



28 January 2008
The Director
Board for Actuarial Standards
5th Floor, Aldwych House
71-91 Aldwych
London
WC2B 4HN

Subject: Consultation Paper

Dear Sir

I am pleased to attach Mercer's response to the consultation paper "Towards a Conceptual Framework".

As noted already, we welcome this document and consider this a significant advance from the preliminary consultation paper. We look forward to seeing the first of the new BAS standards so we can see how the conceptual framework will be applied in practice.

Our answers to the specific question raised in the consultation paper are attached. Our main concerns are that:

- Standards are not unnecessarily restrictive, and
- Actuaries are not disadvantaged relative to other advisers

The consultation document suggests that BAS is sensitive to these concerns.

We are concerned about the growing amount of regulation and guidance, and the consequent risks of over-regulation and conflict. We hope that it will be possible for BAS to coordinate guidance with other bodies such as TPR and maintain a proportionate overall level of regulation. We also trust that BAS will consult openly on proposed guidance and take a balanced view of inputs from stakeholders including actuaries.

Yours sincerely

Phil Turner





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APPENDIX

Response to questions

1 Following the terminology of Section 3, the BAS has determined that Category A should fall within the scope of BAS standards and that Category E should fall outside. In that context:

a) Do respondents consider the five categories drawn up by the BAS (defined in paragraph 3.9) provide a meaningful way to determine which areas of work should be within scope and which should not?

We agree that the five categories provide a meaningful way to determine which areas should be in scope, and believe that the distinction between category A and the remainder is an important concept. The distinctions between the other categories do not seem so significant. We believe that any advice from an actuary should follow actuarial standards or the actuary should explain the reason why it does not.

b) Which, if any, of Categories B, C and D do respondents consider should be within the scope of the framework?

It is reasonable that all categories A-D should fall into the framework. For example, if a generic standard on mortality is developed, this should be considered if work is prepared in any of these categories. In categories B-D, this would be on a "comply or explain" basis. However, developing guidance on category A issues should be given priority over developing other guidance. We suggest that guidance is provided for other categories only when there is a compelling reason for the guidance.

c) The BAS would also welcome feedback, and real examples, indicating whether the non-regulatory element of Category B exists in practice or illustrating any concerns that the definitions are wrongly capturing or omitting areas of work.

An example of work that an entity is required to commission, but not necessarily from an actuary is accounting disclosures. These must be commissioned at each year-end but the accounting standard setters generally avoid requiring that these are prepared by a qualified actuary. The approach BAS suggests for dealing with these kinds of situations sounds reasonable.



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2 The BAS has set out proposals regarding the objectives and characteristics of standards in Section 4. Do respondents agree with them, specifically the proposals:

a) to introduce some generic standards, to provide coherence and consistency across areas of work, in addition to topic-specific standards as is the case now;

Yes, though we believe that great care must be taken to ensure that any requirements are proportionate. If a client telephones an actuary to ask a question, the client would not expect the answer to be preceded by a list of qualifications (although we agree that any substantive advice given verbally should be followed up in writing). Some quite significant advice may be given in this way supported on the back of earlier advice that included all the necessary background material. For example, a pension client may telephone an actuary to ask how the recommended contributions would change if a significant cash injection was made now. This should not generally be the trigger for another full GN9-style report.

b) that standards be principle-based, rather than rule-based; respondents are asked to identify any advantages or disadvantages that they consider may flow from this approach; and

Yes, though this will inevitably lead to requests for further clarification and commercial pressure to provide the most liberal interpretation of standards. We believe that market forces and the profession's ethical guidance will be adequate to counterbalance this pressure.

c) that standards address outputs and responsibilities, as now, with output-based standards focusing on the users of actuarial services and their needs as decision makers?

We have some misgivings that this will inevitably focus on the form the "output" should take which we believe is unnecessarily restrictive. We believe the important requirements are the various factors that should be considered. Writing in the passive form "the assumptions should be derived from..." is generally less clear, but this is more a matter of style than of substance.

We were attracted to the idea that the purpose of advice is to inform the decisions of the recipient and it should be presented in a way that allows this (described to us in a separate meeting). This would be an improvement on the current basis of requiring a detailed report once the major decisions have been made (e.g. GN 9). We use recipient narrowly here to mean the client. We would not expect to constrain advice based on the needs of others.



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3 Do respondents foresee any practical issues or problems that they consider should be addressed in relation to the enforceability of standards, as set out in Section 5, in order to ensure the efficient functioning of the enforceability proposals?

