

The Actuarial Profession

making financial sense of the future

Setting valuation bases

Putting the latest thinking into practice

Martyn Atkinson & Phil Turner

Mercer Human Resource Consulting

30 December 2005

Discuss project plan

2

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Action plan for 31 March 2006
actuarial valuation

Task	Deadline
1. Discuss plan with actuary and company	30 December 2005
2. Agree plan with actuary and company	3 March 2006
3. Actuarial advice on methods, assumptions, and SFP	28 April
4. Agree methods etc with company	26 May
5. Provide member data to actuary	26 May
6. Draft valuation results	25 August

3

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Action plan for 31 March 2006 actuarial valuation (continued)

Task	Deadline
7. (Actuarial advice on recovery plan)	25 August 2006
8. (Draft recovery plan)	1 September
9. Draft schedule of contributions	1 September
10. Agree with company	29 September
11. (Redo until agreement reached)	22 December

4

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Action plan for 31 March 2006 actuarial valuation (continued)

Task	Deadline
12. (Actuarial advice on accrual cutback)	5 January 2007
13. (Agree with company)	2 February
14. (Start consultation with members)	23 February
15. (Complete consultation with members)	25 May
16. (Amend benefit accrual)	15 June

5

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Action plan for 31 March 2006 actuarial valuation (continued)

Task	Deadline
17. Finalise all documents	29 June 2007
18. (Notify TPR of failure to agree)	21 July
19. (Notify member of accrual cutbacks)	13 July

6

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28 April 2006

**Actuarial advice on methods,
assumptions and statement of
funding principles**

7

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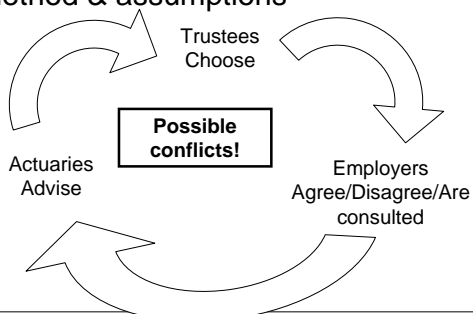
**Solvency target
Impact on member benefits**

Overall solvency target	Pension	Increase	Overall
Pensioners			
70%	79%	16%	66%
80%	90%	18%	76%
90%	100%	27%	85%
Non-pensioners			
70%	79%	55%	74%
80%	90%	63%	85%
90%	100%	73%	95%

8

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**Technical provisions – actuarial
method & assumptions**



9

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Actuarial methods

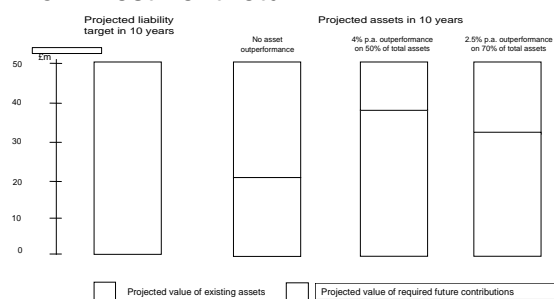
Must be an “accrued benefits” method:

- Projected unit
- Current unit
- Partly-projected unit
- Defined accrued benefit

10

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Projected liability met by contributions or investment return



11

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Anticipated investment policy

Strength of company covenant	Solvency level		
	> 100%	75%-100%	<75%
Strong	Aggressive		Moderate
Average		Moderate	
Weak	Moderate		Low risk

1. Aggressive = high equity content / low risk = high bond content
2. What the Trustees would allow not what they would choose!

12

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Actuarial assumptions

Technical provisions

	Current best estimate	Technical provisions
Investment return	6.6%	5.4%
Salary growth	4.9%	4.9%
Pension increases	2.9%	2.9%

Best estimates

1. Investment return – asset class building block approach
2. Salary growth – implied inflation + 2%
3. Pension increases – implied inflation

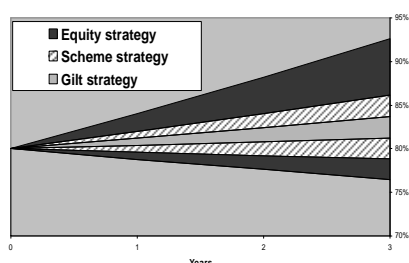
Technical provisions – gilt yield + 0.9%

13

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Solvency target

Range of likely outcomes



14

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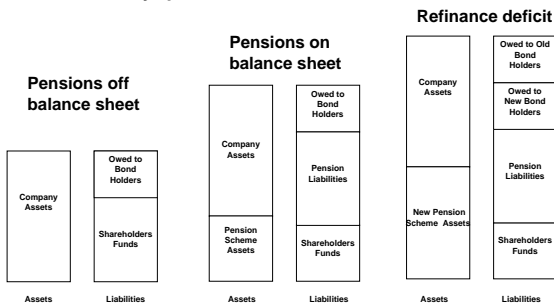
Mortality

- People are living longer
- Our valuation makes an allowance for this
- Recent studies suggest:
 - The allowance is too small
 - Significant variation by industry and location
- New best estimate takes these into account
- Adds 10% to liabilities

15

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Recovery plan - fund now?



16

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Recovery plan – fund later?

What contributions can the employer's cashflow support?

Does the balance sheet cover the wind-up debt?

What is the employer's general attitude to supporting the pension scheme?

Can we learn anything from rating agencies/ forensic accountants?

17

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Recovery plan Employer cash flow

Operating cash flow/net deficit

Company	2.1
FTSE 350:	
25 th percentile	1.1
Median	2.8
75 th percentile	6.2

How might cash flow change in difficult trading conditions?

