



Actuaries & Consultants

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17th August 2010

Ms L Pryor  
Technical Director  
Board for Actuarial Standards  
5th Floor, Aldwych House  
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London  
WC2B 4HN

Dear Louise

**Transformations – June 2010 Exposure Draft  
Lane Clark & Peacock LLP (“LCP”) response**

**1. Our expertise and areas of work**

Lane Clark & Peacock LLP (“LCP”) is a leading firm of actuaries and consultants, with over 90 partners, and a team of more than 450 employees across Europe. The firm provides actuarial, employee benefit, investment, insurance and risk management related advice as well as pensions administration services. Our main focus is in the pension advisory field and our response has been prepared on this basis.

**2. Our response to the consultation**

Our responses to your individual questions, set out in section 7 of your consultation paper, are provided in the appendix to this letter.

We would also like to make the following additional points:

**2.1. Development of the Standard**

It is quite clear that the proposed Standard has been subject to significant development as a result of the consultation process. We in particular welcome the following:

- Clarification that by “transformation” you mean only those situations where changes are occurring without member or policyholder consent;
- The elimination of proposed principles that were duplicating principles found elsewhere;

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- That you have chosen not to develop any content of universal application which is ethical in nature – we had in particular some concerns that you intended to set some principles around “fairness” that would have been inappropriately applied to pensions transformations;
- A shift to explaining how certain principles found in the generic TAS should be interpreted in the context of transformations work.

However, there remain some areas of difficulty for us:

- We have a concern that you have developed your principles for transformations from too generic a standpoint and have not, for example, taken into account the way in which pensions Guidance Note 16 and Guidance Note 51 have been expressed and the legislative background from which they were constructed.

We would have expected to have been able to see quite readily, how the protective principles, contained within these Guidance Notes, have been taken across and in fact for you to have told us how you had done it. At the heart of both Guidance Notes is the contention that the protection offered by the actuarial certificate is not enough and that more information (some of which cannot be called “actuarial information” in your language) may well need to be brought to the attention of “users”, in this case the trustees, before they are equipped to take their “decisions”.

We believe that before GN16 is switched off and the Actuarial Profession makes any necessary adjustments to GN51, you need to work closely with the Profession to examine the contents of both documents. This may result in further principles being inserted into the Transformations TAS or, perhaps more likely, a related document being produced by the Profession, to be settled at the same time as the Transformations TAS is switched on.

- We are concerned that the TAS contains principles, particularly in section D.4, suggesting that there is a requirement to act in a manner outside the scope of the Reliability Objective. We also are concerned that there is a requirement which is in tension with those situations where the actuary’s role is one of expert evaluator.

Given the need to work closely with the Profession on these matters we have, as before, copied our response to Richard Maconachie.

## **2.2. Your decision regarding proceeding with a separate Transformations TAS**

We note your decision to proceed with a separate Transformations TAS, against the overwhelming weight of opinion expressed to you in respect of the December 2009 consultation paper.

Our concern on examining that paper was that you had not made a sufficiently strong case for a separate TAS and we therefore suggested that the principles should be developed within TAS Insurance and TAS Pensions. Now that you have done some further work we are less concerned about there being a separate TAS for transformations, but we are not completely persuaded.

Firstly, our analysis of this Exposure Draft reveals that many of the principles do not seem suited to pensions transformations. They may be better suited to insurance transformations.

Secondly, we believe in the contention that the fewer TASs a piece of work is subject to the better, not least from the practitioner's viewpoint. We appreciate your focus is on users rather than practitioners, but we believe that more accessible standards are in the interests of both. Restricting any area of work to the scope of one topic-specific TAS as well as the generic TASs will:

- Make it easier for users and practitioners to understand the level of compliance required (given the BAS's intention in section 2.9 of the Conceptual Framework document that standards should be intelligible to lay readers);
- Reduce the time taken for practitioners to comply with the TASs, reducing the costs for users;
- Limit the possible conflict between principles in topic-specific TASs that are worded or emphasised differently, reducing confusion for practitioners and reducing the risk of undermining practitioner confidence in the standards; and
- Limit the risk of user confidence in the standards being undermined by the difficulties that a non-specialist (or even specialist) user may have in understanding the combined effect of the various applicable standards and the interactions between them.

