



## **Society of Actuaries in Ireland**

### **ACTUARIAL STANDARD OF PRACTICE PEN-1**

### **FUNDING DEFINED BENEFITS – ACTUARIAL REPORTS**

#### **Classification**

Mandatory

**MEMBERS ARE REMINDED THAT THEY MUST ALWAYS COMPLY WITH THE CODE OF PROFESSIONAL CONDUCT AND THAT ACTUARIAL STANDARDS OF PRACTICE IMPOSE ADDITIONAL REQUIREMENTS UNDER SPECIFIC CIRCUMSTANCES**

#### **Legislation or Authority**

The Pensions Act 1990 together with Regulations issued from time to time under the Act.

#### **Application**

- a) Any Actuary responsible for preparing an actuarial report in relation to a retirement benefits scheme established in the Republic of Ireland that includes advice relating to funding defined benefits where the report has been prepared:
- in order to satisfy legal requirements, including those imposed by the scheme's governing documents,
  - because a formal actuarial valuation report on the funding of the scheme is requested by the client, or
  - to give funding advice when a scheme is initially established.

This ASP applies to, but is not limited to, reports on valuations that are required under Section 56 of the Pensions Act 1990. It does not apply to a funding proposal to which ASP PEN-4 applies. However, an actuarial report prepared for the purpose of a funding proposal may also satisfy the requirements of Section 56 of the Act if it is prepared in accordance with this ASP.

Paragraph 1.4 of this ASP applies to any funding recommendation that is not made in a formal actuarial valuation report. Paragraph 2.1.2 of this ASP also applies to preliminary reports. This ASP does not generally apply to defined contribution schemes. However, it should be applied to such schemes if the advice given is on the contributions required to meet a particular level of benefit (other than lump sum death benefits) or the scheme is subject to the statutory minimum funding standard. The principles of this ASP must be applied if the benefit levels in a scheme with fixed contribution rates are set periodically by the actuary rather than being based on individual account values.



This ASP does not apply to the calculation of Revenue maximum contributions to defined contribution schemes.

This ASP does not apply to calculations of pension expense or directors' remuneration disclosures for employers' accounts.

<b>Version</b>	<b>Effective from</b>
1.0	01.09.1994
2.0	01.07.2005
2.1	30.12.2006
2.2	01.07.2008
2.3	01.11.2010
2.4	01.01.2014
2.4.1	01.05.2017
2.5	01.04.2020

## **Definitions**

“*the Act*” means the Pensions Act 1990 (as amended)

“*ASP*” means Actuarial Standard of Practice

“*should*” (where the context requires) indicates that members of the Society to whom this ASP applies must comply with a particular requirement or prohibition, unless the circumstances are such that the requirement or prohibition is inappropriate and non-compliance is consistent with the standards of behaviour, integrity, competence and professional judgement which other members or the public might reasonably expect of a member

“*the Society*” means the Society of Actuaries in Ireland

“*Statutory Guidance*” means guidance issued by the Pensions Authority and prescribed by the Minister for Social Protection under the Occupational Pension Schemes (Funding Standard) Regulations 1993-2009 (as amended or replaced).

“*Statutory funding level*” means the resources of the scheme expressed as a proportion of the liabilities of the scheme where the resources and liabilities are those that are referred to in Section 44 (1), Part IV of the Act. This should be expressed as a numerical percentage even where it is greater than 100%.

“*Overall funding level*” means the resources of the scheme expressed as a proportion of the sum of the liabilities of the scheme and the funding standard reserve, where the resources and liabilities are those that are referred to in Section 44 (1), Part IV of the Act and the funding standard reserve means the amount calculated in accordance with Section 44 (2) of the Act. This should be expressed as a numerical percentage even where it is greater than 100%.



