme sponsors on any matter related to Scheme Funding where there is a statutory or contractual requirement for the governing body to reach agreement with or consult on the matter with the employer or scheme sponsor or vice versa – **APL Response See above;**
  - 4.26(c) actuarial information provided to a governing body relating to amendments to scheme rules which might affect members' benefits or their security – **APL Response –See above;**
  - 4.26(d) actuarial information provided to a governing body relating to financial matters in connection with a bulk transfer of assets and liabilities from one pension scheme to another – **APL Response – Yes but see above;**
  - 4.26(e) if not covered by a TAS covering business rearrangements, actuarial information provided to governing bodies for pension schemes in wind up, including advice in connection with a transfer of liabilities on buy-out – **APL Response See above;**
  - 4.27(f) actuarial information for a governing body relating to individual calculations and factors which is not Reserved Work – **APL Response See above;**



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These are all areas where reliance is placed on the actuary. By making these areas subject to the pensions TAS it will give the users of the information confidence that they can rely on the actuarial advice. However, it may be desirable to allow the Reliability Objective to be relaxed in relation to non Reserved Work where the clients want to instruct the actuary on this basis.

We would note that in all of the above examples it is assumed that a third party will be relying on the information rather than the actuary making the decision itself.

4. **Question 5** – Do respondents agree that the areas of work described in paragraphs 4.29 to 4.33 should not be within the scope of the pensions TAS?

4.30 and 4.31 Accounting for pension costs – FRS17 and IAS19 – **APL Response** - The APL's view is that accounting for pension cost should be covered by a TAS given the reliance placed by companies and investors on the accounting information. We note that it is proposed not to cover this information in the pensions TAS but in the proposed specific TAS on financial reporting. It is for Board for Actuarial Standards to decide which TAS is most appropriate to cover this area.

4.32 and 4.33 Investment – **APL Response** - We agree that it would not be appropriate to include general investment work in the final version of the pensions TAS given that investment advice is not the exclusive preserve of actuaries. However, actuaries have a significant role in asset/liability modelling which is essentially actuarial work.

If the pensions TAS is to apply to all actuarial work whether Reserved or non Reserved it would be consistent with this approach for asset/liability work to be within the scope of the pensions TAS but pure investment work should not be. Actuaries carrying out investment work should, however, only be doing this if they have the relevant expertise.

We agree that it may be appropriate to bring benefit projections into a TAS given the reliance placed on them by beneficiaries.

5. **Question 6** – Should the following areas of actuarial work performed in connection with defined contribution schemes be within the scope of the pensions TAS:

- a) Scheme design (paragraph 4.35 – **APL Response See above comments** ;
- b) Benefit projections (Paragraph 4.36 – **APL Response – See above comments**;
- c) Any other work (Paragraph 4.3&)- **APL Response** – possibly calculation of pension loss in employment cases and funding of unregistered pension schemes to the extent not covered above.

If the overall approach adopted by the Board for Actuarial Standards is that all actuarial work should be within the scope of the pensions TAS (both of a Reserved and a non Reserved nature) it would be consistent with this approach for the above items to be within the scope of the pensions TAS.



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6. **Question 7** – Should work in connection with mergers and acquisitions be within the scope of the Pensions TAS? (paragraphs 4.38 to 4.40)

**APL Response – see earlier comments** - Actuarial input is absolutely key to sellers and buyers in assessing the liabilities that are being transferred in sales and acquisitions and making commercial decisions on price in relation to those liabilities.

Given the increasing danger in transactions being derailed because companies do not understand these issues commonly blowing these issues out of all proportion to the liabilities involved it is really important that the risks are properly explained.

However, as discussed before there needs to be flexibility for actuaries to be instructed to advise on the basis of limited information without breaching the Reliability Objective. Where appropriate, as long as the client understands that a rough and ready calculation is being carried out, actuaries should not be prevented from being instructed on this basis.

7. **Question 8** – Should work for scheme sponsors on inducements to transfer be within the scope of the pensions TAS?

**APL Response See above comments** –Typically in this sort of exercise members will be advised to take independent financial advice on whether to accept the inducement and employers sometimes are willing to pay for this advice.

It is important that if members are induced to transfer there should be no mis-selling. However, unless the actuary is held out as having carried out calculations designed to ensure that members' do not lose out it is not necessarily the actuary's role (if acting for the employer) to ensure that there is no mis-selling. The employer should have flexibility to determine the basis on which the actuary is instructed.

