

GN9 : Retirement Benefit Schemes - Actuarial Reports

Classification

Practice standard.

Legislation or Authority

Pensions Act 1995, section 41(1) and (2)(c).

The Occupational Pension Schemes (Minimum Funding Requirement and Actuarial Valuations) Regulations 1996. SI 1996/1536. (Hereinafter called "the Valuation Regulations".)

The Occupational Pension Schemes (Disclosure of Information) Regulations 1996. SI 1996/1655. (Hereinafter called "the Disclosure Regulations".)

Application

Any Actuary responsible for preparing a formal actuarial report on funding (or where funding is covered) when a retirement benefits scheme is set up, or at intervals thereafter when an actuarial valuation is to be prepared

It applies to, but is not limited to, reports on valuations which are required under Section 41(2)(c) of the Pensions Act 1995, and so to the Actuarial Statement required under Regulation 30(7) and Schedule 6 to the Valuation Regulations.

In relation to defined contribution schemes and to small self-administered schemes, this Guidance Note should apply if the advice given is on the funding required to meet a level of benefit (other than lump sum death benefits) or on the benefits the funds will support, but not otherwise.

Version 5.1 can be followed for valuations with effective dates before 1 August 1997 and this should be indicated in the report.

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Status

Approved under Due Process.

<i>Version</i>	<i>Effective from</i>
1.0	01.04.84
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3.0	01.04.88
3.1	01.09.90
4.0	29.09.92
5.0	01.03.93
5.1	01.06.94
6.0	01.08.97

1 Introduction

- 1.1 This Guidance Note applies to all formal actuarial valuation reports which are required by the scheme governing documentation or by legislation or are specifically requested by the actuary's client.
- 1.2 In the case of schemes to which MFR legislation applies, regulation 30 of the Valuation Regulations sets forth the time limits attaching to the effective dates of valuations and to the passing of the reports to the actuary's clients. The actuary is encouraged to remind the trustees or managers appropriately when valuations are due, and should comply with the legislation over production of the report.
- 1.3 In the case of other schemes, and notwithstanding any longer intervals permitted by the scheme documentation, the actuary should encourage trustees or managers to have valuations made at appropriate intervals.
- 1.4 Generally the report should be in the hands of the actuary's client within one year of its effective date.
- 1.5 Where an event occurs which under the Trust Deed and Rules commences a discontinuance procedure, this Guidance Note continues to apply and the actuary should consider whether it would be appropriate to advise the trustees that an actuarial valuation should be carried out.

2 Purpose of the Guidance

- 2.1 The purpose of the Guidance Note is to ensure that reports contain sufficient information to enable the current funding level of a scheme to be understood and also, in the case of a defined benefit scheme, to enable the expected future course of a scheme's contribution rates to be understood. It is not intended to restrict the actuary's freedom of judgement in choosing the method of valuation and the underlying assumptions.
- 2.2 Although any report will be addressed to the actuary's client (normally the trustees but in some circumstances the employer) the actuary needs to bear in mind that the advice may be made available to third parties who can reasonably be expected to rely on it. In connection with actuarial reports required under the Pensions Act, Regulation 7 of the Disclosure Regulations specifies third parties including statutory bodies to whom trustees must make reports available.

3 The Report

3.1 Introduction

- 3.1.1 The items in 3.2 to 3.11 below, except where otherwise indicated, are normally regarded as essential components of a report. Other information may often be desirable and suitable explanations of some features may be very important, for example the effect on the funding level of an improvement in benefits with retroactive effect.
- 3.1.2 The report should be in writing. Should a preliminary report be issued not including all the components listed below, in the expectation that a further and full report will be made, it must be made clear in the preliminary report that it does not conform to GN9 but that the further report will do so.
- 3.1.3 A report on a scheme subject to the Minimum Funding Requirement may incorporate the actuary's statement (prepared in accordance with Guidance Note GN27) on that Requirement if it is appropriate to do so, i.e. the prescribed calculations have been made by the appointed Scheme Actuary and the report is addressed to the trustees. Care should, however, be taken that the results of calculations with different objectives are clearly identified.

