

# MERCER

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26 August 2010

Subject: Transformations TAS exposure draft

Dear Sir

Mercer Limited is a global leader for HR and related financial advice and services. In the UK, our client base includes employers and trustees providing occupational pension schemes to employees in all sectors of industry; we provide pensions advice and services to companies in the FTSE100 but we also have a large proportion of clients that are employers classed as “Small to Medium sized Enterprises”, or trustees of pension schemes with sponsoring employers in this class.

We welcome the opportunity to respond to the exposure draft published by the Board for Actuarial Standards (BAS) on transformations.

As our business involves advising companies and trustees on pension arrangements, we will comment from this perspective. We have not commented on the insurance aspects.

Overall, we do not consider that the Transformations TAS will contribute to the Reliability Objective in respect of work done in relation to occupational pension schemes.

The appendix to this letter sets out our answers to the questions asked in the exposure draft.

In addition we would like to make the following points:

Changes since the original consultation paper

We welcome the BAS’s move to introduce changes following the consultation process.



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In particular:

- The removal of many principles which also appear in other TASs
- The move to include explanation as to how to interpret certain generic TAS principles in the context of transformations
- Acceptance that in many cases the focus is only on beneficiaries directly affected by the transformation
- No general requirement to provide an opinion on fairness

### A separate Transformations TAS

We are extremely disappointed that the BAS is still intending to proceed with a separate Transformations TAS, against the overwhelming view of respondents to the consultation. We believe this is a mistake and a missed opportunity, and we press the BAS most strongly to reconsider.

We repeat our view that a separate TAS on transformations is neither helpful nor desirable. We encourage the BAS to listen to the weight of opinion from respondents and to extend the scope and content of the proposed Pensions and Insurance TASs to incorporate the appropriate transformations principles.

The assertion in section 1.5 that a separate TAS is preferable, because this will highlight the focus on beneficiaries that is the essence of transformations, is weak. The proposed Pensions TAS already contains many aspects where there is an important focus on members' benefits and security, and how these may change – see for example C.1.9, C.1.10, C.1.14 and C1.16. It would be natural and more helpful to extend these as appropriate to bring in the transformations principles so all pension matters (and insurance, under its own TAS) are dealt with in the one document.

The fewer TASs a piece of actuarial work is subject to the better. Users are likely to be better served if the regulatory regime remains relatively contained; and, from a practitioner point of view, with around 50 principles or issues to be covered across the generic TASs, it is clear that a tick box mentality is a very real risk. This is likely to become even more the norm when the number of principles increases further, to over 70, once the specific TASs come into effect.

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We understand that the BAS's focus is on users, not practitioners, but we believe that better organised and more easily accessible standards will be to the benefit of all.

While reviewing the draft TAS wording, it became apparent in a number of the draft principles that they sat uneasily in a pension context; maybe they work in the field of insurance. If so, this would give further support to our preference of not having a separate Transformations TAS, but instead combining principles within each of the Pension, and Insurance, TASs.

We would be happy to meet with you to discuss any of the points raised or answer any questions you have on our response.

Yours faithfully

[By email]

Alison Pollock

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## Appendix

### Transformations: Exposure draft – responses to questions

We are answering these questions in the spirit of the consultation, but our answers should not be interpreted as supporting the production of a separate transformations TAS.

The BAS invited views on the following issues:

#### **1. The proposed commencement date of the Transformations TAS**

We are comfortable with the proposed commencement date of 1 October 2011, provided that there is not significant slippage in the publication date of the Transformations TAS, which the BAS intends to issue towards the end of 2010. This timescale gives at least nine months for practitioners to address and implement the TAS, which is helpful, especially since some types of projects in scope for the TAS can be involved and lengthy.

We note from section 5.1 that the BAS intends that GN16 (and other Guidance Notes dealing with transformations) will cease to apply when the Transformations TAS becomes effective. This is inconsistent with the statement in the exposure draft of the Pensions TAS which states that GN16 will cease to apply from the date the Pensions TAS becomes effective, which is proposed to be 1 April 2010.

