

Barnett Waddingham

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The Director
Board for Actuarial Standards
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Our Ref: NCG/PRG/5211

Dear Louise

Technical Actuarial Standards – Pensions (TAS-P): Exposure Draft

Barnett Waddingham LLP is a UK based firm of actuaries and consultants. We provide a range of actuarial and consultancy services to trustees and sponsoring employers of occupational pension schemes, life insurance companies and friendly societies. We have therefore considered the consultation paper on the proposed pensions Technical Actuarial Standard (TAS-P) with a great deal of interest.

The following represents the views of many, but not necessarily all of the actuaries working at Barnett Waddingham LLP.

Neutral Estimates

As set out in our response to the earlier consultation on TAS-P (September 2009), we are in general agreement with the Board's proposed approach of issuing guiding principles, rather than prescribing actuarial output. Our sentiment extends to the three Generic Technical Actuarial Standards (TASs).

Our main concern is in relation to **Paragraph E.4.2**, which will require an actuary advising on scheme funding matters to show "approximate" liability figures on "neutral" assumptions to compare with the prudent position. Whilst we note that BAS acknowledge that there may be a range of assumptions that could be considered "neutral", we are concerned that they may not appreciate just how big that range might be.

As an example, the range of possible "neutral" assumptions for the rate of return on equity investments could be as wide as 2%. A 2% lower investment return assumption would add between 30% to 50% to the liabilities – ie a substantial range for potentially "neutral" liabilities that makes any comparison with the "prudent" liabilities proposed pretty meaningless in our view (and would in fact decrease the reliance that users of such actuarial information can place on it).

We are also concerned about the definition of a "neutral measure" in the TAS. Arguably, the yield on UK Gilts is the closest to an objective assessment of the cost of risk-free borrowing in the markets and therefore the only discount rate that fits definition of "neutral" in this context. However, calculating liabilities using an unadjusted gilt yield in a funding valuation is, in most situations, a "prudent" approach.

In our view, it is appropriate that the actuary should be discussing the level of prudence with the trustees. Sometimes, the best way for trustees to understand the level of prudence will be by reference to a "best estimate" or "neutral" position. But, for the reasons given above that will not always be the right approach, and so we believe BAS should not be prescriptive about this. Effectively BAS will be prescribing the need for an extra set of valuation calculations, that may well not be helpful, and which goes further than anything required by

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legislation or the Pensions Regulator.

The BAS has stated (paragraphs 3.48 and 3.49) that more emphasis has been placed on the needs of users. Trustees are free to request whatever alternative valuation bases they want, and we would of course be happy provide this. However, there is an issue here in what must, in all circumstances, be included. We don't believe that the provision of a neutral estimate would benefit many users in the way BAS suggest. In fact, users would benefit from advisers cutting down the number of alternative valuations, not increasing them.

We are concerned that BAS has missed this point. We note that very few Trustees appear to have responded to the consultation.

We still have some practical concerns over how neutral estimates will be arrived at. In particular with regards demographic assumptions, where in my view prudent usually doesn't mean "best estimate plus a margin". For example, in many cases no allowance is made for withdrawals or cash commutation because it is prudent not to do so and the likely incidence can't be estimated with any confidence. Including a neutral estimate for these items would be of little or no benefit to most users.

Costs are an important issue as additional costs incurred by an actuarial adviser will inevitably be passed onto users. We don't agree with the argument that providing a neutral estimate won't lead to extra costs because the actuary will already be carrying out a sensitivity analysis (see below).

General Comments

We are still concerned that, despite the BAS stance that all TASs should be applied with judgement and proportionality, the TASs could be quite onerous in their application, particularly for smaller pieces of work. If being sued, the defending actuary will automatically be put on a weak footing if a relevant TAS has not been followed in full, even where this is not pertinent to the case and regardless of BAS's suggestion that the actuary can use a proportionality defence.

We are pleased to note that, in general, the exposure draft is clearer on which non-Reserved work is in scope compared with our expectation based on the original consultation document.

We agree that pension scheme members should not be considered "users" of a scheme funding valuation report. However, in our opinion the exposure draft should explicitly state that scheme members are not users. From a legal standpoint, we do not feel that we can unequivocally rely on BAS's opinion (paragraph 2.9 of the consultation document) that members would not be users under the existing wording.

Paragraph 2.19 of the analysis of responses to the original consultation considers the potential duplication of work arising from the wording of the TAS where an actuary is advising a company in relation to scheme funding matters. The BAS says that "the Scope and Authority permits those responsible for commissioning work to instruct the actuary responsibility for carrying it out to depart from specified (or all) requirements of TASs, as long as the work in question is neither Reserved Work nor Required Work.

In our view, this is not a practicable solution to the potential problem for the vast majority of our scheme sponsor clients, who will simply not know what to instruct the actuary to leave out. This leaves the actuary in the awkward position of having to instruct the client as to how to instruct the actuary as to which parts of the TAS can be ignored. What would the legal status of such advice be?

BAS questions

In response to the specific questions raised in the most recent consultation document, we wish to make the following comments:

- 1) *the application of the Pensions TAS to schemes not subject to Scheme Funding*; No comments to add.
- 2) *the definition of governing body, especially examples of schemes for which the definition is not appropriate (paragraph 4.22)*; No comments to add.

3) *the proposed commencement date for the Pensions TAS (see paragraphs 4.23 to 4.25);*

Provided that the finalised TAS is published in good time, we have no problem with the proposal for the Pensions TAS to apply to aggregate reports completed on or after 1 April 2011.

