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The Director
Board for Actuarial Standards
5th Floor, Aldwych House
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Dear Sirs

Response to Exposure Draft: Pensions TAS

We are pleased to be able to respond to the exposure draft on the Pensions Technical Actuarial Standard as follows.

Members of the Association are all qualified actuaries. All actuarial advice given by our members is subject to the Actuaries' Code. ACA members include the scheme actuaries to schemes covering the majority of members of defined benefit pension schemes.

The ACA is the representative body for consulting actuaries, whilst the Faculty and Institute of Actuaries are the professional bodies.

BAS has used the consultation process to improve its proposed Pensions TAS and we welcome in particular clarity that scheme members are not to be considered as 'users'. Overall, we think the Pensions TAS will help BAS meet its reliability objective, but there are still some weaknesses that need to be resolved.

Particular issues:

- There is still some uncertainty associated with the application of the TASs, because of arguably unclear definitions, which should be resolved. Specific concerns relate to:
 - **The absence of a definition of actuarial information or actuarial work:** Since these terms are undefined, the scope of the generic TASs, for example, can be extended to any work carried out by, or on behalf of, any actuary in a reserved role, in relation to that role. Although professionally actuaries might voluntarily choose to extend the principles underlying the TASs to 'non-actuarial' pieces of work, it seems unproductive for BAS to risk the perception that they have been imposed just because its scope has been misunderstood. The ACA recognises that braver people have tried and failed to define

actuarial work; however, BAS only needs to define the actuarial information and work that it intends to bring into the scope of its TASs, and so the challenge is more limited. In this spirit, we suggest some definitions that BAS could consider:

- **Proposed definition for actuarial information:**
'Actuarial information' is information provided to a user that is used to quantify, or relates to the management of, financial risks.
- **Proposed definition for actuarial work:**
'Actuarial work' is work required to produce 'actuarial information'
- **The definition of users:** BAS has helpfully excluded scheme members from this definition, but we believe the definition should just include the entity to whom the report is addressed. This seems to us to be the effect of the first sentence of the definition, but the second sentence clouds this. For example, when advice is presented to trustees, this is only intended to help the trustees; it is not intended to assist the Pensions Regulator (TPR). TPR may subsequently choose to request the advice, and can take a view then as to whether it is effective. However, it is not possible to know in advance whether this will happen, or what TPR's purpose will be if it does, so it is unreasonably to suggest that advice is prepared 'for the benefit' of TPR (unless TPR is the client).

We suggest that the 'definitions' section of each TAS is kept strictly to definitions and that the remaining content of the TAS is used to clarify a definition where necessary.

- **In its response to the Pensions TAS consultation, the ACA suggested that DC schemes should be excluded from Pensions TAS.** BAS says (2.30) that it has chosen to include them to the extent of work relating to scheme design and benefit projections. However, the scope also seems to extend to bulk transfers, winding up and accounting information, to the extent that 'actuarial work' is involved. This is an example of the uncertainty created by leaving 'actuarial work' undefined. For example, we think it likely that, if an actuary comments on the relative benefits of different expense regimes under transferring and receiving defined contribution arrangements, this would be viewed as actuarial work. However, comparing two expense regimes is not a quantification of risk, so, under our proposed definition, this would not be in scope.

It would be helpful if BAS's intention was made clear (noting that currently defined contribution no-consent transfers are currently subject to GN16).

- **BAS has retained its requirement to quantify the degree of 'prudence' in technical provisions (para E4.2) but, instead of relative to a 'best estimate', this is now to be measured relative to a 'neutral estimate'.**

We would like to make two points:

- BAS justifies retaining the requirement to quantify 'prudence' because users requested it and therefore it thinks it will help with the reliability objective. But this is not necessarily so – something helps with the reliability objective because it is useful information, not just because it is desired information. Users have information about the cost of buying out benefits and the cost of securing PPF compensation, two objective benchmarks that should be both

useful and meaningful to them. Where they wish their technical provisions to sit relative to these two benchmarks should rely on the company's covenant. Although it might be useful to know where certain individual assumptions lie relative to, for example, an estimate of the median or mean value of the population the assumption is assumed to belong to, mandating production of a third liability benchmark, with no automatic relevance to the scheme's position does not seem to add materially to a discussion about the appropriate level of technical provisions.

- **We are not convinced by the use of the word 'neutral'**. All models include some qualitative elements, which are likely to be partly subjective and so unlikely to be neutral, in the sense of unbiased.

At a BAS consultation meeting, a trustee said he didn't understand actuaries' reluctance to have it mandated that they must derive a 'best estimate'. He was an engineer, and he said his profession had no difficulty calculating best estimates. But engineering measurements have low tolerances and are tangible and immediately realisable; actuarial measurements of pension schemes have none of these characteristics. For example, we would normally provide trustees with a range of 'best estimate' assumptions for future yields, but adopting something within the range will not necessarily give rise to a 'best estimate' outcome – e.g. some of the economic scenarios that are likely to underpin a 'best estimate' equity return could support the development of new medical developments or technology that result in lighter than current 'best estimate' mortality assumptions.

Rather than contributing to understanding, an additional measure could create further confusion since an additional set of assumptions will be required, and the resultant 'neutral' measure will not be unique.

We agree that there needs to be some discussion about where the trustees' measure of the technical provisions sits relative to other, meaningful, benchmarks, and we also support explaining to trustees the range of possible assumptions that could be adopted. For some schemes, we would also associate probability values with the assumptions, together with the resulting outcomes (also with probability values). **However, we disagree strongly that it would add value to introduce an abstract measure solely for the purpose of saying that the trustees' measure of their technical provisions is different from it.**

We note that the definition of a neutral measure was also in the ExD of the Modelling TAS and suggest that this be reviewed.