#### **2. Its impact assessment and the effects that the introduction of the Transformations TAS is likely to have on actuarial information**

Your impact assessment seems principally to consist of assertions that the additional costs of the Transformations TAS will be modest or are justified because of the resulting benefit to users. You do not provide any supporting evidence to back these views.

We agree that the work in scope for the Transformations TAS is important and carries a number of significant risks for decision-makers (trustees etc). We also believe that much work in this area is already done to a high standard. You propose that these factors would together suggest that the additional costs of compliance may not be very significant, and further that they could be outweighed by the benefits to users.



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Whether this is the case or not, and we note that you present no evidence to back your assertions, your chosen route of a separate Transformations TAS maximises the impact and costs on practitioners.

Even where work is already being carried out to a high standard, the need to apply judgement on each principle's applicability, materiality and proportionality (and for this to be done, checked and reviewed as the work goes through its peer review process) means that the impact of having to refer to two separate and quite lengthy documents is potentially more significant than at first might appear.

More specifically, because some of the principles in the Transformations TAS conflict with the responsibilities given to scheme actuaries under legislation and the actuarial profession's guidance, the TAS increases the risk posed by exercises within its scope. For example, as we explained in our response to the earlier consultation, in a bulk transfer, scheme actuaries have a duty to their trustee client, and have no basis for taking the interests of any other party into account (D2.1).

### **3. The text of the exposure draft as a means of implementing the proposals presented in BAS's June 2010 document "Exposure draft: Transformations"**

A.1.2 – The phrase "including information on cash flows, risk and uncertainty" appears prescriptive and we believe that readers (such as scheme members, practitioners and users) will interpret this as mandating this information. We note your comments in paragraph 2.25, but it would be preferable to make this point clearer by adjusting the wording in the TAS itself.

This could be done by using the alternative phrase "including information such as cash flows, risk and uncertainty".

Again the use of "including" in the final bullet point appears to mandate reference to fairness, whereas the main principles of the TAS restrict a consideration of fairness to aggregate reports which opine on fairness. It would be better to reword the final bullet point in A.1.2 to make this clear and consistent throughout.

B.2.1 – "actuarial factor" does not appear to be used in the text of the TAS so the definition is unnecessary. There are several other definitions which similarly appear



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unnecessary. It would keep the TAS to a more manageable length, and help readers, if superfluous definitions were not included.

The definition of “governing body” refers to “pension schemes” and this in turn is defined to include personal pension schemes. It would be helpful if it was made clear whether the BAS does indeed intend for those entities with a degree of responsibility or governance (eg the employer, the product provider) to be included under the definition of “governing bodies”. As we cannot envisage transformations applying to personal pensions, the definition may present no particular issues, but it could bring in scope actuarial advice to the employer on transformations, and we are not sure whether this is the BAS’s intention. We assume this will be changed to be consistent with the definition in the current (3 August 2010) draft Pensions TAS, which is an improvement.

“Neutral measure” is emboldened but not defined as a term; perhaps only “neutral” should be in bold? However, this term is not used in the TAS so the definition is unnecessary here.

“Pension transformation” – we are not sure whether this is intentionally so wide, but as defined it does not appear consistent with the work described in C.1.5 and C.1.6. The reference to “consent of all the members” is problematic. The references in section C are better defined, as they refer to “consents of those members”, making it clear that it is the affected members and whether they consent that is the issue.

C.1.5 – in the context of occupational schemes, this appears to apply to work carried out for the trustees of both the transferring scheme and the receiving scheme. If this was intended, then we have no issues with the wording as it stands, although it might be worth making this even more explicit.

C.1.6 – is it intended that this covers changes to future service benefits which are proposed by the employer? Employers are generally free to make such changes. It would appear to do so, and this makes the definition of governing body key.

C.1.7 – notwithstanding your comments in 2.29 and 2.30 (which we welcome), the reference to “actuarial work” is still too wide-ranging and brings into scope much work which is not transformational.