We are concerned that the proposal to allow non-actuaries to assert that their advice complies with BAS standards effectively weakens the position of actuaries relative to other advisors, particularly given the lack of enforcement powers over those advisors. This could be mitigated by including in the document described in paragraph 5.14 a general requirement that an advisor who is not a fellow of the Faculty or Institute of Actuaries should state this clearly in his or her advice. Thus such an advisor could not claim he or she was following BAS standards unless this lack of a UK actuarial professional qualification was noted.

We believe it would also be sensible for the terms of any actuarial engagement to include a requirement for the user of the advice to seek approval of the actuary to any representation of that advice to third parties e.g. if pension scheme trustees write to their members and characterise the advice as “actuarial”.

Paragraph 5.11 notes that the profession has not faced this dilemma previously. In fact, when the Guidance Committee framed GN 34, it was well aware that it might create a situation that would encourage companies to seek advice from experts who were not subject to the guidance. It was also noted that an actuary might not be in overall charge of the work, and that the advice provided to the immediate client might not be passed on to the ultimate recipient (the plan member) unadulterated. This is addressed in paragraph 4.1 of GN 34 “The actuary should use his or her best endeavours to ensure that the illustration is presented to the ultimate recipient in a complete and balanced way.”

We consider that having BAS standards apply only if “an actuary in overall charge of the work” (paragraph 5.17) is not sufficient. The focus should be on any work that is characterised as “actuarial”. However, where a project falls into categories B-D and is not led by an actuary (so cannot be enforced overall), any actuaries involved should behave as though it was enforceable with regard to their role (that is “comply or explain”).



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4 Do respondents agree with the proposals in section 8 for:

a) the general principles set out in paragraph 8.2;

Yes. We agree with the proposal to recognise a range of valuation approaches. The significance of market value is that this is the measure of “value” that the users of actuarial advice most readily understand. It is consequently an important benchmark for other measures of value.

b) the quantification principles set out in paragraphs 8.3-8.30;

Yes - except for the provision of liability cash flows. First of all, it may not be straightforward to calculate such cash flows. For example, the value of post-retirement benefits is typically calculated by applying an annuity factor that incorporates post-retirement increases to the current level of pension. The actual cash flows are not determined. The cash flows can be calculated, but additional work would be required. Secondly, we believe that, in many situations, the provision of cash flows will not help the recipients of actuarial advice. We consequently believe it would be inappropriate to require the calculation of cash flows in all situations where actuarial advice is given.

Rather than focus on “how prudence is to be achieved” (paragraph 8.29), we believe it would be more appropriate for BAS to focus on how prudence should be measured. Value-at-risk is a likely candidate.

c) the generic reporting standard set out in paragraphs 8.31-8.55?

Yes, though as noted in our answer to question 2(a), it is important that any requirement to use a generic reporting standard is proportionate. The key issue is the information which the actuary must provide, not how this is presented.

Section 8.36 talks about estimates for future mortality improvements being based on “the actuary’s own beliefs”. We note that the responsibility for mortality assumptions for both funding and accounting purposes lies with others (the plan trustees and the company directors respectively).



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d) the proposal set out in paragraph 8.48(d) for actuarial quantification of liabilities to include an assessment of the probability that the assets held by the entity at the valuation date will be sufficient to meet those liabilities; respondents are asked to focus, in particular, on:

- any practical problems in assessing the probabilities which the proposal calls for; and*
- any limitations on the usefulness of the information if one or more of the probabilities has to be omitted from the assessment.*

This would be appropriate only if “assets” is interpreted broadly to include assets such as a “company covenant” to its pension plan (unfunded plans have no other assets). Attaching a monetary value to such a covenant is difficult.

More generally, we consider that requiring such an assessment would be unnecessary and inappropriate in many situations where actuarial advice is given.

The information suggested may be of limited use because it will not capture the distribution of probabilities. There may be a high probability that the target is missed by a small amount, but a relatively small probability that it is missed by a lot.

9.2 In addition to the specific questions listed above, the BAS invites respondents’ views on any other issues that may impact on the Conceptual Framework. To ensure that the significance of their point is fully appreciated by the BAS, respondents are encouraged to indicate how their comments affect the proposed Framework.

9.3 In particular, as noted earlier in this paper, the BAS regards Sections 6 and 7 of the Consultation Paper as setting out matters of current and historical fact, together with logical analysis based on those facts, rather than matters of judgment or policy. The BAS would welcome respondents’ feedback on the material set out in those sections if respondents believe any of it to be ill-founded, but asks respondents to take note that the implications for the Conceptual Framework of this material follow in Section 8, which therefore provides a more effective opportunity for making comments.

We have no further comments.