Society of Actuaries in Ireland

ACTUARIAL STANDARD OF PRACTICE PEN-3

ACTUARIAL FUNDING CERTIFICATES, FUNDING STANDARD RESERVE CERTIFICATES AND ACTUARIAL STATEMENTS UNDER THE PENSIONS ACT 1990

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

Statutory guidance issued by The Pensions Authority and prescribed by the Minister for Social Protection under the Occupational Pension Schemes (Funding Standard) Regulations 1993 to 2019 (as amended or replaced).

Application

Any Scheme Actuary responsible for signing an Actuarial Funding Certificate, Funding Standard Reserve Certificate or Actuarial Statement under the Pensions Act 1990.

Version	Effective from
1.0	05.04.1993
2.0	15.07.2003
3.0	05.09.2003
3.1	30.12.2006
3.2	01.07.2008
3.3	01.11.2010
3.4	01.07.2011
4.0	01.01.2013
4.1	01.10.2021

Definitions

"the Act" means the Pensions Act 1990 as amended

"ASP" means Actuarial Standard of Practice

"the Code" means the Society's Code of Professional Conduct

"the Disclosure of Information Regulations" means the Occupational Pension Schemes (Disclosure of Information) Regulations 2006 as amended

"should" (where the context requires) means 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 of the Society 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 to 2019 (as amended or replaced).

1 Introduction

1.1 This ASP is the “applicable professional guidance issued by the Society of Actuaries in Ireland and specified in the regulations” referred to in section 42(4) of the Act.

1.2 It is essential that Scheme Actuaries keep themselves informed on amendments to the Act as well as the Regulations pursuant to the Act and Statutory Guidance and any amendments thereof as may occur from time to time. This ASP does not contain the full text of the relevant sections of the Act and does not give any interpretation of them. Any Scheme Actuary must satisfy himself/herself that he/she has acted in accordance with the legislation as well as this ASP.

1.3 The Scheme Actuary, in completing the Actuarial Funding Certificate, Funding Standard Reserve Certificate or Actuarial Statement must comply with this ASP or “with any other applicable guidance issued by any other person (including the Minister) and specified in the regulations.” It is essential that Scheme Actuaries keep themselves fully informed on any such additional applicable guidance including Statutory Guidance.

1.4 The requirements of Statutory Guidance are in addition to those outlined in this ASP and, in the event of any conflict, Statutory Guidance shall prevail.

1.5 The Act requires that

(i) the trustees of a relevant scheme cause Actuarial Funding Certificates and Funding Standard Reserve Certificates to be prepared by an actuary (section 42 of the Act).

(ii) the trustees submit to the Pensions Authority such certificates (section 42 of the Act).

(iii) the Actuarial Funding Certificate certifies that as at a date, the “effective date”, the scheme does/does not satisfy the funding standard provided for in section 44 of the Act (section 42 of the Act).

(iv) the Funding Standard Reserve Certificate certifies that, as at the same effective date as the Actuarial Funding Certificate, the scheme satisfies/does not satisfy the funding standard reserve (section 42 of the Act).

(v) for a scheme where an Actuarial Funding Certificate has been prepared under section 42 of the Act, an Actuarial Statement must be included in the trustees’ annual report relating to a period ending after the effective date of that certificate.

1.6 The importance of the Actuarial Funding Certificate, the Funding Standard Reserve Certificate and the Actuarial Statement contained within the trustees' annual reports places a high level of responsibility on the profession. An Actuarial Funding Certificate, a Funding Standard Reserve Certificate or an Actuarial Statement may be signed only by an actuary who holds a current Scheme Actuary Practising Certificate issued by the Society.

It is emphasised that the responsibility for signing the document is that of the signing Scheme Actuary alone. The Code makes it clear that every actuary in his/her professional capacity, whether remunerated by salary or fee, has a duty to his/her profession and his/her responsibility to his/her employer or client must be consistent with this.

1.7 The Scheme Actuary is in a special position in that, in addition to the normal responsibilities to his/her employer or client, when signing a certificate he/she has statutory obligations laid on him/her by the Act and by regulations made pursuant to the Act.

1.8 This ASP highlights issues arising for Scheme Actuaries in signing certificates and completing statements. In particular, the considerations needed in the interpretation of the "financial and other assumptions" to be adopted are dealt with in detail.

2 The Actuarial Funding Certificate

2.1 The Act places responsibility on the trustees to have an Actuarial Funding Certificate prepared as at the effective date. In practice, the effective date is chosen by the trustees, subject to the requirements of the Act.

2.2 In relation to the signing of Actuarial Funding Certificates, the Scheme Actuary is required to state if, in his/her opinion, the resources of the scheme at the effective date are/are not sufficient etc. and, based on this opinion, to certify that the scheme satisfies/does not satisfy the funding standard.