8. **Question 9** – Is there any work for scheme sponsors, other than work on Scheme Funding where agreement is required and inducements to transfer, that should be within the scope of the pensions TAS?

**APL Response – See earlier discussion** There are many occasions where the scheme sponsor will take separate actuarial advice for example in relation to scheme mergers; negotiations about Type A events and scheme apportionments and calculation of section 75 debts.

As discussed there are policy arguments that either:

- (1) the pensions TAS should apply only to Reserved Work (including work reserved to the actuary under the trust deed); or
- (2) the pensions TAS should apply to all work of an actuarial nature and the employer should be able to expect the same standard of advice in relation to actuarial advice as trustees can expect.



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If the second approach is taken consideration should be given to whether employers should have the flexibility to instruct actuaries on the basis that a lower standard of care applies.

9. **Question 10** – is there any work which is not mentioned above that should be within the scope of the pensions TAS?

We would also note that the approach taken in the pensions TAS is to try to set out an exhaustive list of what type of actuarial work is and is not covered by the pensions TAS. This may result in gaps in coverage in the pensions TAS as it will not always be possible to provide an exhaustive classification of all actuarial work.

If the basic distinction adopted for application of the TAS is between Reserved or Non Reserved Work or actuarial and non actuarial work there is an argument for setting out the distinction in general terms with the examples being included as examples.

**Question 11** – Do the respondents have any comments on the proposals concerning data that are presented in section 5, especially those in paragraphs 5.7, 5.10 and 5.12?

- 5.7 The data sought should include information from the scheme sponsor about matters affecting benefits payable to members over which it has influence or control e.g. level of salary increases and numbers of members retiring early –**

**APL Response** - The APL L & P Committee has no issue with this requirement as long as it is only a requirement to seek this information. Employers will not necessarily be willing to disclose information on likely levels of salary increases or early retirement programmes.

- 5.10 Where there is uncertainty about the impact of overriding legislation on the calculation of benefits, the data sought should include any relevant legal opinion**

**APL Response** - We have some concerns about making it a professional practice requirement that legal advice has to be shared as this could result in the loss of legal privilege. Any legal advice will generally have been given to the Trustees and not to the actuary directly. However, as long as the requirement is just to “seek” this information it may not create issues in practice as the information would not have to be provided.

- 5.12 The data sought should include information about any practice of granting discretionary benefits, its history and any policy regarding the exercise of discretion.**

**APL Response** - As long as this requirement is limited to information sought the APL L&P Committee can foresee no major issue with this.

10. **Question 12** – Are there any other data issues which respondents believe should be covered by principles in the pensions TAS?



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**APL Response** - The actuarial profession is best placed to comment on whether there are any other data issues which should be covered by the pensions TAS.

11. **Question 13** – Do respondents have any comments on the proposals concerning assumptions that are presented in section 6 especially those in paragraphs 6.3, 6.8, 6.12, 6.14, 6.16, 6.19, 6.33, 6.35, 6.36, 6.42, 6.46, 6.53, 6.61 and 6.63?

6.3 It has been suggested to us by users in particular that we should set benchmarks for assumptions used for certain tasks such as Scheme Funding. It is argued that this would improve consistency and help the trustees of pension schemes. However, we believe that actuaries and trustees should use their judgment to select assumptions which are appropriate for the particular circumstances. No benchmarks can be universally applicable and we are therefore not inclined to set benchmarks.

**APL Response** – this would be consistent with the Scheme Funding requirements.

6.8 The selection of assumptions should take account of the purpose of the calculations for which they will be used.

**APL Response** – would seem logical.

6.12 The selection of assumptions should take account of the information available at the effective date of the calculations for which they should be used. The selection of assumptions should also take account of any material events which are known to have occurred after the effective date of the calculations.

**APL Response** – Our understanding is that the actuary has discretion at the moment as to how material events that are known to have occurred after the effective date of the calculation are dealt with.

We can see the argument for making the selection of the assumptions take account of any material events which are known to have occurred after the effective date of the calculations. However, we would suggest that consideration is given to the impact this will have on valuation practice, in particular given practicalities of negotiation and timing.

6.14 Recent experience of pension scheme should be analysed and compared with the selected demographic and salary increase assumptions.

