The Actuarial Profession
making financial sense of the future

Mr Mark Heholt
Private Pensions Centre (Design Division)
Department for Work and Pensions
Room 312, The Adelphi
1-11 John Adam Street
London WC2N 6HT

28 February, 2003

Dear Mark

Review of the MFR basis

As part of its role in continually reviewing the actuarial basis for the Minimum Funding Requirement (MFR) the Pensions Board has been considering the changes that should be made to the MFR to ensure that its strength under current economic conditions remains consistent with the original intentions of the MFR when it was introduced in 1997.

We last proposed amendments in September 2001 and in the following February the Government approved a change to the basis in GN27. The main driver for recommending a weakening of the MFR at this time was a reduced level of the non-payment of dividends. The extent of this weakening was, however, mollified by an allowance for improvements in mortality. Since then, MFR has weakened substantially. This is mainly as a result of falling stock markets. We believe that further changes are now needed if the Government wishes to align the MFR more closely to the level of protection originally envisaged. The strength of the MFR is a decision for Government. Should a change to MFR be required we would amend GN27 following agreement by the Secretary of State.

We are aware of the Government's proposals for replacing the MFR. We recognise that this will require primary legislation and will inevitably take some time. Our advice is that retaining the MFR at its current strength in the meantime would represent materially less security of members' benefits, especially where schemes are funded at the MFR minimum level, compared with the security implicit in the MFR when it was originally introduced. We do recognise that if the MFR is strengthened, additional cost burdens will be imposed on sponsoring employers.

When Janet Hill and Hilary Reynolds attended the Pensions Board meeting earlier this month, we gave them a draft of an article we will publishing in the March edition of *The Actuary*. The purpose of this article is not to offer any comment on whether the current MFR is too weak, but rather to consider what the original objectives of MFR were and what MFR would look like if it were being set to meet these objectives in current economic conditions. However it does contain some salutary messages and shows that for many schemes the current MFR may well not be suitable for funding. We have already taken steps within the profession to address the transfer value issue. Changes to the MFR basis do, of course, require approval by the Government.

We would be pleased to meet to discuss this further.

As before, we shall, in due course, be informing our members that we have made this proposal.

Yours sincerely

Ronald Bowie
Chairman
Pensions Board