Given that you have chosen to prepare a TAS covering many disparate areas of pensions actuarial work (and for that matter the many disparate areas of insurance too) we do not warm to the proposition that a particular aspect of this work – namely transformations – merits treatment in the form of two topic-specific TASs. The structure of both TAS Insurance and TAS Pensions acknowledges that there are special situations that merit their own suite of principles. It seems a straightforward matter to continue in this vein and add further sections dealing with insurance and pensions transformations. There are in fact dangers in proceeding with a separate TAS unless you can be absolutely sure that there is a mirroring in the scoping (as you intend) and that none of the principles in one TAS are in tension with any of the principles in the other (as you must surely intend).

We acknowledge your decision to proceed with a separate TAS for transformations (which, from your response to the Consultation Paper, seems to be driven mainly by administrative convenience for you), but ask that you review this decision at two points:

- once you have settled the text for TAS Insurance and TAS Pensions; and
- as part of your general review (post completion and issue of all the TASs) as to whether all the material is in the right place.

Please feel free to contact us if you would like to discuss any of the points we have made.

Yours sincerely

{Sent as an attachment to an e-mail on 17th August 2010 at 13:46}

Fiona J Morrison FIA  
*Partner*

Enc:           Appendix

Copies to:    bastransformations@frc.org.uk  
                  Richard Maconachie, Head of Professional Regulation, The Actuarial Profession

## Response to specific questions

**1. The proposed commencement date of the Transformations TAS (paragraphs 4.14 to 4.16)**

We are relaxed about the proposed commencement date of 1st October 2011, which we trust is intended to be after the commencement of TAS Pensions and TAS Insurance. We also welcome the implication of issuing the TAS by the end of 2010 that there is at least a nine month period between the settling of the content of the TAS and its commencement. This will not only enable the actuarial community to assess its impact, but also recognise that work within the scope of the Standard can be subject to extended timescales. It also gives you scope to revisit your decision to proceed with a separate TAS for transformations, if in fact it becomes much more straightforward simply to create a fresh section in each of TAS Pensions and TAS Insurance.

We are not sure from when you intend to withdraw GN16. In this consultation it seems to be from when the Transformations TAS commences. In the consultation on the exposure draft of the Pensions TAS, it was when the Pensions TAS commences.

GN16 contains a number of important matters regarding transformations, some of which should be picked up by the Transformations TAS and others potentially by the Actuarial Profession. We ask you to work closely with the Profession to ensure that there are no unintended gaps (from either of your perspectives).

We are unable to reconcile the phrase “This standard applies to work performed for aggregate reports completed on or after 1 October 2011” under the Commencement sub-heading, with the use of the wording “actuarial work.... in connection with...” in the Scope section. Should you replace the former with something along the following lines?

“This standard applies to actuarial work completed on or after 1 October 2011 and earlier actuarial work in connection with aggregate reports completed on or after 1 October 2011”

**2. Our impact assessment and the effects that the introduction of the Insurance TAS is likely to have on actuarial information (see section 6)**

Your impact assessment is little more than a number of assertions that any additional costs will be modest. We have not seen any scientific backing for this view.

Looking through the three finalised generic TASs, the current exposure draft of TAS Pensions and this exposure draft for TAS Transformations, we believe that there are between 70 and 80 principles that will need to be assessed when undertaking transformation work. In the list below we have counted those principles that appear in boxes in each of the TASs. However, it seems to us that there are a number of further principles which are outside the boxes, bringing the total closer to 80 principles:

- TAS Reporting – 25
- TAS Data – 7
- TAS Modelling – 16
- TAS Pensions – 15 (we have counted only those in sections D.1 to D.3)

- TAS Transformations – 8

Whilst we accept that aggregate reports will not necessarily get longer, you cannot ignore the cost of a doer, a checker and a reviewer using their judgement on applicability, materiality and proportionality to ensure that around 80 principles are being applied appropriately.

Despite all these principles it is unlikely that users will be able to take sound decisions on pensions transformations on the strength of the multiple TAS-compliant actuarial information alone. This is because there are important financial considerations of a non-actuarial nature – in particular the employer covenant given its importance to pension security – as well as ethical matters that users may need to take into account.