In fact in our view, the shorter the period of overlap between TAS-P and the Actuarial Guidance Note GN9, the better. In this regard, our preferred approach to reduce compliance costs would be for compliance for GN9 to become optional for any aggregate report

4) *the transition to the Pensions TAS from the adopted Guidance Notes (see section 5);*

GN9 – see comments above

GN16 – we have found Counsel’s opinion on the “broadly no less favourable than” test to be helpful in the past and would urge BAS to ensure that the Profession maintains this document on their website.

GN26 – we expect that the Actuarial Profession would be best placed to support and maintain a glossary of actuarial terms.

GN28 – we would hope that the BAS’s discussions with the DWP are fruitful. We believe it is important to maintain the existing aspects of GN28 which give rise to an interpretation of the Reference Scheme Test (eg the treatment of spouse’s pensions as noted in the consultation document).

GN49 – we suggest that GN49 is disapplied with immediate effect now that references to it in legislation have been removed and the matters covered by GN49 are effectively covered by the generic TASs.

We have no other comments on the transition from existing Guidance Notes to the new regime.

5) *our impact assessment and the effects that the introduction of the Pensions TAS is likely to have on actuarial information (see section 6);*

We do not necessarily agree with BAS’s assertion that valuation costs will not increase when TAS-P comes into effect, because of the “neutral estimate” proposals. Even though the additional calculations required will be estimates, there will still be an associated increase in time spent producing them, and therefore an increase in costs to our clients.

The implication, it seems, is that the actuary will simply include a single figure in the form: “the neutral estimate is about £X”. We think this underestimates the importance of the neutral estimate to the Scheme Funding process and the potential disagreement between actuaries as to what it represents and how it should be determined.

BAS make it clear (paragraph 3.53) that they do not see funding negotiations as relevant to their standards. However, these are still practical realities and actuaries will want to devote a lot of attention to the calculation of an “accurate” neutral estimate, and also ensure that its derivation and uncertainty are communicated clearly to the client.

Furthermore, we believe that the requirement to explain the cashflows being discounted (paragraph D.2.12(c) could lead to additional costs with little material benefit to the user. This is particularly true for small schemes or schemes where pensioner benefits have been secured via an insurance company contract in the trustees’ name (a “buy-in” policy).

Finally, in the medium term, an actuarial valuation carried out over the next 12 months or so could potentially be subject to TAS-R, TAS-M, TAS-D, GN9 and GN49, further increasing the costs of compliance.

We do not agree with the view expressed in paragraph 6.13 of the consultation document that “much of the cost of transition” will be borne by actuarial advisers. These costs will be commercially significant which a competitive business may need to pass on, at least in part, to its clients – albeit this may not

need to be applied immediately. This will be particularly true for smaller consultancies who could not afford to simply absorb the new additional costs highlighted above.

6) *the text of the exposure draft as a means of implementing the proposals presented in this document.*

Paragraph C.1.15 says that the standard “shall apply to actuarial work ... that concerns winding up”. What does “actuarial work” mean in this context? Are we to assume that the specific examples listed are to imply a fairly narrow interpretation of this term, or is it all work undertaken by an actuary that is related to a wind-up (in which case, this may also encompass consultancy that is not particularly actuarial in nature)?

Paragraphs D.2.1 and D.2.2 refer to “assumptions used in, or proposed for use in, models”. We feel that the wording should be amended to “assumptions proposed for use in”. The TAS should only set standards for proposals made by the actuary. If a governing body decides to use something different, where it is their decision, and the actuary feels that this is materially inappropriate, then TAS-R and D.2.7 already require the actuary to comment on this.

Paragraph D.2.3 is too onerous and should be removed. There is no need, in our opinion, for an actuary to comment on the appropriateness of *every* assumption. TAS-R and D.2.7 already require the actuary to comment if (s)he feels the assumptions as a whole are materially inappropriate. We think this should be the key principal for a standard on assumptions.

Paragraph D.2.10 requires the actuary to “explain any changes in the rationale underlying the assumptions between two similar exercises”. We are concerned that “similar” in this context should be properly defined so as to avoid unnecessary additional work.

Paragraph D.2.16 is unnecessary as it repeats what is already covered by D.2.12(a) and D.2.13.

Paragraph D.4.1 could leave the actuary open to criticism where he has provided instructions that he feels are “sufficiently clear” but errors are still made by the users of those instructions. We feel that the interpretation of “sufficiently clear” is too subjective.

Paragraph E.3.6 states that “aggregate reports shall include an explanation of any uncertainty in benefit definitions due to overriding legislation.” We believe this should be amended to “aggregate reports *might need to include...*” as it will not always be appropriate to include a range and a sensitivity analysis for every material assumption. The actuary should be able to use his/her judgement and the existing wording may discourage this. The revised wording would be consistent with other sections of the standard where judgement is expected to be applied.

Paragraph E.5.10 requires the actuary to state what actions have been taken to mitigate risks. We do not believe this is necessary – it is the pension scheme trustees’ responsibility to manage risk. Unless the actuary is specifically advising on ways to manage risks, we feel that it would be more appropriate for the aggregate report to refer to the trustees’ risk register.

If you would like to discuss any of our comments in more detail, please let me know.

Yours sincerely

Tyron Potts
Fellow of the Institute of Actuaries
Barnett Waddingham LLP