The Actuarial Profession
making financial sense of the future

Exposure Draft response

Board for Actuarial Standards

EXPOSURE DRAFT: PENSIONS

May 2010

About The Actuarial Profession

The Actuarial Profession is governed jointly by the Faculty of Actuaries in Edinburgh and the Institute of Actuaries in London, the two professional bodies for actuaries in the United Kingdom. A rigorous examination system is supported by a programme of continuing professional development and a professional code of conduct supports high standards reflecting the significant role of the Profession in society.

Actuaries' training is founded on mathematical and statistical techniques used in insurance, pension fund management and investment and then builds the management skills associated with the application of these techniques. The training includes the derivation and application of 'mortality tables' used to assess probabilities of death or survival. It also includes the financial mathematics of interest and risk associated with different investment vehicles – from simple deposits through to complex stock market derivatives.

Actuaries provide commercial, financial and prudential advice on the management of a business's assets and liabilities, especially where long term management and planning are critical to the success of any business venture. A majority of actuaries work for insurance companies or pension funds – either as their direct employees or in firms which undertake work on a consultancy basis – but they also advise individuals, and advise on social and public interest issues. Members of the Profession have a statutory role in the supervision of pension funds and life insurance companies as well as a statutory role to provide actuarial opinions for managing agents at Lloyd's.

The Profession also has an obligation to serve the public interest and one method by which it seeks to do so is by making informed contributions to debates on matters of public interest.

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21 May 2010

The Director
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Dear Sir/Madam,

Response from the Actuarial Profession to the BAS *Exposure Draft: Pensions*

Thank you for providing the Actuarial Profession with the opportunity to comment on this Exposure Draft. We offer a few general comments in the covering letter and a number of more detailed comments in the accompanying appendix.

The failure to define 'actuarial work' and 'actuarial information' continues to cause difficulties and ambiguity in interpretation. We do not accept the assertion in 4.14 of the Analysis of Responses that there is a clear consensus amongst actuaries and users as to what is and is not actuarial work and actuarial information. Indeed, many users would probably say that they regard anything done by actuaries as actuarial work. This means that Part C needs to be much clearer about what is and is not within scope. 4.14 of the Analysis of Responses also asserts that the detailed descriptions in Part C of work which will be in scope will help practitioners decide whether work is within scope or not. However, to help clarify a boundary by giving examples, it is necessary to give examples which lie both sides of the boundary. It is noticeable that Part C only describes work which is within scope, and does not give examples of work which is out of scope, leaving the position very unclear.

We consider that the term 'funded defined benefit pension scheme' should be defined explicitly. It would also help to differentiate between DB schemes and DB elements of a hybrid scheme. Currently there appears to be the potential for anomalies whereby DB benefits in a pure DB scheme are treated differently to DB elements in a hybrid scheme (depending on the definitions). The same need for differentiation also applies to pure DC schemes and DC benefits in a hybrid scheme.

It would be clearer to the reader if the use of 'might', 'shall' and 'will' is consistent throughout the document. Some examples of paragraphs using different terms are D.3.3 to 3.7, E.2.2, E.3.5 to E.3.7.

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We believe that, as drafted in D.5.2 to 5.4, there is a severe risk of confusion between what is 'material' for the purpose of this TAS (as defined in B.2.) and what is 'material' for the audit in question. It is not clear which of the references to 'material', 'materiality' and 'materially' refers to which definition.

The inclusion in paragraph E.5.8 of information on cash flows is a new requirement compared to GN9 and appears to be more information than is required elsewhere in the Pensions Exposure Draft. Is this your intention?