2.3 The Scheme Actuary must make whatever enquiries he/she considers appropriate to satisfy himself/herself that he/she has been supplied with all the relevant data and information. Section 54(4) of the Act obliges both the employer and trustees to comply with any requests from the Scheme Actuary to furnish him/her with such information as he/she may reasonably require to enable him/her to carry out his/her functions under the Act.

2.4 For the purposes of the funding standard, the liabilities at the effective date must represent the value placed by the Scheme Actuary on the benefits outlined in section 44(1)(a) of the Act.

Such value must be computed as follows:

(a) In respect of pensions in payment (including pension benefits for members who have reached normal pensionable age), on an actuarial basis which is consistent with the cost of buying annuities in the marketplace.

<u>Traditional Annuity Basis</u>

(i) The cost can be determined by:

a) obtaining annuity quotations either on an individual or bulk basis, or
b) fitting an actuarial basis to sample market rates, bearing in mind the age profile and pension amounts of the pensioners and subject to adjustment, where appropriate, for bulk annuity discounts based on current market practice provided that the Scheme Actuary is satisfied that such a discount is likely to be available for the scheme.

(ii) The Scheme Actuary is not required to take account of the issue of market capacity in the event of the actual wind-up of a scheme that has large amounts of pensions in payment.

(iii) However, the Scheme Actuary should make suitable adjustments where the pensions payable under the scheme rules cannot be replicated easily in the market.

(iv) Specifically, for schemes providing index-linked or parity pay increases to pensions in payment, the Scheme Actuary may assume that, in the event of a wind-up, annuities with a fixed rate of increase in accordance with the basis specified in the Appendix to this ASP would be purchased by the trustees.

(v) For a scheme where there is substantive evidence that the scheme-specific mortality experience is significantly different from the mortality experience of individual life office annuitants and the Scheme Actuary is satisfied that this evidence would be taken into account by an insurer in a bulk purchase, the Scheme Actuary may adjust the mortality basis underlying current market annuity rates to reflect the extent of the difference between the scheme's mortality experience and the experience of individual life office annuitants. However, the adjusted mortality basis must still take into account an allowance for future improvements in mortality rates.

Section 53B Basis (as defined in Statutory Guidance)

(vi) The actuary may, in the circumstances and to the extent permitted by the Statutory Guidance, reduce the value placed on some or all of the pensions in payment under the scheme.

(b) In respect of deferred pension entitlements (all active members are treated as becoming deferred members on the effective date), the value shall be not less than the sum of individual transfer values to which each member would be entitled under the standard transfer value basis contained in ASP PEN-2 issued by the Society and Statutory Guidance issued by the Pensions Authority.

(c) Allowance must be made for the estimated expenses of administering the winding up of the scheme. Such allowance would typically be the greater of 2% of the sum of the liabilities under (a) and (b) above and €10,000. The Scheme Actuary may use an alternative figure provided he/she is satisfied that his/her figure represents a best estimate of these expenses, bearing in mind such factors as the length of time to complete the process, difficulties with administration, the number of members involved and the complexity of benefits.

2.5 Section 46 of the Act states that, notwithstanding any provision in the winding up rule in relation to the purchase of annuities, the Scheme Actuary "may" assume that the liabilities of the scheme "could" have been provided by applying resources, of equivalent actuarial value to the benefits specified in the Acts to the payment to another scheme or to the purchase of approved contracts e.g. buy-out bonds. The Act does not compel the Scheme Actuary to adopt this approach. Where this approach is not used in relation to deferred pension entitlements, the Scheme Actuary should draw the trustees' attention to that fact in his/her covering letter or report.

If this approach is used in relation to pensions in payment (including pension benefits for active members who have reached normal pensionable age), the Scheme Actuary must assume that the payment to another scheme would be equivalent to the actuarial value of the benefits calculated in accordance with paragraph 2.4.

2.6 The Scheme Actuary signing a certificate must have regard to any concentration of investments or self-investments as prescribed by the regulations under the Act. Self-investment includes contributions due to the scheme but not yet paid.

2.7 If the assets of the fund take the form of insurance policies, the Scheme Actuary should have regard to the practice of the office in terminating such policies and, where appropriate, the realisable value of such policies. Where annuity policies have been purchased in respect of pensions in payment or deferred annuity policies in respect of deferred benefits, either the liabilities can be reduced in respect of the annuities or deferred annuities purchased or the policies valued on a basis consistent with paragraph 2.4.

2.8 For the purposes of the funding standard, the value of assets at the effective date should represent a best estimate of the distributable proceeds on an orderly wind-up of the scheme commencing on the effective date. Prepaid contributions may be included as part of the distributable proceeds on winding up if they would not fall to be refunded to the sponsoring employer in these circumstances.

2.9 If part of the assets of the scheme to be taken into account for the purpose of meeting the Funding Standard take the form of Contingent Assets, as defined in Statutory Guidance, the Scheme Actuary must comply with the relevant Statutory Guidance.