**APL Response** – While we can see why this would be helpful to establish whether the assumptions used are borne out by actuarial experience we would be concerned if this imposed a significant cost burden for the smallest schemes and there may be circumstances where sufficient data on the experience of the scheme is not available to perform this comparison. In the Occupational Pension Scheme (Transfer Value) Regulations 1996 a similar issue was addressed as follows in regulation 7B by providing that in determining the demographic assumptions, the trustees must have regard to:



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- (a) the main characteristics of the members of the scheme; or
- (b) where the members of the scheme do not form a large enough group to allow demographic assumptions to be made, the characteristics of a wider population sharing similar characteristics to the members.

6.16 The selection of assumptions should take account of information from the sponsor on matters over which it has influence or control.

**APL Response** Would seem logical.

6.19 No adjustment should be made to any assumption to compensate for a shortcoming in another assumption.

**APL Response** – This is an actuarial issue. However, care should be taken to ensure that whatever position is adopted on this issue it is not inconsistent with The Occupational Pension Schemes (Scheme Funding) Regulations 2005.

Under Regulation 5(4) there are three separate prudential requirements which mirror those in the IORP directive, namely:

- (a) the economic and actuarial assumptions must be chosen **prudently**[our emphasis] , taking into account, if applicable, of an appropriate margin for adverse deviation;
- (b) the rates of interest used to discount future payment of benefits must be chosen **prudently** [our emphasis], taking into account either or both-
  - (i) the yield on assets held by the scheme to fund future benefits and the anticipated future investment returns, and
  - (ii) the market redemption yields on government or other high quality bonds;
- (c) the mortality tables used and the demographic assumptions made must be based on **prudent** [our emphasis] principles, having regard to the main characteristics of the members as a group and expected changes in the risks to the scheme;
- (d) ....."

It is therefore arguable that a separate prudential requirement applies when assessing compliance with each of the above principles and there can be no adjustment in the level of prudence in one principle to compensate for a shortfall in the level of prudence in another but within a particular principle the assumptions used can be looked at together to comply with the level of prudence.

6.33 If a discount rate is related to future returns on scheme assets its selection should take account the trustees' investment strategy and anticipated changes in that strategy.



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**APL Response** – This is an actuarial issue. However, the principle appears sensible and logically consistent.

- 6.35 If the discount is related to future returns on scheme assets its selection should take account of the risk that yields on the investment of future income will be lower than the yields currently available.

**APL Response** – Actuarial issue.

- 6.36 Assumptions about future rates of inflation should take account of financial indicators and publicly available forecasts

**APL Response** – Actuarial issue.

- 6.42 Separate assumptions should be selected for the current rates of mortality and for future changes to mortality rates. Assumptions concerning current rates of mortality should reflect the estimated current mortality rates applicable to the pension scheme in question.

**APL Response** – Actuarial issue but query whether information will be available to meaningfully assess the current mortality rates applicable to smaller schemes with only a handful of members.

- 6.46 Assumptions about the award of discretionary benefits should take account of past experience and information about the sponsor's or trustees' intentions which might affect the practice in the future.

**APL Response**– Actuarial issue but would appear a logical approach to take.

- 6.53 Separate assumptions should be selected for running costs paid by trustees in respect of liabilities relating to accrued benefits and future accruals of benefits.

**APL Response** – Actuarial issue.

- 6.61 The assumptions selected for any calculations relating to the position if a scheme had been discontinued or wound up should be determined taking into account possible annuity rates available from providers, the nature of the pension scheme liabilities and the level of relevant bond yields.

**APL Response** – Actuarial issue. However, we would note that some of the largest schemes may have assets in excess of those that could be secured by insurance companies operating in the annuity market.

We would note that there were real problems requiring employer debt calculations to be carried out by reference to the cost of purchasing annuities on the market in relation to larger schemes. The DWP has now amended The Occupational Pension Schemes (Employer Debt) Regulations 2005 to provide at regulation 5(12) that:



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(12) *The actuary must estimate the cost of purchasing annuities:*

- (a) *on terms the actuary considers consistent with those available market and which he considers would be sufficient to satisfy the scheme's liabilities in respect of pensions and other benefits; or*
- (b) *where the actuary considers it is not practicable to make an estimate in accordance with sub-paragraph (a), in such manner as the actuary considers appropriate in the circumstances of the case.*

We would suggest that consideration is given to taking a similar approach in the pensions TAS or as a minimum whatever is in the pensions TAS should be made expressly subject to any contrary statutory provision.