If you have any questions or would like to discuss any of these matters further, please do not hesitate to contact us. Should you wish to do so, please contact Martin Hewitt, Pensions Practice Manager on 0207 632 2185 or via Martin.Hewitt@actuaries.org.uk

Yours sincerely,

Robert Hails
Chairman, Consultations Group of the Pensions Practice Executive Committee

APPENDIX

	para	comments
1.	B.2.1	Please consider: • tightening up the definition of funding assessment • the definition of 'neutral', which should be consistent with the TAS M definition • regarding 'neutral measure', we understand the concept of neutral assumptions being used to derive a neutral estimate of a specified measure (e.g. a neutral estimate of the assets required to pay the benefits based on best estimate investment returns, or a neutral estimate of the buy-out cost, or a neutral estimate of technical provisions such that the probability of assets equal to the value of technical provisions would have an agreed probability of being sufficient to meet the benefits) but do not believe that there is such a thing as a neutral measure
2.	C.1.7	Please clarify what kind of investment advice is being referred to regarding 'actuarial work concerning contribution requirements or funding levels that is provided to support a governing body of a funded defined benefit pension scheme in making decisions on investment strategy'. Would Asset/Liability Modelling be covered here if it included projections of expected funding levels (or probability distributions of funding levels)? Is this para consistent with BAS' intention not to cover investment work?
3.	C.1.13	It appears that the intention is that advice to trustees regarding bulk transfers is within scope of this section but that advice to employers would not. However, how does the reference to a 'governing body' apply in the context of a local government governing body outsourcing services, where the body is both the employer undertaking the commercial negotiation and then the administering authority of the scheme? 'Bulk transfer' is not defined and the current wording of C.1.13 appears to cover transfers both without *and* with consent, but only if more than one member is involved. Is this the intention?
4.	C.1.15	Please clarify what is meant by 'actuarial work for a scheme that concerns winding up'. For example would it include enhanced transfers and/or discussions about alternatives to wind-up and/or Asset/Liability Modelling work which includes projections of funding levels on a discontinuance basis (assuming this is not already covered under C1.7) or is the intention to limit coverage to schemes that have commenced winding-up? If this is a matter of professional judgement, is it appropriate that work in-scope should have to rely on judgement?
5.	C.1.19	To avoid excluding DC projections for hybrid schemes (including AVC schemes), we suggest tightening up the wording for 'defined contribution pension schemes' using

		one of the following: • leave as is, but recognise that the paragraph has limited scope • replace ‘defined contribution pension schemes’ with ‘DC elements of pension schemes’ Also, the use of the term ‘other rules’ may be unintentionally vague. Does this, for example, include scheme rules?
6.	C 1.21	Might this paragraph be taken as discouraging the provision of projections on different assumptions, for example alongside an SMPI to demonstrate uncertainty? Such discouragement may not be in the best interest of the recipient.
7.	C.1.22	Clearly, advising on assumptions or calculating defined benefit obligations for a UK pension scheme by a UK actuary would be in scope. Presumably, so would similar work in relation to a non-UK scheme (for a company which reports in to a UK parent), even if performed by that actuary overseas for the non-UK sponsor. However, it is not clear what obligations this paragraph imposes on a UK actuary consolidating disclosures produced for a number of global pension schemes. For the schemes where the work was not done by a UK actuary, is the UK consolidating actuary required to fill in any gaps to make the whole work in relation to those schemes comply with UK Technical Actuarial Standards, or can the UK consolidating actuary take the work for those schemes as an input, with no need to consider the degree of compliance with TASs of the underlying work done in respect of those schemes?
8.	D.1.3	This paragraph seems to rather materially understate the number of areas on which judgement may be required. Why single out this one? Would this para be best placed in Section A as a new A.1.3?
9.	2.10	Do the requirements apply to the assumptions proposed by the actuary or the actual assumptions finally selected by the governing body? In cases where the assumptions are determined by the governing body, that body might choose different assumptions for various reasons without the scheme actuary understanding why. Therefore the actuary may not be in a position for example to explain the trustees’ underlying rationale.
10.	2.12 & 2.16	The phrase ‘….used in, or proposed for use in…’ is used in both paragraphs – this may relate back to paragraph 2.10 but could lead to confusing interpretation where changes in assumptions have been made as the discussions have evolved.
11.	D.2.17	We would comment that ‘future changes’ may in practice incorporate some element of the past too (as the base rate may not be for the current year). Could the wording be a little wider to accommodate this?
12.	D.2.18	In some cases, it may also be appropriate for assumptions to reflect *anticipated* membership.
13.	D.3.1	The obvious inclusion here is UK Government (e.g. with respect to GMP equalisation). Might this paragraph be phrased too widely?