### **3. The text of the exposure draft as a means of implementing the proposals presented in the document**

We set out below a line by line comment on the Transformations TAS starting with section A. Our comments have been made on the basis of the text in the document being exposed. We are aware that some of this text may be in the process of being adjusted by you as a result of comments received on other BAS Standards under development.

#### **3.1. Part A**

The words “including information on cash flows, risk and uncertainty” in A.1.2 appear to mandate information on each of those areas. We would prefer that the word “potentially” is inserted before “including” so allowing for cases where information on those areas might be inappropriate.

We remain sceptical that the actuarial information supplied within a pensions context will be sufficient in itself to enable the users to assess fairness issues (indeed principle D.4.16 has been adjusted to reflect that it only applies where an opinion on fairness is given). Yet this is the implication of a reading of the last part of A.1.2. We believe the last bullet of A.1.2 should be reworded along the following lines:

“to assess the impact, including security, level of benefits and, where appropriate, fairness on beneficiaries”

#### **3.2. Part B**

We have some difficulties with a number of your definitions set out in section B.2. They are as follows:

- Actuarial factor – this is defined in relation to actuarial techniques but as you are not giving any guidance as to what is actuarial work, it is not clear when a factor becomes an actuarial factor.

In any event, you do not appear to use the definition within this Standard and so it can be removed.

- Governing body – we feel that your definition is insufficiently precise. It is not clear whether the employer is brought within the definition where it has a role in

part of the governance of an occupational pension scheme – eg where the employer has the power to set the commutation terms. We feel that you should make a specific exclusion here otherwise you may find that, unintentionally, corporate actuarial advice on transformations is brought within scope.

A further difficulty is in understanding what is meant by the governing body in relation to personal pension schemes (potentially brought into scope through your definition of “pension scheme”). Are you intending to cover the employer here, the product provider, or both? Or do you in fact not intend to cover such schemes? It is not clear to us how a transformation can apply to a personal pension scheme.

- Measure and method – it is not clear to us how the generally accepted pension funding methods (described in Guidance Note 26 and called on in the Pensions Regulator’s Code of Practice 3 on Scheme Funding) fit within these terms. Perhaps they don’t at all. Is the projected unit method a method under your terminology or is it a measure? Or is it neither of these? We suggest that there should be some clarity here otherwise there will be scope for much confusion amongst actuaries and users (which in turn will be at odds with paragraph 2.9 of the Conceptual Framework).

In any event, you do not appear to use these definitions within this Standard and so they can be removed.

- Neutral – It is not clear, from the drafting, what is meant by a “*neutral measure*” (which although an emboldened term is not defined). We understand that the intention is for the measure selected to be without bias. So, for example, in establishing a neutral measure of the buyout cost of a pension scheme’s liabilities, neutral assumptions would be used and the resulting estimate would be intended to be neither a cautious nor an aggressive estimate of the cost.

In any event, you do not appear to use the definition within this Standard and so it can be removed.

- Pension scheme – some precision is needed here so that it is clear to which UK legislation you are referring. Our suggestion is that you should refer to the definitions of “occupational pension scheme” and “personal pension scheme” within section 1 of the Pension Schemes Act 1993. Without such precision it will not be clear what types of pension scheme are in scope. Under your current approach there may be confusion with other parts of legislation where “pension scheme” is explicitly defined (see in particular section 150 of the Finance Act 2004 which is a very broad definition and extends to include certain overseas schemes). Even with our proposed linkage the definition would draw in some unusual pension arrangements, such as funded and unfunded EFRBS and certain overseas schemes. We are not clear whether you intend that they should be covered.
- Pension transformation – this does not seem to be right and it seems to be inconsistent with C.1.5 and C.1.6. We think that you need to express the definition in terms of a change, without the consent of all the **affected** (our emphasis) members. In pension transformation work it is common to segment

the scheme membership so that only a subset of the entire membership is subject to the (non-consent) transformation.

### 3.3. Part C

As with the Pensions TAS, the scoping can only be expressed meaningfully if you provide some guidance as to your intended meaning of the phrases “actuarial information” and “actuarial work”. Whilst we were disappointed with your stance when you exposed TAS Pensions, we note the development in your thinking on this subject in paras 4.12-4.13 of the response to the consultation on TAS Transformations.