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There is extreme overlap between the draft Pensions TAS that has been issued for limited consultation and the Transformations TAS (C.1.10, C.1.14 and C.1.15 in the draft Pensions TAS cover the same ground as C.1.5, 6, and 7 of the Transformations TAS). This is unhelpful. In principle, when BAS consults on exposure drafts we understood these are intended to be pretty close to the final product, but it is clear this is not the case with regard to one, or both, of these cases.

D.1.2 – this relates to scope and would seem to fit better in section C on scope.

D.1.3 – this relates to applying judgement on the whole TAS, not just section D, and would seem to fit better in the interpretations section (section B).

D.2.1 – where there is a bulk transfer to another pension scheme, for example, we do not see how a scheme actuary for the transferring scheme can place any emphasis on the interests of the employer in relation to the receiving scheme. You might argue, therefore, that the ‘proper’ emphasis is no emphasis, but in our minds that makes a nonsense of the principle.

D.4.1 – this seems reasonable and we support this principle with the exception of the third bullet point. In a pension context, it appears to require commentary on the change in sponsor covenant, which could be outside the area of expertise of the actuary.

D.4.3 and D.4.4 – because of the definition of ‘beneficiaries’, in the case of transfers, these appear to require the scheme actuary to one scheme to comment on the effects on the beneficiaries in any other scheme affected, which is unreasonable. In any case, once improved, these would be better placed as minor revisions to TAS R rather than including here.

However, we have issues with the wide-ranging nature of the wording of D.4.3 to D.4.5. As drafted, they include risks beyond actuarial ones, and in particular would include comment on employer covenant which is generally outside an actuary’s area of expertise.

D.4.7 – the first bullet is confusingly written (possibly some words have been omitted?) and we are not at all sure what you intend. However it appears to be covering a situation where the actuary is speculating on matters about which he or she has little or no



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knowledge. A better example might be where there is a partial transfer, commenting on the effect not only on those being transferred, but also the remaining members.

D.4.10 – quite apart from being confusingly written, D.4.10 echoes the requirement in D.2.12b) of the (draft) Pensions TAS. Such duplication is unnecessary.

D.4.11 – the suggestion of indicating the “degree of comfort” with giving an actuarial certificate is problematic. If we provide advice or a certificate, our clients assume we are ‘comfortable’ with it. If you mean to require us to indicate the uncertainty associated with the advice or other actuarial information we provide, then this could be expressed better.

D.4.12 – this principle, again, expects scheme actuaries to look at the position of parties about whom they will have no information, and no right to access that information. Also, the phrase “any change in the value of the interests” is not particularly clear, but the illustrations in D.4.13 are helpful in giving some indication as to what you are looking for. However it is not clear to us whether this means a change in the actuarial value of the benefits, or a wider measure such as a change to the conditions of benefit payment.

D.4.14 – this principle, again, expects scheme actuaries to look at the position of parties about whom they will have no information, and no right to access that information. There may be advantages to the party proposing the transformation of which the actuary cannot be aware, or may be unqualified to comment upon (as they fall outside an actuary’s area of expertise). This should be reflected by revised wording. To some extent this is also a problem with the first part of the sentence also; comments on the benefits to be gained by beneficiaries should be limited to those which fall into an actuary’s area of responsibility.

D.4.15 – the first bullet point is problematic because it appears to require commentary on the change in sponsor covenant, which might be outside the area of expertise of the actuary. The second bullet point should be re-thought; what you intend in a pension context is quite unclear to us. (This may be clear in the insurance context.) In any case, although the rules-based financial structures of insurance companies might make it possible to comment on the effects a Part VII transfer, the effect on an employer of a bulk transfer of pension liabilities that is likely to have taken place as part of a company restructuring is unlikely to be within an actuary’s competence.

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**In addition to the specific questions listed above, BAS would welcome respondents' views on any other aspects of the proposed transformations TAS.**

No further comments.

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