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Paul Seymour
Chairman
Board for Actuarial Standards
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Dear Paul,

TOWARDS A CONCEPTUAL FRAMEWORK CONSULTATION PAPER

This consultation paper is a substantial move forward from the preliminary consultation and contains some valuable analysis, particularly in relation to issues of valuation versus planning, pensions regime versus insurance regime, communication of probabilities.

However we note that this is a 67 page paper requiring considerable study. After this a draft conceptual framework will be published, then a final framework, and all this before a single standard is produced.

We have two concerns about this:

1. The delay in actually producing new standards to replace the current GNs which are dating fast. When does the BAS envisage new standards will actually begin to emerge?
2. The danger of devoting such significant resources to developing a framework in the abstract without apparently "road testing" it on any actual standards.

We also note the absence of any element of the framework relating to how the standards will be maintained and updated as circumstances inevitably change over time.

Turning now to the detail of the paper:

Section 2

On page 5, the paper makes the point that BAS is focusing on actuarial *standards* rather than actuarial reports or actuarial work. It then contrasts this with the accountancy model under which there are standards for *financial reports*, but not for *accountancy reports* generally. Does this imply that there is scope for actuarial work to be more widely regulated than is the case for accountancy work? Is this the BAS's intention?

Section 3

On page 7, the paper identifies that a significant minority didn't accept the previously proposed distinction between information and advice. The BAS then attempts to defuse this by developing definitions of different categories of work. However, we suggest the given that the FRC's strategic goal as quoted on page 5 of the paper refers to *information* and not *advice*, this issue needs closure.

The categorising of actuarial work is definitely helpful. However, can the BAS clarify explicitly in which category they would see:

- a) advice to an employer in relation to a pension scheme's technical provisions
- b) advice to an employer in relation to pension scheme funding generally
- c) advice to trustees in relation to actuarial reports (as defined in PA2004), statement of funding principles, schedules of contributions, summary funding statements
- d) advice to employers in relation to reporting pensions in company accounts

We are comfortable with the BAS's proposals on which categories of work should be inside/outside the scope of the BAS standards, and on what basis. However, in practice we suggest it could be articulated as A and B in (B on comply or explain basis); E out; and we'll think about C and D once we've dealt with A and B. ie let's get the priorities right.

Section 4

We fully support the aspiration for principle based standards, whilst recognising that some rule based elements are inevitable. We would simply ask that whenever the BAS envisages something in a standard which could be construed as a rule, the drafters ask themselves "What is the principle behind this, and could the standard utilise this instead?"

Section 5

The principle that the BAS only issues standards and not guidance is clear and helpful. However, the distinction between compulsory vs comply or explain depending on the category of the work means there has to be complete clarity about categorisation. We suggest some refinement of the definition of category B may be helpful (eg see questions re section 3).

The paragraphs on actuaries working as part of a team are not satisfactory. It will often be difficult to tell/easily manipulated whether an actuary is in “overall charge” of the work. We suggest that this is an undue complication and that the important point is that the user is told whether the work complies with the relevant standard or not. In other words, for this category of work there’s always a need to comply or explain.

A detailed point for clarification is the responsibilities of student actuaries working as part of a team with qualified actuaries. Do they have responsibilities under the standards?

Section 6

As stated at the beginning of our response, we find this a very informative analysis of valuation versus planning, pensions regime versus insurance regime. We agree that there are many differences between the calculations used by life insurance actuaries, general insurance actuaries and pensions actuaries. We agree that it is not the role of BAS to force a convergence between different regulatory calculations. We agree with the distinction between valuation and planning.

We assume this level of detailed analysis will not appear in a framework document. The important point is presumably that the BAS intends to recognise these differences and distinctions in the standards it will issue, a point with which we agree.

Section 7

Again, the analysis is informative. We think that the past confusion about probability issues amongst users of actuarial information may be overstated. But we fully support the intention for standards to make such issues as clear as possible to users in the future.

Section 8

The second principle in para 8.2 that existing assets are to be taken at market value seems unduly restrictive. In practice, the vast majority of actuarial work does currently use market values, but we wonder if it is appropriate to exclude other valuations in a framework document. It sounds very permanent.

