

**Emily Brown**

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**From:** Dick, W Mike [WDick@scottishlife.co.uk]  
**Sent:** 21 September 2009 15:33  
**To:** BAS Pensions  
**Subject:** Comments on Consultation Paper: Pensions

The Comments below are written by me, on behalf of the Pensions Actuaries at Scottish Life.

Rather than provide answers to the questions asked in Section 11, there are some specific points and some matters of principle which we wish to bring to BAS' attention.

**(A) Members as Users**

The first point on which we would like to comment is the proposal, alluded to in 2.5 and further developed in 8.30 and 8.31, where scheme members are to be assumed to be users (albeit to be assumed to be informed readers of Scheme Funding reports) of actuarial information. We believe that this is neither appropriate nor realistic. It is not appropriate since Scheme Funding reports are written, as required by legislative requirements, for the Trustees of defined benefit schemes. The legislation requires the Trustees to produce a Summary Funding Statement to explain the funding position for the benefit of scheme members. The legislation clearly expects this document to inform scheme members and to include the type of information which may inform the decisions they may take. It is also written in a style which may be more accessible to scheme members than a Scheme Funding report. We note that BAS suggests that a scheme member should be assumed to be "informed". It is not realistic in that no actuary can know the range of issues, concerns and intentions of particular members nor how "informed" they may actually be. Consequently, no report produced for a diverse group of members could address their individual needs. It is also worth noting that a Scheme Funding Report will reflect funding matters, and financial conditions, at a date which could be up to 15 months prior to the date it is signed off. (It is accepted that the Summary Funding Statement will be produced at a later date still). There is thus a limit to the validity of any conclusion which a member may draw from such a document – the purpose of which is to describe funding matters for the scheme to the Trustees in a manner which satisfies legislative and other requirements.

**(B) Assumptions**

BAS should not attempt to impose additional conditions on actuarial assumptions in excess of those laid down by legislation or the Pensions Regulator. In particular, the funding legislation only mentions rates of discount, mortality tables and demographic as requiring to be chosen prudently or based on prudent principles. Thereafter, legislation requires only that the overall Technical provisions are prudent. Therefore it is not a requirement that each individual assumption should be prudent. Similarly, the transfer value regulations state only that the overall cash equivalent should be a best estimate. There is no requirement for each assumption to be a best estimate.

**(C) Responsibility Extension**

BAS appears to wish to make individual actuaries responsible for the actions and activities carried out by third parties. It is the Trustees of a defined benefits scheme who will decide which scheme actuary to appoint and which administration company to appoint. There is no requirement that the actuary and the administrator be employed by the same company. It is the Trustees' responsibility to judge and monitor the performance of the administrator, and the responsibility of the administration company to ensure that its staff are properly trained, follow appropriate instructions etc. The implication in 2.3(b), 4.24 and 4.25 of this TAS, that actuaries are responsible for the actions of professional administrators, is inappropriate.

**Para 1.7**

We assume that insured defined benefit scheme are to be included as being covered by the pensions TAS. We would welcome clarification on this point.

**Para 3.5**

Does BAS intend that those complying with the standards document their rationale for matters not contained in a report as well as matters contained in a report? What does BAS have in mind here, bearing in mind proportionality considerations?

How does BAS intend to interpret "rationale"?

**Paras 4.24 and 4.25**

We are concerned that BAS may be suggesting requirements based on a relationship which does not formally exist. There is no direct relationship between administrators (and their systems) and the scheme actuary. It is generally the Trustees who choose the basis for actuarial factors, albeit with actuarial advice. We believe that, in these situations, it is the Trustees, and not the scheme actuary, who should be responsible for checking that the administrators are carrying out their duties in line with the Trustees' expectations.

**Paras 4.30 and 4.31**

We feel that, having regard to the principle that matters on which decisions may be taken should fall within scope, there seems to an inconsistency in not including FRS17 within scope. Many employers have regard to FRS17 results in their decision-making process on scheme funding matters.

The Trustees only implement the scheme in accordance with the Scheme Rules. It is the Employer who will decide the benefit structure and whether benefits continue to be provided. In a "principles based" regime, the principles should apply equally to all reports or not at all.

**Paras 6.13 – 6.15**

Analysis for small and/or insured schemes will not yield much which is statistically significant. We should be grateful for BAS' further guidance having regard to proportionality. We should also be grateful for clarity on what BAS regards as "small".

**Para 6.19**

Is it intended by BAS that there is to be some regard to materiality and proportionality in this requirement? For example a small change to a non-material assumption e.g. proportions married may be covered by a contingency margin.