14.	D.3.5	Please clarify the meaning of 'overriding legislation', given that there are different types of legislation affecting pensions work, and that some types can override scheme arrangements whilst others require adjustments to arrangements.
15.	D.3.7	Suggest using 'may' in place of 'might need to' to avoid possible tension implied between what the client needs and what the actuary can deliver.
16.	D.4.1 to 4.2	For good reasons, the instructions may have been simplified, with the result that following the instructions correctly gives an answer that is approximate rather than exactly equal to the theoretically correct amount (whilst still being fit for purpose). We therefore suggest making clear that the requirement here is for the instructions to be sufficiently clear that the instructions can be followed as intended (and that there is no requirement that following the instructions gives exactly the theoretically correct answer). Also, please consider if this principle concerning instructions to third parties is a subordinate part of 'D.4 Calculations of payments to members' OR if it is better placed as a standalone principle in its own right. The second option would have implications for the existing structure of the Exposure Draft and its subsequent numbering.
17.	D.5.2	Please clarify what actuaries should do if the auditor fails to provide a materiality limit? Should they accept the lack of a limit or impose their own limit on work for accounting purposes? Should there be a further principle governing a situation where a materiality limit is not available? Our understanding is that for audits of larger companies, there is a hierarchy of thresholds relating to the escalation of issues upwards through the audit team, and that these thresholds are applied across groups of issues rather than item by item, none of which is captured by the simple reference here to 'materiality levels'.
18.	D.5.4	As this para refers to generic TASs and not exclusively to pensions, and adds nothing to the generic requirement, we suggest deleting it.
19.	E.3.4 to E.3.5	In the light of 3.7 and of Appendix A to the Conceptual Framework, is it intentional that the word 'method' in 'funding method' is shown in bold implying that it is used as defined in B.2.?
20.	E.5	This material is instructional in tone and may not fit appropriately into a principles-based TAS. Also, as drafted, none of the items would inform the decision for a user, so would not be 'material' as defined in B.2., so could be omitted without breaching the requirements of the TAS, so the inclusion of this material in the TAS appears not to succeed in its purpose. An alternative approach would be for the requirements to be covered in the disclosure regulations. We note in passing that the material is more similar in style to TM1, and that something like a 'TM2' may be a more appropriate vehicle for these requirements.
21.	E.5.3	Is this para necessary given the BAS' definition of 'informed reader'?

22.	E.5.5 - 5.7	Small insured schemes might not have a 'stated investment strategy'; they are not required to produce SIPs. E.5.5 – 5.7 do not cover the eventuality that there is no previous scheme funding assessment. Is the scheme actuary expected to exercise judgement on this point or should it be covered explicitly?
23.	E.6	There may be complication and unnecessary confusion if, for example, there has been a change to mortality assumptions since the previous AVR (two years ago perhaps), resulting in the current best estimate mortality assumption being stronger than the previous AVR 'prudent' (at that time) mortality assumption. More importantly, however, we do not see the proposed requirements adding much from the client's point of view. There is some sympathy for the trustees to see how prudent their AVR assumptions are versus best estimate (however described), but there appears little to be gained by tying the best estimate assumptions to the previous (or current?) AVR assumptions
24.	E.6.2	What is the purpose of the comparison? What methods of comparisons should be used? It is also not clear which Scheme Funding assessment is intended to be in 'a Scheme Funding assessment' e.g. the most recently completed scheme funding valuation or a more historic one or, if appropriate, one currently being prepared? The aim is presumably to give the trustees an idea of the effect that their chosen CETV basis could have on the funding position. However, this seems to be another attempt to require the 'rational reconciliation' that TPR tried to introduce into their 2008 transfer value guidance. After receiving comments that initiative was eventually simplified in para 23 of their guidance to a suggestion that the trustees 'consider how the two bases relate to each other'. Something similar would be appropriate here, since the trustees may want to know how the results (for different profiles) compare, but not necessarily how the underlying assumptions compare. Materiality must also be a factor if transfers out are insignificant to the scheme as a whole.