The Actuarial Profession
making financial sense of the future

Ms C Mo
Pension Protection Fund
Knollys House
17 Addiscombe Road
Croydon
CR0 6SR

8 November 2010

Dear Ms Mo,

2011/12 Pension Protection Levy Consultation – September 2010

We welcome the opportunity to respond to the above consultation and thank you for allowing us a few extra days to finalise our submission. We focus our comments on our main area of concern: bulk transfers.

Whilst the proposals are in line with those that applied in the last two years, we nevertheless have major concerns, as we commented last year, over the continuation of the approach into future years. Our concerns are summarised below.

- The PPF in effect requires full s179 valuations of the transferring and receiving schemes, not just of the liabilities transferred – which imposes a disproportionate burden on the schemes involved.
- Worse, depending on when in the year the transfer occurs, the valuation may be required over a very short timescale which may not be achievable. The short timescale would be less of a concern for a valuation of just the transferring liabilities.
- Worst of all, the proposals acknowledge that in general the valuation will not be at a date at which audited assets are available, and require the actuary in these circumstances to certify that the unaudited value of assets is not overstated. This is a certification which is normally professionally inappropriate for an actuary to give. Last year, the Actuarial Profession wrote to members including the following warning:

  "Scheme Actuaries are reminded that, under the Actuaries' Code, actuaries "will not act unless they have an appropriate level of relevant knowledge and skill" and are asked to consider carefully whether, in the light of this and in the circumstances of the pension scheme in question, they are able to give the statement sought by the PPF."

  The full note to members is included in the Appendix to this response. Due to being issued so late in the process last year, the note was deliberately low key. The Actuarial Profession will need to consider in the light of the final requirements in respect of bulk transfers for the 2011/12 levy whether it would be appropriate to issue somewhat earlier in the year, while there is still time for schemes to make alternative arrangements, a somewhat stronger statement. In effect, this may force a full audit of the assets at an out of cycle date on a very short timescale, further increasing the costs imposed by the PPF proposals. The alternative of certification of the assets and liabilities transferred would be straightforward since the value of assets transferred would be a matter of fact.

- The consultation document assumes that the transferring scheme can arrange the appropriate certification from the receiving scheme – but in practice it has no leverage to achieve this (and the receiving scheme generally has little incentive to co-operate).
- Conversely, where the transferring scheme is winding up, there may no longer be a scheme actuary appointed to give the required certification.

As noted above, certification of the assets and s179 liabilities transferred would be much less onerous, would not raise the professional issues, and would be far more proportionate. We do not see any disadvantages for the PPF in adopting such an approach in place of requiring full s179 valuations of all the assets and liabilities of both the transferring and receiving schemes.

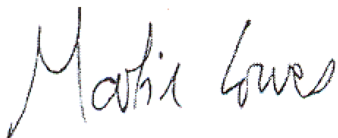
At a meeting between the Profession and the PPF last month, it was suggested that one way forward might be to amend the wording of the certificate that the actuary is expected to sign. Whilst this would address the most serious of our concerns, it would not address the other issues raised above. Nevertheless, we have prepared a draft form of words which we believe would be reasonable to ask actuaries to sign. We have included comments on the uncertainties in the asset value in line with the requirements of TAS D and TAS R issued by the Board for Actuarial Standards.

"The estimated asset value shown in this certificate has been provided to me for or on behalf of the Trustees. I am aware that estimates of asset values at a date can increase or decrease significantly for some time after that date as (for example) more up to date information becomes available from asset managers and/or custodians, as the processing of sales/purchases implemented on or before that date is completed, as payables and receivables due but not paid (or perhaps booked) before that date are processed, and as the accounts are audited. I have not made any adjustment to the asset value to reflect the uncertainty as to whether the value quoted is correct. Other than this general experience that estimated asset values are amended significantly over time until completion of the scheme accounts for the period covering the date, I have no reason to believe that the amount shown is more than the actual asset value at that date."

On a related issue, we question, as last year, whether it is appropriate to retrospectively change the basis that will apply where an “expected” block transfer certificate was not provided in the first half of 2009. Schemes will have weighed the not inconsiderable expense of undertaking full valuations against the then expected levy adjustment before deciding whether calculations should be performed and a block transfer certificate submitted. They would have taken into account the PPF’s 2009/10 formulae which implied that there was no overall levy “penalty” where similarly well-funded schemes were merged without providing the necessary certificate. The latest proposals effectively rewrite the rules for this decision and impose, retrospectively, a substantially higher penalty on such schemes. Since they are past the deadline for submitting the appropriate certificate, they can take no action now to remedy the situation.