18

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Recovery plan
Balance sheet position

Pension deficit vs shareholder equity

Company	2.5%
FTSE 350:	
25 th percentile	21.7%
Median	7.8%
75 th percentile	2.1%

19

Recovery plan
Suggested spread periods

Strength of covenant	Spread period (years)
Strong	10 – 15
Average	5 – 10
Weak	2 - 5

Recovery plan and disclosure items will go to TPR for “risk” screening

20

Statement of Funding Principles

<ul style="list-style-type: none">• Trustees Policy for securing SFO• Record of all funding decisions• Any supplementary funding objective	<ul style="list-style-type: none">• Other contributors• Refund to employer• Discretionary Powers and policy	<ul style="list-style-type: none">• Approach to CETVs• Calculation and underfunding
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21

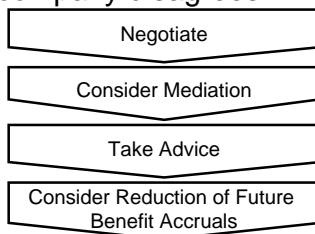
Statement of Funding Principles

- Trustees Policy for securing SFO
- Record of all funding decisions
- Any supplementary funding objective
- Other contributors
- Refund to employer
- Discretionary Powers and policy
- Approach to CETVs
- Calculation and underfunding
- Frequency of actuarial valuations
- Triggers for more frequent actuarial valuations
- Directions by the Regulator
 - Technical Provisions
 - Recovery Plans

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If the company disagrees?



If all else fails...
report to the Regulator within 15 months
plus 5 working days of effective date

23

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25 August 2006

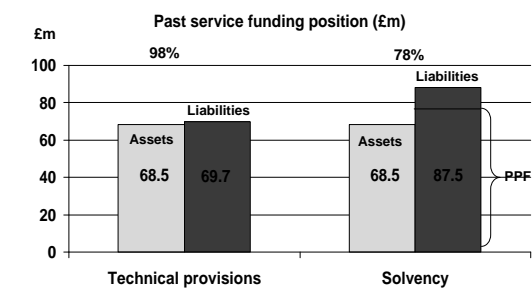
**Draft actuarial valuation results,
recovery plan, and
schedule of contributions**

24

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Results

Technical provisions & solvency

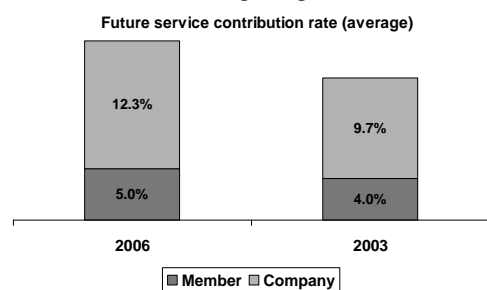


25

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Results

Future service - ongoing



26

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Results

Spreading the past service shortfall

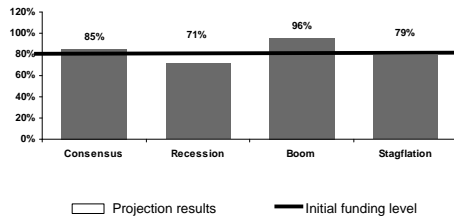
Years	% of Pensionable Pay	First year extra contribution £K pa
5	1.2	187
10	0.8	125
15	0.5	78

27

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Future variability

Solvency level in 3 years' time



28

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29 June 2007

Formal actuarial valuation
results and other
documentation

29

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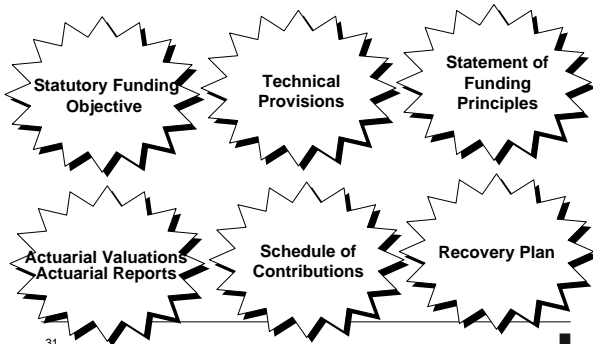
6 June 2005

Formal documentation and
key issues

30

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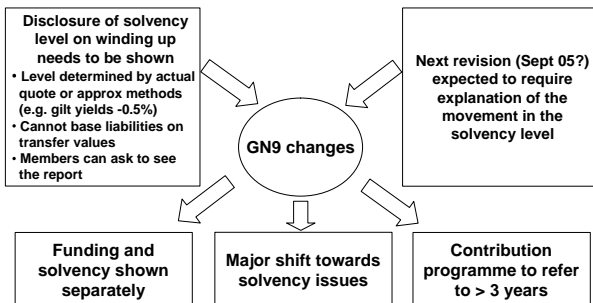
The key valuation items



31

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GN9 changes



32

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Actuarial valuations

Must include the actuary's certification of the calculation of technical provisions

Must include the actuary's estimate of the solvency position

Triennial valuations still allowed

Time limit 15 months from effective date (for all valuation items)

33

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Actuarial reports

Need annually if actuarial valuations are not annual

Small schemes exempt (fewer than 100 members)

Update on technical provisions

Update on assets

Report on changes in "risk"

34

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Key issues

Educating clients

Interpreting prudence

Forming a view on employer covenant

Importing these principles into current funding advice

35

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Questions



36

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