Nevertheless, we feel that you should give further guidance on what is and is not actuarial work within the context of the Transformations TAS otherwise the interpretation by pensions actuaries is likely to be limited to no more than the specific inclusions you have set out in C.1.8. Examples of certain exclusions from scope are particularly helpful.

Looking at each pensions non-Reserved Work area in turn we comment as follows:

#### C.1.5 – Transfers without consent

Can you provide some clarity as to the intended scope? The actuarial reader may believe that this is intended to be a replacement for GN16 and so only those situations to which Regulation 12 of the Occupational Pension Schemes (Preservation of Benefit) Regulations 1991 applies are intended here. But the drafting brings into scope transfers between all types of pension scheme, including for example a transfer from one personal pension scheme to another.

It is also not clear whether you intend to bring into scope actuarial work carried out for the governing body of the receiving scheme.

We assume that the expression “*in connection with*” will exclude work that is undertaken at a very early stage to check the general feasibility of a potential transformation project. If it does not then we assume that the materiality and proportionality safeguards can be applied to limit the compliance required at this stage.

#### C.1.6. – Modification of benefits without consent

Some further clarity would be useful here too. Once again, the actuarial reader may believe that this is intended to be consistent with the situations to which GN51 applies and so only those cases governed by Section 67 of the Pensions Act 1995 are intended here. But the drafting brings into scope:

- Changes to benefits which have yet to accrue, which would not seem appropriate given that scheme sponsors are generally free to make such changes, subject to only a consultation process for “listed changes”;
- Changes to benefits which have accrued but which fall outside Section 67 because, for example they are specifically exempted or they fall under Section 68.

Our point above in relation to the expression “*in connection with*” applies also to this area of work.

### C.1.7 – Securing benefits with an insurance company on a scheme’s winding up

We feel that the phrase “actuarial work... that concerns” is far too broad and could bring into scope all kinds of activities undertaken by the actuary when a scheme is in the process of winding up, much of which will not be transformational in nature.

It is not clear to us why the phrase “without the consents of those members” is missing from C.1.7.

On C.1.8 it is not particularly helpful to list three types of actuarial work as if they are of potentially equal application across the three distinct areas of actuarial activity in C.1.5 to C.1.7. For example, it is not clear to us that the first bullet is relevant to C.1.7 and the second bullet is unlikely to be relevant unless you are intending to cover partial wind ups. There may be more merit in taking the three areas in turn and setting out for each of them which aspects of advisory work will be treated as actuarial work and list some areas of activity which will not be regarded as actuarial work.

## **3.4. Part D**

Our thinking on the actual principles has evolved now that we have seen them on the face of the proposed Standard. We are having difficulty with nearly all of them, as they apply to pensions transformations.

### D.1 – Introduction

D.1.2 seems to be misplaced. As it is about scope it would seem to naturally belong in section C.

We believe that the principle set out in D.1.3 should in fact appear in section B since it is not so much a principle but rather a guide to interpretation of all the Standard (and not just section D).

### D.2. Assumptions

D.2.1 – We continue to have some significant difficulties here. ”Proper emphasis” is a powerful term, but you do not then go on to give an explanation of what you intend by it, stating instead in D.2.4 what it may not mean. Do you simply mean that, when selecting assumptions, the actuary must reflect with some gravity on the precise nature of his or her role? We believe that it is essential that you set out your thoughts in this area, because, as we mentioned in our response to the earlier paper, without some anchoring the term is capable of wide interpretation.

We believe that assumption setting has little application to pensions transformations:

- In pensions modifications (C.1.6), because in Section 67 work the legislation requires the actuary to select assumptions that are consistent with the cash equivalent basis in order to carry out his or her statutory role;
- In pensions wind ups (C.1.7.), because assumptions are likely to only be relevant in Section 73 work in relation to determining asset shares and here they have to be determined on a buyout basis;

- In pensions transfers (C.1.5), because in practice there are very few GN16 situations where actuarial calculations are required (because the benefits are changing shape). More typically, benefits will be mirror image. And in those situations requiring actuarial calculations, they tend to be insensitive to the particular assumptions.