3.2 Basic Information

- 3.2.1 The report should make it clear to whom it is directed, by specifying the client. This will normally be the trustees of a trust-based scheme but in some circumstances will be the employer or both, jointly. An opening statement should state the purpose for which the valuation is made and the dates as at which the current valuation and, if applicable, the immediately preceding valuation were conducted.
- 3.2.2 It is desirable that the opening statement should also refer to the appropriate sections of the legal documentation of a scheme under which the valuation is being made.
- 3.2.3 The report should include a statement of the benefits which have been valued (for example, by a summary of the terms of a scheme or by reference to appropriate documents). Reference should be made to the extent to which allowance has been made for discretionary increases in benefit (and the recent practice in granting such increases) or discretionary benefits.
- 3.2.4 The report should include a brief but clear description of the membership and financial data on which the investigation is based, including a description of the assets. If the actuary has relied on information or opinions provided by others, he should carry out appropriate investigations to assess the accuracy and reasonableness of the data being used. If the actuary has any reservations as to the reliability of the data, such explanation or qualification as appropriate

should be given. In particular, if audited accounts as at the date of valuation are not available, this fact should be stated.

3.2.5 Reference should also be made to any insurance arrangements in place for the benefit of the scheme or any insolvency insurance. This would include, for example, group life assurance held by trustees.

3.2.6 In the case of a scheme in discontinuance, there should be a statement of when benefits ceased to accrue.

3.3 **Inter-valuation Period**

3.3.1 The report should include a statement of the rates of contribution due during the inter-valuation period; and a commentary on any material developments in the scheme during that period, and on any significant variations in experience from the assumptions made at the previous valuation.

3.3.2 In the case of a defined contribution scheme, there need only be a statement of the rates of contributions due.

3.4 **Funding Objectives**

3.4.1 In the case of a defined benefit scheme, the report should explain the funding objectives and the method being employed to achieve those objectives. A statement should be made as to the extent to which there have been changes in the objectives or the method since the last report of a similar nature. Implications in terms of stability of contribution rates and of future funding levels should be explained. If the scheme is subject to the Minimum Funding Requirement, comment should be made on the difference from the objectives of that requirement.

3.5 **Valuation Assumptions and Methods**

3.5.1 The report should contain a statement of both the demographic and economic assumptions made, explicitly or implicitly, in valuing both the liabilities and the assets and, in the case of a defined benefit scheme, the method employed in deriving the contribution rate in paragraph 3.6.1 below. Attention should be directed particularly to those assumptions to which the contribution rate is sensitive. A statement should be made as to the extent to which there have been changes to the assumptions used since the last report of a similar nature.

3.5.2 Where appropriate, the report should state whether and in what way future entrants have been taken into account in the valuation.

3.5.3 The report should comment on the compatibility of the basis of valuing the assets with that of valuing the liabilities. The actuary should also comment on any notable or particular risks in the investment strategy of a scheme relative to the form and incidence of the liabilities. The actuary is encouraged to comment on the sensitivity of the funding to future investment market changes.

Where relevant, attention should be drawn to such aspects as concentration of assets, levels of self-investment, and currency mismatching. If the assets include derivatives, the actuary should consider the requirements of GN25.

3.6 Contribution Rate

- 3.6.1 In the case of a defined benefit scheme, the report should recommend appropriate contributions consistent with the funding objectives for the period until the next anticipated formal actuarial valuation. If appropriate, the actuary may recommend different contribution rates for different groups of members, or different contribution rates payable for different intervals in the period to such a valuation. Alternatively, if the contribution rate is determined elsewhere, e.g. in governing documentation, so that a recommendation by the actuary is inappropriate, the report should include comment on the adequacy of the rate.
- 3.6.2 The report should also address the issue of the expected future course of a scheme's contribution rates in the longer term on current methodology and assumptions.

3.7 Minimum Funding Requirement

- 3.7.1 In the case of a scheme subject to the Minimum Funding Requirement, the Minimum Funding Requirement funding level as given in the most recent statement should be stated with appropriate explanation.

3.8 Current Funding Level - Discontinuance Assumption

- 3.8.1 The purpose of the statement on this subject is to give an indication of the accrued solvency position of a scheme in discontinuance or were the scheme to become a scheme in discontinuance at the valuation date and, in particular, if there were no further contributions due from the scheme sponsor. The actuary should adopt an approach with that principle in mind.
- 3.8.2 The report should state whether or not, in the actuary's opinion, the assets would have been sufficient at the valuation date to cover liabilities arising (including any dependants' contingent benefits) in respect of pensions in payment, preserved benefits for members whose pensionable service has ceased and accrued benefits for members in pensionable service, the last of which will normally be related to pensionable service to, and pensionable earnings at, the date of valuation including revaluation on the statutory basis (or on such higher basis as has been promised). The accrued benefits of all active service members should be included irrespective of the preservation legislation. If the assets were not sufficient, the report should indicate the level of coverage.
- 3.8.3 If the scheme is not already in discontinuance, the actuary must make a judgement as to whether, in the event of contributions from a scheme sponsor terminating, a wind-up would be likely in the short term. If a wind-up were