- If BAS has a specific objective it wishes to achieve (for example, compare technical provisions against a calculation produced using median assumptions) then it should say this, rather than creating unclear expectations. For example, IAS19 requires the actuarial assumptions used to be 'unbiased', and states that '... assumptions are unbiased if they are neither imprudent nor excessively conservative'. As mentioned above, we agree that it can be appropriate to put individual assumptions in the context of 'unbiased' estimates, although we would not support a requirement to include an 'unbiased' estimate of the liabilities.

- **Scheme funding reports:** although the report required by legislation that completes the valuation process is in scope of the generic TASs, normally it is provided to trustees after all material decisions have been taken. Consequently, it would be considered at most a component report (since it might be relied on in future) and the TASs would impose few requirements on it. However, BAS has chosen to bring it into scope of the Pensions TAS (although we observe that, since it is still the case that no users will make material decisions based on the report, it is possible to ignore the requirements).

The consultation response says this was at the request of ‘users’, but whilst we think there could be a role for the report we are not convinced that a BAS TAS is the place to define that role.

Rather than a report to trustees, BAS has recast it as a potentially helpful document for scheme members. This does not help BAS meet its reliability objective; and since the required information goes beyond information likely to assist scheme members make decisions regarding the scheme, such as cash flow projections and funding levels under different scenarios as well as sensitivity analysis, we do not believe it will be helpful to scheme members either.

Under current legislation the report remains the responsibility of the scheme actuary, which is presumably why BAS agreed to this compromise. However, to address the conflict between the report’s content and its (now) intended readership, BAS has had to invent an ‘informed reader’, who members may or may not have access to. This and the proposed content go beyond the legislative intent. Although we can see a role for a detailed report from trustees to members on their approach to the valuation and planning exercise, we are not convinced that this is the best way to achieve it. Discussion with the DWP and TPR about the possible alternatives might result in a better solution.

- Each TAS contains about 20 principles. Not all of them are unique, but it is not always clear how they are associated. Although BAS wanted to avoid a tick box mentality, the plethora of principles means that people will start to adopt this approach to determine whether they have complied appropriately with the necessary standards. Fewer ‘stand alone’ principles would be far more likely to encourage thoughtful best practice, so we recommend that, before publishing the pensions TAS, BAS reviews the principles included and replaces them with references to the relevant principles in the generic TASs where this is possible. Then, the pensions TAS (and other specific TASs) can be reduced to a clarification of a small number of existing principles, rather than a development of new principles.

BAS issues:

1. The application of the Pensions TAS to schemes not subject to Scheme Funding (paragraphs 4.19 to 4.21)

It seems appropriate for similar actuarial standards to apply to defined benefit schemes not subject to Part 3 of the Pensions Act 2004.

2. The definition of governing body, especially examples of schemes for which the definition is not appropriate (paragraph 4.22)

The definition of governing body refers to ‘pension schemes’ and the TAS’s definition of pension scheme includes personal pension schemes. Although

these do not have governing bodies in the same sense as an occupational scheme, nonetheless there are aspects of governance associated with them and there are 'bodies' (for example, the employer) that are considered responsible.

We are not sure what the intention is, and we do not think it creates special issues, but think the TAS would be a stronger document if the intention was made clear.

3. The proposed commencement date for the Pensions TAS (4.23-25)

Using the proposed implementation date, the TAS will apply to work being carried out now. Provided no material new requirements are added, the proposed date seems workable. However, the staggered commencement of BAS's standards is not helpful, and our answer depends partly on the outcome of the consultation on the transformations TAS. If a transformations TAS is required, we would suggest the two commence on the same date, even if this would defer the introduction of the Pensions TAS.

4. The transition to the Pensions TAS from the adopted Guidance Notes (5)

We have no comment on the suggestion in respect of GN9, 16, 19, 34, 36 and 49.

GN 28 – we suggest that BAS could use a technical memorandum to reproduce its effect. We believe this would be preferable to putting the reference scheme test into legislation.

5. Our impact assessment and the effects that the introduction of the Pensions TAS is likely to have on actuarial information (6)

Although we agree that the ongoing costs of complying with the TASs is unlikely to be material, a one off cost of transition of 5-10% of revenue is not immaterial. Larger consultancies might be able to bear this, although it will be a significant dent in profit margins, but smaller firms, for whom the costs are likely to represent a higher proportion of revenue, might find it a challenge. Although we agree that, in general, the outcome should be better communication and so presumably better understanding of the underlying risks, we are not certain that in all cases this will be material enough to justify the additional requirements.

If the requirements to produce the scheme funding report remain, we do not agree that the TAS will not result in higher costs for scheme funding assessments.

6. The text of the exposure draft as a means of implementing the proposal presented in this document.

The reliability objective could be improved if some language was made clearer.

For example:

D2.10 – should read: 'two similar and related exercises'.

D2.14 – the implications of the first bullet are not clear. Possibly the intention is to illustrate that adopting a weaker assumption for valuing certain member options could lead to lower contributions or a stronger solvency position if lots of

members elect that option, although this is implicit in the second bullet. In that case, we suggest it would be clearer to say:

D2.14 – an explanation of the implications of adopting particular discount rates might need to include the possible effect on the scheme's future funding level (on a solvency or a technical provisions basis), or on the level of future contributions, assuming different scenarios for future membership experience.

D2.18 – there could be examples where mortality assumptions need not relate directly to the scheme's membership. For example, when investigating how a longevity swap is priced relative to the scheme.

F – It is not clear whether section F applies to 'target' DC schemes, or just to defined benefit arrangements not covered by Part 3 of the Pension Act 2004.

We hope this is helpful.

Kind regards

Charles Young
Chairman
ACA Pension Schemes Committee