Other values have been used for certain purposes in the past and could be advantageous in the future. We would suggest that if market values are

considered universally appropriate at present this is incorporated in individual standards. If this were to change for certain types of work, it could then be reflected by changing a standard rather than revisiting the conceptual framework.

Similarly, we suggest the value of contingent assets would be more appropriate for standards rather than as part of a conceptual framework.

We are surprised that in para 8.29, the BAS suggests it would specify how prudence is to be achieved. In the context of the Pensions Act 2004, technical provisions are to be set using prudent assumptions, but the determination of these assumptions is the responsibility of the scheme trustees; not the scheme actuary.

The rest of section 8 seems to outline what might then be in a generic reporting standard. Our comments on the proposals are as follows:

- We cannot see the advantage for users of actuarial work in providing the total undiscounted cash flows, as envisaged in para 8.37. It might be more informative to provide details of the projected cash flows in each year, but see later comments about the costs/benefits of compliance with these proposed requirements.
- We do not agree with the proposed requirement for a probability of sufficiency in 8.48(d). It is not clear how it would have to be calculated, what it would mean, and what value users would get from it.
- To take an example, reports on the actuarial valuation of a pension scheme currently run to 50 pages or more. We suspect that the requirements proposed could double that. Have the proposals been “road tested” by trying to generate such a report? Is this what users of such report want?

Taking forward the final point above, has the BAS considered a tiered approach to reporting standards, based on the size of the entity to which the report is addressed. In a pensions context, compliance with the above proposals would probably be deemed disproportionately expensive for small to medium pension schemes. Could a less detailed standard apply for such schemes?

Specific BAS questions

1 Following the terminology of Section 3, the BAS has determined that Category A should fall within the scope of BAS standards and that Category E should fall outside. In that context:

a) Do respondents consider the five categories drawn up by the BAS (defined in paragraph 3.9) provide a meaningful way to determine which areas of work should be within scope and which should not?

Yes, as long as it is clear what work is in category B.

b) Which, if any, of Categories B, C and D do respondents consider should be within the scope of the framework?

B, and then see how things develop.

c) The BAS would also welcome feedback, and real examples, indicating whether the non-regulatory element of Category B exists in practice or illustrating any concerns that the definitions are wrongly capturing or omitting areas of work.

2 The BAS has set out proposals regarding the objectives and characteristics of standards in Section 4. Do respondents agree with them, specifically the proposals:

a) to introduce some generic standards, to provide coherence and consistency across areas of work, in addition to topic-specific standards as is the case now;

In principle, yes, but there needs to be a practical solution to the resulting need for an actuary to have to comply with multiple standards for a single piece of work.

b) that standards be principle-based, rather than rule-based; respondents are asked to identify any advantages or disadvantages that they consider may flow from this approach; and

Yes.

c) that standards address outputs and responsibilities, as now, with output-based standards focusing on the users of actuarial services and their needs as decision makers?

Yes, but see detailed response.

3 Do respondents foresee any practical issues or problems that they consider should be addressed in relation to the enforceability of standards, as set out in Section 5, in order to ensure the efficient functioning of the enforceability proposals?

See detailed response.

4 Do respondents agree with the proposals in section 8 for:

a) the general principles set out in paragraph 8.2;

See detailed response.

b) the quantification principles set out in paragraphs 8.3-8.30;

Broadly, yes.

c) the generic reporting standard set out in paragraphs 8.31-8.55?

See detailed response.

d) the proposal set out in paragraph 8.48(d) for actuarial quantification of liabilities to include an assessment of the probability that the assets held by the entity at the valuation date will be sufficient to meet those liabilities; respondents are asked to focus, in particular, on:

- any practical problems in assessing the probabilities which the proposal calls for; and
- any limitations on the usefulness of the information if one or more of the probabilities has to be omitted from the assessment.

We see more problems than benefits with this requirement.

We hope this response, coupled with the points made at our recent Sessional meeting will be of assistance in moving matters forward.

Kind regards

David Robertson

Secretariat

On behalf of the Association of Consulting Actuaries