## **1 Introduction**

- 1.1 The main purpose of this ASP is to ensure that reports contain sufficient information to enable the expected future course of a scheme's contribution rates to be understood and also to enable the current solvency level of a scheme to be understood. The ASP is therefore intended to ensure that the methods and assumptions used are properly explained and that variations between the assumptions chosen and actual experience are analysed in the report.
- 1.2 This ASP is not intended to restrict the actuary's freedom of judgement in choosing the method of valuation and the underlying assumptions employed in deriving the contributions referred to in paragraph 2.6.2 (or commenting on their adequacy) where these are not restricted by legislative requirements.
- 1.3 In this ASP references to the previous or preceding valuation or report mean the previous or preceding valuation or report of a similar nature, whether carried out by the actuary or another actuary.
- 1.4 The actuary may need to update the funding advice between formal actuarial valuations to allow for benefit changes, or to take account of recent experience that differs from the actuarial assumptions. The actuary should exercise judgement to consider the extent to which updated funding advice should comply with this ASP.
- 1.5 This ASP continues to apply while a scheme is run as a closed fund. Where an event occurs which under a scheme's Trust Deed and Rules triggers winding-up, the actuary must consider whether it would be appropriate to advise the trustees that an actuarial valuation should be carried out. The ASP continues to apply where a scheme has commenced winding-up, although in such circumstances some parts of the ASP might not be applicable (see paragraph 2.2.3 below).

## **2 The Report**

### **2.1 Introduction**

- 2.1.1 The items in paragraphs 2.2 to 2.10 below, except where otherwise indicated, are essential components of a report. Suitable explanations of other features may also be very important and therefore additional information may often be desirable.
- 2.1.2 Should a preliminary report be issued not including all the components listed below, in the expectation that a further and full report will be made, it must be made clear in the preliminary report that it does not conform to ASP PEN-1 but that the further report will do so.
- 2.1.3 The actuary must ensure that the report is clear and appropriate to the circumstances and its intended audience.



## **2.2 Basic Information**

- 2.2.1 The report must make it clear to whom it is addressed, by specifying the client. The report must state the purpose for which the valuation is made and the dates as at which the current valuation and, if applicable, the immediately preceding valuation were conducted. The report must be signed by the actuary and the date of signing must be provided.
- 2.2.2 Although any report will be addressed to the actuary's client (normally the trustees) the actuary needs to bear in mind that the client may wish to make the report available to third parties. Any limitations on the extent to which third parties can rely on the advice must be set out in the report.
- 2.2.3 The report must state that it has been prepared in accordance with ASP PEN-1 current at the date the valuation report is signed. The actuary need not comply with any part of ASP PEN-1 that is clearly inappropriate, but a complete explanation of all such departures must be given. If the valuation is intended to satisfy the requirements of Section 56 of the Act, the report must state that this is the case and must confirm that the actuary signing the report holds a current Scheme Actuary Certificate.
- 2.2.4 The report must also refer to any legislative provisions and, if applicable, the appropriate sections of the legal documentation of a scheme under which the valuation is being made.
- 2.2.5 The report must include a statement of the benefits which have been valued. This may be a summary of the terms of the scheme or a reference to appropriate documents. Reference must be made to the extent to which allowance has been made for discretionary increases in benefit (and the recent practice in granting such increases) or discretionary benefits. If the actuary has excluded from the report assets and corresponding liabilities in respect of certain benefits, such as AVCs and pensions secured by annuities, the report must note these exclusions.
- 2.2.6 Where there is any doubt about the benefits, the actuary must specify where the uncertainty exists and make clear the assumption made.
- 2.2.7 The report must include a summary of the membership on which the investigation is based.
- 2.2.8 The report must state that the actuary has relied on the accuracy of the information provided by the trustees or administrators. The actuary must take reasonable steps to satisfy himself or herself that the data provided by the trustees or administrators is of adequate quality for the purpose of the valuation. If the actuary has any reason to doubt that the data is sufficiently reliable, the report must be qualified appropriately.



