

**To All Members**

December 2005

Dear Member

**GN9: Funding Defined Benefits – Presentation of Actuarial Advice**

**Introduction**

The main purpose of this Guidance Note is to ensure that actuarial advice on the funding of defined benefits is presented with sufficient information to enable the recipient of the advice to understand the expected future course of a scheme's contribution rates and of its solvency level. The guidance does not in itself seek to restrict the choice of funding method and assumptions but seeks to ensure that sufficient explanation is given of the methods and assumptions being proposed or used, including the associated risks and other implications for solvency and contribution rates. It applies to all funding advice (except where methods and assumptions are prescribed) and not just to valuations that are required by legislation. In particular, it should be noted that it applies to advice preceding a formal valuation and advice in between formal valuations.

GN9 needed to be amended to take account of the scheme funding changes that are being introduced by Part 3 of the Pensions Act 2004, along with the associated secondary legislation and Code of Practice from the Pensions Regulator. The opportunity has also been taken to make various other changes, including adjustments and clarifications to the section on solvency that was introduced at the last revision in March 2004. Version 8.0 is therefore substantially different from version 7.0 and consequently no 'track changes' version has been produced. However, a 'track changes' version from EXD55, the exposure draft under which the revised GN was exposed under Due Process, is available.

The revised GN9 comes into force on 30 December 2005. However, version 7.0 may continue to be used in certain circumstances, for example for valuations (and advice relating to such valuations) with effective dates before 22 September 2005.

Attention is also drawn to GN49, a new Guidance Note coming into force at the same time and which deals specifically with the new legislative requirement for trustees to obtain advice from the scheme actuary on certain matters.

**Detail**

A summary of the main changes in version 8.0 of GN9 compared with version 7.0 is as follows:

**Faculty of Actuaries**  
Maclaurin House  
18 Dublin Street  
Edinburgh EH1 3PP  
Tel: +44 (0)131 240 1300  
Fax: +44 (0)131 240 1313  
e-mail: [faculty@actuaries.org.uk](mailto:faculty@actuaries.org.uk)  
[www.actuaries.org.uk](http://www.actuaries.org.uk)

**Institute of Actuaries**  
Staple Inn Hall  
High Holborn  
London WC1V 7QJ  
Tel: +44 (0)20 7632 2100  
Fax: +44 (0)20 7632 2111  
e-mail: [institute@actuaries.org.uk](mailto:institute@actuaries.org.uk)  
[www.actuaries.org.uk](http://www.actuaries.org.uk)

**Institute of Actuaries**  
Napier House  
4 Worcester Street  
Oxford OX1 2AW  
Tel: +44 (0)1865 268200  
Fax: +44 (0)1865 268211  
e-mail: [institute@actuaries.org.uk](mailto:institute@actuaries.org.uk)  
[www.actuaries.org.uk](http://www.actuaries.org.uk)



# The Actuarial Profession

making financial sense of the future

- In keeping with version 7.0, which does not apply to valuations on prescribed actuarial bases, version 8.0 specifically provides that it does not apply to 'entry' or 'levy' valuations required by the Board of the Pension Protection Fund.
- Paragraph 1.8 provides that the GN applies to work carried out in a jurisdiction outside the UK only to the extent required by paragraph 1.10 of the Professional Conduct Standards.
- The new section 2 addresses the presentation of the actuary's advice at any stage in the process when he or she is advising on a funding objective or funding principles, whereas section 3 (which substantially follows the general format of version 7.0) focuses on the report that follows a formal valuation. A key underlying principle of section 2 is that the actuary should ensure that an appropriate level of advice is available sufficiently early in the process on matters such as the susceptibility of results to variations in assumptions and the risks associated with a proposed funding strategy, including in particular the implications of the strategy for the evolving solvency position of the scheme.
- Paragraph 2.2 requires the actuary to make clear which (if any) parts of his or her advice constitute recommendations or determinations under particular powers granted to the actuary in the scheme rules. This paragraph was not explicitly included in EXD55, but the 'Scheme Funding' Regulations have been amended in the meantime with regard to such powers.
- Paragraph 2.4 requires the actuary to consider whether or not there is a significant likelihood that, under a proposed funding objective, there would still be insufficient assets to pay full transfer values even if the funding objective were fully met. This paragraph was not included in EXD55.
- Paragraph 2.7 aims to ensure that funding principles are specified with sufficient clarity, the measure being that two actuaries could be expected to produce valuation results based on these principles that are not materially different (with a similar requirement in 3.4.7 in relation to the description of the method in the valuation report). In response to comments made during the consultation process, this paragraph now makes clear that this does not necessarily mean that all the details have to be included in the trustees' formal Statement of Funding Principles.
- The scope of the items required in the main valuation report (Section 3 of v8.0) has not generally been reduced, even where some of the information may already have been given in detail at an earlier stage of the process. The Board's view (in part, because members do not normally have the automatic right to see advice to the trustees other than the valuation report) is that it is best to ensure that there is one consolidating document with all the relevant advice, and this view was endorsed during the consultation process.