likely, the statement should be based on assets valued at market value and liabilities in respect of active service members and deferred members either as cash equivalents or as an estimate of the cost of deferred annuities or as a combination of both. For pensioners (and contingent pensioners) an estimate of the cost of immediate annuities will normally be appropriate. A reminder should be given that market conditions change. If a wind-up were not likely, a closed fund approach should be adopted. The report should state whether a closed fund approach or a wind-up approach has been adopted. If a wind-up approach has been adopted, the report should also state whether liabilities in respect of active service members and deferred members have been valued as a cash equivalent or as an estimate of the cost of deferred annuities, or as a specified combination of both.

- 3.8.4 Provision for future expenses should be made. The provision should be appropriate to the approach adopted under 3.8.3 above. The report should give the basis of the provision and point out that it is a provision, not an estimate or quotation.
- 3.8.5 Where appropriate, having regard to the approach adopted under 3.8.3, it should be pointed out that the value of the liabilities may not represent the cost required to secure the liabilities of a scheme were a scheme to wind-up as at the date of the valuation.
- 3.8.6 The report should include a description of the consequences (without necessarily quantifying) of the priority clause in the Trust Deed and Rules as overridden by the Pensions Act 1995 and regulations.

3.9 **Current Funding Level - On-going Assumption**

- 3.9.1 If the scheme is not already in discontinuance, the report should include a statement as to the funding position on the assumption that both scheme and the scheme sponsor(s) are on-going. The statement should include, where relevant, a comparison between assets and accrued liabilities, the latter with pensionable salaries projected where appropriate to assumed end of pensionable service, if this is not otherwise conveyed by the comments on the funding objectives and the contribution rate.

3.10 **Reconciliation**

- 3.10.1 A reconciliation of the valuation should be made with the position disclosed by the previous valuation, and a statement included in the report quantifying the financially material items of actuarial gain or loss, including changes in the valuation method and of the valuation assumptions.

3.11 **General**

- 3.11.1 A statement should be made in the report whether the valuation has been prepared in accordance with GN9 current at the effective date of the valuation report.

- 3.11.2 There should be a statement indicating any departures from GN9. The actuary is expected to comply with GN9, unless the actuary is convinced that full compliance would be inappropriate, in which case a complete explanation and justification of all departures should be given.

4 The Actuarial Statement

- 4.1 This section relates only to the Actuarial Statement required under regulation 30(7) and Schedule 6 to the Valuation Regulations.
- 4.2 A Statement will normally follow a formal valuation to which the earlier parts of this Guidance Note apply. A revised statement can, however, be issued at any time.
- 4.3 Section 1 of the Statement requires an opinion from the actuary on the adequacy of the resources of a scheme 'in the normal course of events'. In interpreting this expression at the date of each Statement, the actuary should take a prudent view of the future without taking into account every conceivable unfavourable development. The actuary should regard this as excluding the possibilities of events - including those external to a scheme - which cannot reasonably be expected to have been allowed for in a conservative approach to the matter. The actuary will not generally need to give a negative or qualified opinion provided that the contribution rate specified reflects that referred to in 3.6.1 above and provided that any Statement under 3.9.1 does not indicate cause for concern. If a negative or qualified opinion is given, attention should be drawn to the relevant sections of the latest valuation report.
- 4.4 For the purpose of Section 2 of the Statement, use may be made of the names of commonly used valuation methods in GN26: *Pension Fund Terminology*. It is sufficient to describe the *key* funding assumptions; these are not necessarily limited to the financial assumptions. Readers should be referred to the latest valuation report for fuller details.
- 4.5 Care should be taken to avoid confusion between MFR liabilities, liabilities on an ongoing valuation basis and discontinuance liabilities.
- 4.6 If the Statement has been based on data (either in respect of assets or liabilities) which the actuary considers to be unreliable, mention should be made of the actuary's reservations. Particular reference should be made if the statement is not based on audited accounts.
- 4.7 Regulation 30 refers to the issue of a revised Statement during the inter-valuation period. This is not designed to require the actuary to monitor the situation continuously; however, if he or she is made aware or becomes aware of developments which materially affect the continuing validity of the latest Statement, then a revised Statement should be prepared and issued under Regulation 30.