- 2.2.9 The report must include a summary of the investment strategy being pursued by the trustees, a statement of the market value of the assets at the valuation date and a summary of the investments held, subdivided between the main asset classes. If the scheme's assets are invested in an insurance policy or policies and a breakdown is not possible, a description of the nature of the policy or policies must be given. The report must confirm the source of the information on the scheme's investments. If the actuary has any reservations as to the asset information provided, this fact must be stated. Any reduction in the assets due to self-investment and concentration of investment (within the meaning of the Act) must be quantified.
- 2.2.10 Reference must also be made to any insurance arrangements in place for the benefit of the scheme. This includes group life assurance held by the trustees. Information on any self-insurance of scheme benefits must be provided and where the funding position could be materially negatively affected by the death of one or more members, this must be highlighted.
- 2.2.11 If part of the assets of the scheme to be taken into account for the purpose of meeting the Funding Standard or Funding Standard Reserve take the form of contingent assets or unsecured undertakings (as defined in Statutory Guidance in relation to Section 47 of the Pensions Act issued by the Pensions Authority), the Scheme Actuary must carefully consider whether he or she has the relevant skills to competently value such assets. Where necessary, the Scheme Actuary must ensure that advice and guidance is sought from appropriate experts (which may include but is not limited to legal advisers, covenant assessors or corporate debt specialists) when determining the value to be placed on the contingent assets. The report must include a brief description of the contingent assets or unsecured undertakings held by the scheme and how they have been valued and must specifically refer to any minimum period over which such assets are in place. When valuing or considering the use of contingent assets or unsecured undertakings, the Scheme Actuary must refer to and take account of the content of the Statutory Guidance referred to in this paragraph issued by the Pensions Authority.
- 2.2.12 The requirements of 2.2.11 may be met alternatively by appropriate reference to a separate legal agreement documenting as a minimum the above information in relation to the contingent assets or unsecured undertakings. In this case, the value of the contingent asset and the source of the valuation should be specified in the report together with the reference to the agreement.

### **2.3 Inter-valuation Period**

- 2.3.1 The report must include a statement of the rates or amounts of contribution paid during the inter-valuation period; and also those recommended in the previous report and, where the amounts involved are material, in any subsequent advice. The report must also include a commentary on any material developments affecting the scheme during that period, and on any significant variations in experience from the assumptions made at the previous valuation.



## **2.4 Funding**

- 2.4.1 The report must state the funding objectives on which the advice referred to in paragraph 2.6.2 has been based. The report must note any changes in the funding objectives since the previous report.
- 2.4.2 The implications of the funding objectives for the stability of contribution rates must be explained.
- 2.4.3 Where the scheme has more than one funding objective, comment must be made on the difference between the objectives.

## **2.5 Valuation method and assumptions**

- 2.5.1 The report must contain a summary of both the demographic assumptions and economic assumptions made, explicitly and implicitly, in valuing both the liabilities or target benefits, and the assets at the valuation date. The summary must include details of other assumptions such as the exercise of material options by the members, for example lump sum commutation or early retirement but these examples are not exhaustive. The implications of these assumptions regarding the exercise of material options on the valuation results should be explained. A statement must be made as to the extent to which there have been changes to the assumptions used since the previous report.
- 2.5.2 The derivation of the assumed rate of investment return(s) at the valuation date should be explained. In particular, an explanation of how these assumptions are influenced by the trustees' investment strategy and, where relevant, funding objectives should be provided.
- 2.5.3 The report must identify the mortality table(s) used in respect of pre- and post-retirement periods, in sufficient detail that another actuary could replicate the calculations and must state the life expectancy for a person reaching normal retirement age at the valuation date. The report must explain the assumptions made in relation to future mortality improvements and quantify the impact that these assumptions have on life expectancy for future cohorts of retirees.
- 2.5.4 The report must explain the method employed in developing the advice referred to in paragraphs 2.6.2 and 2.6.4 below and whether and in what way future entrants have been taken into account in the valuation. A note must be made of any changes to the method set out in the previous report.
- 2.5.5 The report must draw attention to those assumptions to which the valuation results are particularly sensitive.