**Faculty of Actuaries**  
Maclaurin House  
18 Dublin Street  
Edinburgh EH1 3PP  
Tel: +44 (0)131 240 1300  
Fax: +44 (0)131 240 1313  
e-mail: [faculty@actuaries.org.uk](mailto:faculty@actuaries.org.uk)  
[www.actuaries.org.uk](http://www.actuaries.org.uk)

**Institute of Actuaries**  
Staple Inn Hall  
High Holborn  
London WC1V 7QJ  
Tel: +44 (0)20 7632 2100  
Fax: +44 (0)20 7632 2111  
e-mail: [institute@actuaries.org.uk](mailto:institute@actuaries.org.uk)  
[www.actuaries.org.uk](http://www.actuaries.org.uk)

**Institute of Actuaries**  
Napier House  
4 Worcester Street  
Oxford OX1 2AW  
Tel: +44 (0)1865 268200  
Fax: +44 (0)1865 268211  
e-mail: [institute@actuaries.org.uk](mailto:institute@actuaries.org.uk)  
[www.actuaries.org.uk](http://www.actuaries.org.uk)



# The Actuarial Profession

making financial sense of the future

- In the light of the roles of the trustees and actuary in determining funding strategy under the Pensions Act 2004 (with the trustees making the decisions, having taken advice from the actuary), various references (in particular, paragraph 3.4.12) in the GN have been amended, in general to drop the concept of a 'recommended contribution rate'.
- Paragraph 3.4.9 has been amended so that the actuary would now have to *comment* on the compatibility of the bases for valuing assets and liabilities, rather than *confirm* their compatibility. This reflects the possibility that the bases may be determined by the trustees, against the advice of the actuary. In such circumstances, as in any other circumstances connected with this Guidance Note where the trustees appear to be disregarding actuarial advice, the actuary would need to consider what further action he or she might take, such as reporting to the Regulator and/or resigning his or her appointment. The Pensions Board is considering changes to GN29 to cover such situations.
- To ensure that these important matters are not overlooked, paragraph 3.4.5 now makes clear that the option to take a transfer value is one of the options that must be considered in terms of a possible effect on the funding or solvency of the scheme, and paragraph 3.4.8 now makes clear that mortality assumptions must be included in the discussion on the sensitivity of results to variations in experience.
- The DWP is introducing its own solvency disclosure requirement (under Regulation 7 of the 'Scheme Funding' Regulations). This estimate of solvency is not necessarily the same as that required under section 3.5 of the Guidance Note, because the Guidance Note is not providing a basis for the purposes of the Regulations. However, the Board has amended the wording in EXD55 in response to a strong desire expressed in the consultation process for any need for 'two solvency disclosures' to be avoided. Paragraph 3.5.2 now allows the *statutory estimate of solvency* to take the place of an estimate in accordance with Section 3.5, subject to adequate disclosure (in broad terms) of any material difference.
- New requirements have been introduced in the Solvency section (3.5) for an explicit statement of the solvency level associated with a 100% funding level on the stated funding objective (3.5.4, and also reflected in 2.3), an explanation of the difference compared with the solvency position at the previous valuation (3.5.14), and a description of the projected evolution of solvency over at least the next three years (3.5.15, and also reflected in 2.3). However, 3.5.15 has been amended compared with EXD55, and now permits less detail to be provided where the actuary considers that the extra information would not be material to the trustees' understanding of the associated risks to members' benefits.
- Various adjustments and clarifications have also been made to the detailed provisions on assessing the solvency value (paragraphs 3.5.5 to 3.5.12). A particular point to note is the last sentence of 3.5.10, on the likely unsuitability of 'gilts – 0.5%' for a scheme with

**Faculty of Actuaries**  
Maclaurin House  
18 Dublin Street  
Edinburgh EH1 3PP  
Tel: +44 (0)131 240 1300  
Fax: +44 (0)131 240 1313  
e-mail: [faculty@actuaries.org.uk](mailto:faculty@actuaries.org.uk)  
[www.actuaries.org.uk](http://www.actuaries.org.uk)