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 Margaret Marchetti, Acting Secretary to the Pensions Practice Executive Committee’s Consultations Group on 0207 632 2184 or via margaret.marchetti@actuaries.org.uk.

Yours sincerely,



Martin Lowes
Chairman, Consultations Group of the Pensions Practice Executive Committee

Appendix – Note issued to Scheme Actuaries in June 2010

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PPF guidance on bulk transfers: an announcement from the Actuarial Profession to scheme actuaries

Introduction

The Transfers Appendix to the 2010/11 Levy determination issued by the Pension Protection Fund requires that, following a bulk transfer, the Transferring and Receiving Schemes each provide by 30 June 2010 a Post-Transfer Valuation (in accordance with the s179 requirements).

The PPF allows this Post-Transfer Valuation to be based on an asset value that has not been audited, but nevertheless requires that the actuary certify that the value of the assets is unlikely to be overstated.

Scheme Actuaries are reminded that, under the Actuaries' Code, actuaries "will not act ... unless they have an appropriate level of relevant knowledge and skill" and are asked to consider carefully whether, in the light of this and in the circumstances of the pension scheme in question, they are able to give the statement sought by the PPF.

"Simple" and "Complex" Schemes

For a "simple" small scheme, for example, with a single investment in a pooled fund, a Scheme Actuary may feel able to give the statement sought by the PPF.

For a more "complex" scheme, the Scheme Actuary will need to consider whether he has the appropriate experience and skills in order to be able to decide how big a margin would be needed to be able to certify that an unaudited asset value less such a margin is unlikely to exceed an audited value. It might be difficult for the Scheme Actuary to demonstrate the necessary skill set where, for example, the pension scheme has investments such as in hedge funds or property or other investment in derivatives where values are not available until a month or two after the pricing date. Experience shows that final asset values are sometimes significantly different from the initially reported figures.

Comparison with other tasks pensions actuaries carry out without audited assets

The issue is very different from the requirements for sponsor accounting under FRS 17, IAS 19 and US GAAP. Here the actuary uses unaudited asset values, but can make clear that he is just using the asset value provided to him or her, that the asset value is approximate, and that it may therefore be overstated. The sponsor's auditor applies appropriate audit checks to the asset value supplied to the actuary as well to the work performed by the actuary. Also, it is the net surplus or deficit, rather than the asset value in isolation, which is important. So if the actuary is unaware of significant payments from the scheme that would reduce the asset value and value of liabilities to a similar extent, this is not important for the accounting work, whereas the PPF is seeking separate certification of the asset value from that of the liabilities.

Exceptions to normal certification

Where the Scheme Actuary is unable safely to give the statement required by the PPF, it is suggested that the Trustees and Scheme Actuary discuss alternatives with the PPF.

Following a scheme merger, using the s179 valuations of the predecessor schemes rolled forward and added together (until it is possible to carry out a s179 valuation based on audited accounts), would give the PPF the information it needs, although this would not strictly satisfy the requirements of the PPF's Levy Determination.

Where it is possible to give caveated estimates of assets provided by the actuary, a discussion could be held to discuss a time extension to allow asset valuations to be appropriately done. Alternatively, exceptional late adjustments to levies in the light of changed asset values which emerge later could be allowed, if they are substantially different from earlier estimates supplied by third parties.

Discussions with PPF

The Actuarial Profession raised with the PPF its concerns about the proposed wording of the actuarial certification at the time of the PPF consultation on the proposed 2010/11 Levy Determination, and has discussed the issue with the PPF again since the Determination was issued. This matter has been discussed with the PPF immediately prior to the issue of this guidance. The Profession therefore hopes that the PPF will be flexible where the required certification cannot be given. The PPF expects that this would only affect a small number of schemes which they will be prepared to deal with on a case by case basis and that for the majority of schemes the standard process will be followed.

The Actuarial Profession regrets having to write to members about this issue so late before the 30 June 2010 deadline, and will continue to discuss the issue with the PPF with a view to avoiding any similar late discussions in relation to the 2011/12 and later Levy Determinations.

Professional Regulation Executive Committee

June 2010