## 2.6 Valuation results

- 2.6.1 The report must state the value of assets, the value of accrued liabilities and the funding level on the basis being used for the current valuation. The report must also include an analysis of the actuarial surplus or funding level compared with the position disclosed by the previous valuation. The analysis must be sufficient to identify and broadly quantify the impact of the material items of actuarial gain or loss including changes in the valuation method and the valuation assumptions.
- 2.6.2 The report must recommend contributions consistent with the funding objectives for the period until the next formal actuarial valuation. Alternatively, if contributions are determined elsewhere, e.g. in governing documentation, so that a recommendation by the actuary is inappropriate, the report must include comment on the adequacy of the rate.
- 2.6.3 The level of detail in the report must be sufficient, in the normal course of events, to determine unambiguously the contributions that should be paid without further reference to the actuary. In particular the following must be considered:
- (i) (if applicable) whether AVCs are excluded from the member contribution rate,
  - (ii) whether premiums for death benefit insurance are payable in addition to a fixed contribution rate,
  - (iii) whether expense payments are payable in addition to the fixed contribution rate,
  - (iv) the definition of pensionable payroll,
  - (v) the timing and frequency of contributions, and
  - (vi) the effective dates of any changes to the contribution rate including changes effective from the valuation date.
- 2.6.4 The actuary should state the implications for the expected contributions in the longer term (for example, over the future working lifetime of active members) if these contributions differ from the contributions recommended in accordance with paragraph 2.6.2. This may include, among other situations, where a deficit is being funded over a fixed term or where a funding proposal is in place.
- 2.6.5 References to contributions and contribution rates above or elsewhere in this ASP are not intended to constrain the way future contributions are described.



## **2.7 Statutory minimum funding standard and funding standard reserve**

2.7.1 In the case of a scheme subject to the statutory minimum funding standard, the report must state:

- (i) the amount of the statutory liabilities valued in accordance with ASP PEN-3 and the statutory funding level at the valuation date, or the date of the most recent Actuarial Funding Certificate.
- (ii) the amount of the funding standard reserve valued in accordance with ASP PEN-3 and the overall funding level at the valuation date, or the date of the most recent Funding Standard Reserve Certificate.

2.7.2 Where the previous valuation complied with either requirement outlined in 2.7.1, the actuary must include the relevant figures from the previous valuation in the report.

2.7.3 If, for the purpose of calculating the statutory funding level, the liabilities in respect of active and deferred members have been valued on the assumption that such liabilities would be discharged by the payment of transfer values in the event of a wind-up, the report must point out that the value of the liabilities does not represent the cost required to secure the accrued benefits on a guaranteed basis (i.e. by purchasing deferred annuities, if such annuities are available for purchase).

## **2.8 Discontinuance**

2.8.1 In the case of a scheme that is subject to the statutory funding standard, the amount required to discharge the liabilities in the event of an actual wind-up may be greater than the amount of the statutory liabilities valued in accordance with ASP PEN-3. Where this is the case, or for schemes which are not subject to the statutory funding standard, the report must provide a commentary on the potential liabilities that may arise on wind up which should include:

- (i) a description of some of the relevant factors that may influence the liabilities that could arise if the scheme were to wind up as at the date of the valuation, and
- (ii) an explanation of the possible range of approaches which could be taken for valuing those liabilities.

The actuary may, but is not required to, provide an estimate of the amount required to discharge the liabilities on wind-up, using one or more of the approaches discussed.