6.63 The assumptions selected for cash equivalent transfer values should be justifiable in relation to the assumptions used for Scheme Funding.

**APL Response** – Actuarial issue.

12. **Question 14** – Respondents are asked for their views on whether a standard comparator rate for discount rates would assist users' understanding, and if so whether a low risk rate should be used?(paragraphs 6.28 to 6.31)

**APL Response** – Actuarial issue.

13. **Question 15** – Are there any other principles on the selection of assumptions which respondents believe should be in the pensions TAS?

**APL Response** – Actuarial issue.

14. **Question 16** – Do respondents have any comments on the proposals concerning modelling and calculations that are presented in section 7, especially those in paragraphs 7.6 and 7.10?

Paragraph 7.6 The funding method employed in Scheme Funding exercises should be explained to trustees. This explanation should include the way future entrants and future increases to benefits have to be taken into account.

Paragraph 7.10 Instructions to another party for the calculation of benefits or other payments related to individual members should include:

- *Clear descriptions of the circumstances in which the instructions apply;*
- *Sufficient information to enable the calculations to be performed correctly;*
- *Procedures for checking the calculations; and*
- *Comments on when the instructions should be reviewed.*



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**APL Response** – The APL agrees that Trustees need to be in a position where they understand the implications of choosing a particular method. The APL also agrees that instructions to third parties to carry out calculations of benefits and other information should include the information proposed.

15. **Question 17** – Are there any other principles relating to models and calculations which respondents believe should be in the pensions TAS?

**APL Response** – Actuarial issue.

16. **Question 18**–Do respondents have any comments on the proposals concerning reporting that are presented in section 8, especially those in paragraphs 8.4, 8.17, 8.18, 8.35, 8.38, 8.39 and 8.40?

8.4 The reason for any change in the rationale underlying the selection of assumptions between two similar exercises should be explained to the users.

**APL Response** – Should aid understanding and transparency.

8.17 The actuarial information given to trustees in the course of Scheme Funding exercises before they make decisions should include an explanation of how the funding objectives adopted by the trustees have been taken into account. It should also include comments on the following risks:

- The risk that the scheme sponsor may not be able to continue to pay contributions or make good deficits;
- The risk that the investment return on assets will be insufficient to meet the funding objective;
- The risk that fall in asset values will not be matched by similar falls in the value of liabilities, thereby reducing the funding and/or solvency levels of the scheme;
- The risk that unanticipated future changes in mortality will increase the cost of benefits;
- The risk associated with the potential exercise (by members or others) of options against the scheme;
- Any other material risks

**APL Response** – Agree with proposal.

8.18 The treatment of any uncertainty in benefit definitions due to overriding legislation should be explained to trustees in the course of Scheme Funding exercises. The explanation should include an indication of the maximum liability.



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**APL Response** –This is a legal issue on which it may not be appropriate for actuaries to advise. Sometimes there is inherent uncertainty (and difference in legal opinion) as to how benefit definitions are affected by overriding legislation. It would be appropriate in our view for actuaries to advise on the funding implications of various legal interpretations but care should be taken not to provide legal advice on what those interpretations could be (see Appendix 1). Also query whether maximum liability will always be capable of being determined.

- 8.35 It should be assumed that the intended user of the formal report giving the results of the PPF levy calculations is the PPF, and that decisions that will be based on the report will concern the compliance of the calculations with the specified assumptions.

**APL Response** - Inclusion of this principle is likely to ensure that actuaries owe a duty of care to the PPF when preparing a PPF levy calculation. On the basis of existing cases, it is likely that the actuary's duty of care may already extend to the PPF under the general law as it is reasonably foreseeable that the report will be supplied to the PPF for levy calculation purposes and the PPF will rely on the report.

17. **Question 19** – Do respondents agree that in Scheme Funding exercises any prudent estimate of scheme liabilities should be accompanied by a best estimate? (paragraphs 8.10 to 8.15)

**APL Response:** The APL have real concerns with this proposal and its implications for negotiations between scheme sponsors and trustees. The statutory funding requirements broadly require the trustees to adopt prudent assumptions in a number of respects. There is no definition of what is prudent means in the legislation. There is some judicial comment on the meaning of prudence in the context of use of surplus in the Edge case where it was said in the Court of Appeal that:

*"...the task of the trustees is to maintain a balance between assets and liabilities valued on that actuarial basis; so that, so far as the future can be foreseen, they will be in a position to provide pensions and other benefits in accordance with the rules throughout the life of the scheme. That task is to be performed by setting appropriate levels for employers' and members' contributions. If that task could be performed with perfect foresight there would be no surpluses and no deficits. But, because the task has to be performed in the real world, surpluses and deficits are bound to arise from time to time and prudent trustees will aim to ensure that the likelihood of surplus outweighs the risk of deficit. Nevertheless, it is no part of the trustees' function, in a fund of this nature, to set levels for contributions which will generate surpluses beyond those properly required as a reserve against contingencies."*

APL members have been to leading counsel to opine on this issue on behalf of certain of their clients and it is apparent that what is prudent is going to vary in accordance with the circumstances of the scheme and general practice at the time and guidance issued by the Regulator. The APL supports the Board for Actuarial Standards' decision not to attempt to define prudence.



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The APL appreciates the importance of explaining to trustees that there is a range of assumptions that may be prudent. However, it would be very concerned if it was a requirement under the pensions TAS that the actuary had to provide a best estimate of the liabilities of the scheme to illustrate the degree of prudence. In the APL's view, is **not consistent with the legislation** and inappropriate as a requirement. It will almost certainly be used by employers in negotiations with the trustees about the strength of the technical provisions.

If the Trustees argue, on the advice of the actuary, that ZYX assumptions are prudent the employer is likely to point to the difference between the best estimate and the proposed prudent assumptions and argue that the Trustees are acting unreasonably with "excessive prudence".

18. **Question 20** – Do respondents agree with our conclusion that the final Scheme Funding report should include sufficient information for an informed reader to understand the financial position of the Scheme, and that this is best accomplished by defining the intended users and decisions accordingly? Do respondents agree with our conclusion that this would require little extra work (paragraphs 8.20 to 8.31)

**APL Response** – We are unsure what is meant by an "informed reader" for the purposes of this question or what is meant by defining the intended users and decisions accordingly.

It must be correct that the Scheme Funding report can be understood by the trustees and the employer otherwise the actuary cannot have done his job. It would also be helpful if the Scheme Funding report can be understood by a numerate beneficiary. Short form summary reports are often issued to beneficiaries in practice.

We are not qualified to comment on how much extra work this would involve.

19. **Question 21** – Would the provision of specimen Scheme Funding reports be of value to users (Paragraph 8.32)

**APL Response:** We are not in a position to comment of whether this would be of assistance.

20. **Question 22** – Are there any other principles on reporting which respondents believe should be in the pensions TAS?

**APL Response** – Actuarial issue

21. **Question 23** – Do respondents think that actuarial comparisons in pensions should be covered in pensions TAS or in a Specific TAS covering similar matters across all areas of actuarial work?

**APL Response** – The APL considers that this is not an issue on which it is qualified to comment.

22. **Question 24** – do respondents have any views on whether it would be of value to users of actuarial information for BAS to maintain a glossary of actuarial terminology and if so, what it should contain?



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**APL Response** – Yes this would be useful although we accept that it should not be in the pensions TAS. Perhaps this could be prepared in conjunction with the PMI.

23. **Question 25** – Do respondents have any comments on the proposed transitional arrangements from the adopted GNs to TASs described in section 10.

**APL Response** – The APL would note that there are some matters dealt with in the existing Actuarial GNs of an ethical nature for which the Pensions Standard Board is not responsible. Care will need to be taken to ensure that if the GNs are withdrawn before new ethical standards are adopted, there is not a gap in coverage.

Also as mentioned in the covering letter at various places specific reference is made to compliance with guidance issued by the Board for Actuarial Standards and even to specific Guidance Notes. If any GNs are withdrawn consideration will need to be given to whether any consequential changes will be needed to the relevant regulations.

24. **Question 26** – Do respondents have any views on whether matters which could be construed as technical or ethical such as those mentioned in paragraphs 10.5, 10.13, 10.20 and 10.24 should be included in the pensions TAS?

10.5 Seeking advice and naming the actuary - **APL Response** – Ethical

10.13 **APL Response** – all technical

10.20 The process for taking instructions to determine whether a scheme satisfies the reference test - **APL Response** – technical

10.24 Bringing the attention of trustees to matters listed in sections 75, 79 or 102 of tPRs code of practice for funding defined benefits on which the actuary has not given advice – **APL Response** – Technical

Bringing to the attention of trustees that prior to obtaining advice they must provide sufficient and up to date information – **APL Response** – Technical