The principle illustrated here is inconsistent with legislation – see preliminary comment (B).

**Para 6.23**

This paragraph is inconsistent with the legislation [SI2005/3377 Reg 5 (4) (b)] which states that the rate of discount should be set based upon the scheme assets or gilts or bonds.

We are concerned that what is being suggested by BAS at the end of the paragraph is too restrictive, as an example. Gilt yields may be used – which may not reflect the trustees' investment strategy.

**Paras 6.58 and 6.59**

It is our view that regulation 5 of The Occupational Pension Schemes (Scheme Funding) Regulations 2005 requires the trustees or managers to exercise their judgement in reaching a view on prudence; not their advisers. In order to assist trustees, it may be the case that a range of assumptions, with supporting historical evidence, may be presented. It is for the trustees, having regard to their view as to the strength of the employer's covenant, to form a view on where "prudent" sits within this range.

**Para 6.63**

Regulation 7 B.(5) of The Occupational Pension Schemes (Transfer Values) (Amendment) Regulations 2008 states that "the trustees must determine the assumptions under this regulation with the aim that, taken as a whole, they should lead to the best estimate of the initial cash equivalent". This is different to what is stated in para 6.63. We are not clear why the proposal described by BAS is being made.

**Para 7.4**

Although the comment may be made in respect of TAS M, the requirement would seem to require that the users are furnished with a manual describing the computer routines used to place a value on future expected cash flows. Where does BAS see the practical limit being drawn in this respect?

**Para 7.6**

We would be grateful for more detail in respect of the proposal regarding "future increases to benefits". Is this expected to cover assumed future salary increases only? – or to include rates of inflation, revaluation, pension increases etc?

**Para 7.8 and 7.9**

Similar comments apply here as were made above, initially in Preliminary comment (C) and in respect of paras 4.24 and 4.25. We believe that it is for the Trustees to liaise with the administrators as required, not the scheme actuary.

**Para 8.4**

We would rather see the word "material" appear before the word "change" and the word "proposed" appear before the word "assumptions". What does BAS mean by "similar exercises"? Does this relate to the previous exercise of the same form i.e. scheme funding valuation compared to previous scheme funding valuation, or also to latest GAAP figures, CETV report etc?

**Para 8.11**

See comments made under Preliminary comment (B) and under 6.63. The legislation requirements have been mis-stated.

**Para 8.14**

This may not be possible as best estimates at the previous valuation may not have been derived. In addition, it is not a trivial exercise to determine "best estimate". The costs for production of best estimates of each assumption would be prohibitive to most clients.

**Para 8.18**

We are concerned that this proposal is excessive. For example, to allow for GMP equalisation on a maximum liability approach would add significantly to the cost of providing advice to the Trustees. The

benefits of providing this advice, even if a maximum liability could be calculated, are not clear. Given that the legal profession cannot interpret this legislation, the placing of an “upper limit” or “maximum liability” is not possible.

#### **Para 8.28**

For reasons stated above at the start of this email, we do not believe that it is realistic to expect a scheme member to be as well-equipped as a TKU-enabled Trustee. Consequently significant modification would be required to scheme funding reports to make them accessible to members. Although a member is permitted to ask the Trustees for a copy of the report and is always free to ask questions, if the need arises, in our experience, very few members ask for a copy of the scheme funding report. The recent introduction of the Summary Funding Statement may reduce this aspect further.

#### **Para 8.39**

We wonder if there has been some confusion with the wording used here in the proposed principle. We believe that the words “actual cost to” should replace the words “funding of”

#### **Paras 9.7 – 9.9**

When a scheme winds up, the decision by the Trustees on which insurance company to use is an investment decision, not a matter of actuarial advice. The investment advice is likely to have been provided by either an IFA or an investment consultant, whereas the suitability of the individual policy conditions vis-a-vis the Scheme Rules should be provided by a lawyer. These are not matters of specific actuarial competence and hence should not be covered by BAS guidance.

#### **Section 10**

We look forward to further clarity in the debate regarding “technical” and “ethical” guidance and also on how any conflicts between new BAS requirements and existing professional guidance notes (GNs) should be resolved.

#### **Paras 10.15 – 10.17**

Given BAS’ overriding responsibility for actuarial matters, we believe that BAS should maintain a website available to the public in which they define and explain standard actuarial terms including those matters currently covered by GN26.

On behalf of the Scottish Life Pensions Actuaries,

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