## **2.9 Investment risk**

- 2.9.1 The report must include an analysis of the scheme's exposure to investment risk and the sensitivity of the funding position to future investment market changes.
- 2.9.2 The actuary should:
- (i) explain the scope for variability in the recommended contributions referred to in paragraph 2.6.2 and the funding level referred to in paragraph 2.6.1, having regard to the assets held and the form and incidence of the liabilities;
  - (ii) to the extent that this has not already been addressed in the report, indicate the contributions that would be required, and the relative level of variability in those contributions and the funding level, if the assets were invested in a mixture of fixed interest and index-linked long dated government bonds at the effective date of the valuation. The assumed rate of return should reflect the actual gross redemption yield on such bonds or the yield on a government bond index of appropriate duration (subject to adjustment to reflect the possible risk of default if some or all of the bonds in the index are not considered investment grade), and the liabilities were valued accordingly
- 2.9.3 Unless the funding level referred to in paragraph 2.6.1 is the statutory funding level, the actuary should explain the scope for variability in the statutory funding level and overall funding level, having regard to possible investment market changes and to the relationship between the assets held and the form and incidence of the statutory liabilities. This would normally include providing information on how the funding level(s) would vary under different investment strategies and asset allocations, and varying interest rate environments.
- 2.9.4 Attention must also be drawn to specific investment risks that are relevant to the scheme, in particular currency mismatching, concentration of assets, and self-investment.
- 2.9.5 The report must contain sufficient analysis to convey a reasonable understanding of the nature and extent of the investment risk. The actuary is, however, not required to give investment advice.
- 2.9.6 The requirements of section 2.9 may be met alternatively by appropriate references to a separate report dealing with investment risk that includes comparable information and analysis to that specified in paragraphs 2.9.1 – 2.9.5. If such a report is available to the actuary, and he or she is satisfied as to its suitability for this purpose, the actuary may refer to the report on investment risk, stating the effective date of the report, the author and, if required, the relevant sections in the report on investment risk that meet the requirements of section 2.9 of this ASP. The actuary may also append the investment report to the valuation report in its entirety, or if he or she considers it appropriate, the relevant sections of the investment report, provided that if only the relevant sections are appended, the author and effective date of the full report is referred to in the valuation report.



## 2.10 Other risks

2.10.1 The actuary must also comment in the report on other risks that may impact the scheme's future development. The actuary need not refer to all the risks the scheme is exposed to, but should comment on those risks that in his or her opinion are significant in relation to the likely future development of the scheme. These risks should include, where relevant:

- Improvements in longevity
- Demographic changes
- Employer covenant
- Legislative, regulatory or statutory guidance changes
- Market changes (including risk of default on bond holdings)
- Scheme administration
- Other financial risks e.g. inflation, salary increases, etc.

This list is not exhaustive.



## EXPLANATORY NOTE

### ACTUARIAL STANDARD OF PRACTICE PEN-1, VERSION 2.5

*This Explanatory Note does not form part of the ASP.*

In Version 2.5, changes have been made to reflect feedback from Reviewing Actuaries following the compliance monitoring process and discussion at the SAI Scheme Actuary Forum in March 2019. A presentation made to the SAI summarising the feedback from Reviewing Actuaries can be found here:

<https://web.actuaries.ie/sites/default/files/180315%20Scheme%20Actuary%20Forum%20AL.pdf>

The key changes are broadly summarised as follows:

- Provided for funding levels to be expressed as a numerical percentage, even where they are greater than 100%.
- Replaced the “reserve funding level” with the “overall funding level” for clarity and moved the definition from the body of the document into the Definitions section.
- The requirement to highlight where the death of one or more members could materially affect the funding position now arises only where the funding position could be materially *negatively* affected.
- Provided examples of assumptions regarding material options by the members, and inserted the requirement to explain the implications of those assumptions.
- The requirement to explain how the funding objectives influence the derivation of the assumed rate of investment return(s) is required now only where relevant.
- The impact of material items of actuarial gain or loss since the previous valuation must now be broadly quantified.
- The requirement to comment on the implications for contributions over the long term is clarified.
- The section on Discontinuance has been substantially re-written; a key change is that the requirement to estimate the liabilities that would arise on wind up as at the date of the valuation has been removed. Actuaries are instead required to comment on the potential liabilities that may arise (and may provide an estimate of the value of these liabilities if they wish).
- Some terminology changes for consistency throughout the document (e.g. “contribution rate” changed to “contributions”).

A “tracked changes” version of this ASP is available on request (email [info@actuaries.ie](mailto:info@actuaries.ie)).