**Institute of Actuaries**  
Staple Inn Hall  
High Holborn  
London WC1V 7QJ  
Tel: +44 (0)20 7632 2100  
Fax: +44 (0)20 7632 2111  
e-mail: [institute@actuaries.org.uk](mailto:institute@actuaries.org.uk)  
[www.actuaries.org.uk](http://www.actuaries.org.uk)

**Institute of Actuaries**  
Napier House  
4 Worcester Street  
Oxford OX1 2AW  
Tel: +44 (0)1865 268200  
Fax: +44 (0)1865 268211  
e-mail: [institute@actuaries.org.uk](mailto:institute@actuaries.org.uk)  
[www.actuaries.org.uk](http://www.actuaries.org.uk)

predominantly deferred pensioner liabilities. A general requirement for disclosure of the basis used for the solvency estimate has also been introduced in paragraph 3.5.11, replacing the 'bits and pieces' of such a requirement that were previously spread around the relevant paragraphs.

- A requirement is included in paragraph 3.5.17 for some comment on the position of the scheme relative to entry conditions for the Pension Protection Fund. (This requirement has been significantly reworded to reflect views expressed during the consultation process.)
- The possibility is acknowledged that at the time the valuation report is issued, there may still be key decisions by the trustees outstanding that will affect the future contribution rates. In the absence of these decisions, certain disclosures in the valuation report may not be possible (e.g. some of those in 3.4.12 to 3.4.15 and 3.5.15 to 3.5.16). These decisions would normally then be implemented through a subsequently drawn up recovery plan and/or schedule of contributions. Paragraph 4.1 then requires the actuary to fill in the gaps when advising the trustees on the recovery plan and/or schedule of contributions, and to point out the implications in terms of disclosure rights of members.
- Paragraph 4.2 seeks to address the issue that extra assumptions (over and above those used at earlier stages of the advice process) may be needed when drawing up a recovery plan.

Other changes of note (not mentioned above) compared with EXD55 are:

- In several places, it has been made clear that whether a matter is 'material' is to be determined by the actuary's opinion in those circumstances (i.e. the actuary does not have to second guess whether or not another person would consider it material).
- Various paragraphs (numbered 2.2, 2.3, 3.4.13 and 4.3 in EXD55) have been deleted – in general, these removals are consequent upon changes made to the legislation or to the Code of Practice.
- Although HMRC maximum contribution calculations are no longer explicitly mentioned in the list of exclusions in the Application section, the removal of this reference is in anticipation of the new pensions tax regime from April 2006 and the Board confirms that GN9 still does not apply to them.

This version of the Guidance Note does not include any guidance on 'actuarial reports' (normally required in years when full valuations are not done) under section 224 of the Act. This is because such reports will in general not be produced until at least September 2006, so the need for guidance on them is not urgent. However, a further revision of the Guidance Note is anticipated in the near

future to cover these reports. Such a revision would also provide an opportunity to adjust any other aspects of the GN where this appears appropriate in the light of early experience of the new scheme funding regime.

You are reminded that a paper entitled 'Estimating the Cost of Securing Benefits with Insurance Companies' has recently been issued and is available on the website at <http://www.actuaries.org.uk/files/pdf/pensions/buyout.pdf>. This paper was the result of research that was commissioned by the Pensions Board prior to the publication of EXD55, and is intended to be useful to actuaries carrying out solvency valuations in accordance with the solvency section of GN9 version 8.0.

Covering letters are only being sent to those members who have requested them. Should you wish to stop receiving these letters in hard copy and receive an e-alert instead, please alter your despatch preferences in the members' only part of the profession's website, or contact the MAP Editor, Sarah Gander ([sarah.gander@actuaries.org.uk](mailto:sarah.gander@actuaries.org.uk)).

A copy of GN9 version 8.0 can be found, from its effective date, on the profession's Website at <http://www.actuaries.org.uk/files/pdf/map/Contents.pdf>  
Or at: [http://www.actuaries.org.uk/Display\\_Page.cgi?url=/pensions/pensions\\_gns.xml](http://www.actuaries.org.uk/Display_Page.cgi?url=/pensions/pensions_gns.xml)

Before the effective date, it can be found at:  
[http://www.actuaries.org.uk/Display\\_Page.cgi?url=/pensions/pensions\\_gns.xml](http://www.actuaries.org.uk/Display_Page.cgi?url=/pensions/pensions_gns.xml)

A copy of version 8.0 of GN9 that tracks the changes which have been made since the Exposure Draft can be found at:  
[http://www.actuaries.org.uk/Display\\_Page.cgi?url=/pensions/pensions\\_gns\\_track.xml](http://www.actuaries.org.uk/Display_Page.cgi?url=/pensions/pensions_gns_track.xml)

Yours sincerely

Wendy M Beaver  
Chairman, Pensions Board