But where assumptions are relevant is another problem that the certificate relates to the people being transferred, whereas there are members in receiving schemes who could be affected? Are they supposed to be considered when setting the assumptions?

We suspect that this principle is of greater relevance to insurance transformations than it is to pensions transformations given the different role that is performed. As such it might have been a principle you would not have been taken forwards if the principles had been developed in a separate section of the Pensions TAS.

We believe that further work is needed on the drafting of this principle and the explanations subsequently given in D.2.4.

### D.3 – Data

We have no comments on this section.

### D.4 – Reporting

D.4.1 – We supported this principle and welcome your example wording in D.4.2 with the exception of the third bullet which seems to introduce a requirement to comment on the employer covenant, which is, in the pensions context, not within the area of expertise of many actuaries.

D.4.3 – D.4.4 – These principles seem to be covered adequately by C.5.5 – C.5.7 of TAS R. We therefore believe that they should not appear as new principles in TAS T, but as extensions to the TAS R principles. Having said this, in relation to pensions transformations we are concerned that these principles may be taking you beyond your remit. The risks are not limited to actuarial ones (in the drafting), so they could be interpreted as requiring actuaries to give out non-actuarial information (such as opinions on the employer covenant which seems to be the implication of the first bullet of D.4.5).

This may be another instance where the TAS needs to differentiate between pensions and insurance transformations.

D.4.7 – We do not understand the meaning of the first bullet. It also seems to be covering a situation where the actuary is providing thoughts which lie outside actuarial expertise.

D.4.8 – D.4.17 – All these paragraphs are set out under the heading of “Range of assumptions”. But it seems that only paragraphs D.4.8 – 4.11 relate to that subject. Perhaps you need some further headings?

D.4.8 – D.4.11 – In D.2. we suggest that the selection of assumptions plays little part in pensions transformations. If we are correct in this analysis, then your thoughts in relation to alternative plausible assumptions, outlined in sections D.4.8 – D.4.11, will also be of little relevance in pensions transformations.

D.4.11 – We have difficulties with the concept of indicating the “degree of comfort” with which the actuarial certificate is given. Such disclosure has the potential to undermine the actuary where he or she is called upon to be the expert evaluator giving a formal opinion. We believe that the proper place for such a concept is where the actuary is in an advisory role and others are taking the judgment.

D.4.12 – It is not clear to us how to interpret “*change in the value of the interests*”. Is it intended to be limited to actuarial values or is a broader interpretation intended to encompass, for example, change to benefits and conditions of their payment? For example, in a Section 67 situation, if it were known that there was to be an adverse change to a death in service lump sum, which, due to its nature, falls outside the actuarial certificate, would this be a “*change in the value of the interests*”? And what about a reduction in a benefit, that is offset, for the same member, by an improvement in another?

Also, within pensions transformation work, it is often not necessary to indicate the extent of any change when the actuarial role is to provide advice and expert opinion on whether or not affected members are worse off.

D.4.14 – We have some difficulty in interpreting “*benefits to be gained*”. To what extent (if any) do such “*benefits*” go beyond those, for which actuarial expertise is required in order to assess? Are benefits that are lost covered, or are they intended to be picked up in D.4.12? It is also unlikely that the actuary will be equipped to indicate, other than in a superficial manner, the “*advantages to the party proposing that the transformation should proceed*”. There could be some unknown unknowns as far as the actuary is concerned.

D.4.15 – We are not sure about these indications in relation to pensions transformations:

- In the first bullet “*the effect on security of benefits of a change in pension scheme sponsor*” seems to be a request for covenant type information which, of course, is not actuarial information.
- We are unable to interpret your intentions in the second bullet.

D.4.16 – We have not commented on this on the grounds that in pensions transformation work the actuary will not be required to give an opinion on fairness. Again, this is a principle that may well have appeared in a transformations section of the Insurance TAS, but not its equivalent in the Pensions TAS.

**In addition to the specific questions listed above, the BAS invites respondents’ views on any other aspects of the proposed TAS. To ensure that the significance of their point is fully appreciated by the BAS, respondents are asked to indicate how their comments would address the BAS’s aim of increasing the reliance that users of actuarial information can place on it.**

We have no further comments to make.