3 Funding Standard Reserve Certificates

3.1 Section 42(2A) requires the trustees of a relevant scheme to have a Funding Standard Reserve Certificate prepared by a Scheme Actuary who is required to certify that the scheme either satisfies or does not satisfy the funding standard reserve.

3.2 The funding standard reserve is set out in section 44(2) of the Act and under section 42(2)(b) includes the amount by which the funding standard liabilities of the scheme would increase if interest rates fell by ½% (or such other percentage as may be prescribed by the Minister). For this purpose the Scheme Actuary should calculate the increase in the annuity cost for pensions in payment and the increase in transfer values for active and deferred members due to the change in the relevant post retirement Market Value Adjustments arising from the fall in interest rates. The discount rates pre and post retirement used for calculating transfer values can be assumed to remain unchanged.

3.3 If part of the assets of the scheme to be taken into account for the purpose of meeting the Funding Standard Reserve take the form of Contingent Assets including Employer Undertakings, as defined in Statutory Guidance, the Scheme Actuary must comply with the relevant Statutory Guidance.

4 Actuarial Statements

4.1 The trustees' annual report must contain a copy of the latest Actuarial Funding Certificate. In addition, section 55 of the Act requires that the trustees' annual report shall include a statement by an actuary as to whether he/she is reasonably satisfied that, if he/she were to prepare an Actuarial Funding Certificate and a Funding Standard Reserve Certificate having an effective date of the last day of the period to which the annual report relates, he/she would certify:

a) in the case of the Actuarial Funding Certificate, that the scheme satisfies the funding standard, and

b) in the case of the Funding Standard Reserve Certificate, that the scheme satisfies the funding standard reserve

4.2 Also under section 55 of the Act, where a Funding Proposal has been submitted in accordance with section 49 of the Act, each trustees' annual report relating to a period ending on a day after the effective date of the Actuarial Funding Certificate or Funding Standard Reserve Certificate to which the Funding Proposal relates shall include an Actuarial Statement. This form of Actuarial Statement is covered in ASP PEN-4.

4.3 It is not required that a full actuarial valuation be undertaken in order that the Scheme Actuary can sign the Actuarial Statement. Approximate projections may be used based on previous funding calculations for the scheme.

The Scheme Actuary must decide in the light of the funding level at the previous valuation and prevailing conditions, together with those experienced since the previous calculations, as to whether an approximate projection or a full valuation is appropriate.

In deciding whether to use approximate projections or not, the Scheme Actuary should take into account that, even with very stable financial conditions ruling over the period of projection, the value of liabilities in respect of active and deferred members can rise very rapidly and that the value of pension liabilities can rise as well as fall depending on the nature of the pension payments, on mortality experience and on annuity rates.

4.4 The Scheme Actuary should satisfy himself/herself that the value of the assets reflects the estimated distributable proceeds on an orderly wind-up of the scheme commencing on the effective date.

5 Other issues

5.1 The funding standard set down in the Act may not necessarily be the same as that typically used in assessing solvency for the purposes of advice to trustees. The Scheme Actuary should have regard to differences between the scheme rules on winding up and the members' expectations on the basis of the trustees' established practice in relation to discretions, options, etc. In particular, when winding up occurs, some members might well have options which they might otherwise have no occasion to take or exercise. Included here might be a unilateral right to immediate early retirement pensions on winding up or an option which is only available subject to the consent of the trustees or employer. In all such cases, the Scheme Actuary should take particular care to notify the trustees or employer of the assumptions made and the consequences of them exercising their discretion or members availing of options different than those assumed.

5.2 When an Actuarial Funding Certificate is submitted to the Pensions Authority and the Scheme Actuary signing the certificate is also a trustee or a director of a company acting as trustee, then that status must be disclosed in a letter accompanying the certificate.

Appendix **Substitution of fixed rate increases for index-linked pension increases**

For the purpose of paragraph 2.4 (a) (iv), the assumed rate of price inflation (PI) must be derived from the Eurozone HICP (ex tobacco) inflation swap curve for a duration in line with that of the relevant pensioner liabilities as at the effective date of the calculation.

PI must be calculated to 1 decimal place, i.e. x.x%.

The fixed rate of pension increases to be substituted for index-linked increases must then be determined on the basis of the following tables:

Annual Floor of 0%, Annual Cap 2%

PI	Index Linked Increase	Parity Pay Increase
-1.0%	0.20%	0.55%
0.0%	0.55%	1.00%
1.0%	1.00%	1.45%
2.0%	1.45%	1.80%
3.0%	1.80%	1.95%
4.0%	1.95%	2.00%

Annual Floor of 0%, Annual Cap 3%

PI	Index Linked Increase	Parity Pay Increase
-1.0%	0.20%	0.60%
0.0%	0.60%	1.15%
1.0%	1.15%	1.85%
2.0%	1.85%	2.40%
3.0%	2.40%	2.75%
4.0%	2.75%	2.95%

Annual Floor of 0%, Annual Cap 4%

PI	Index Linked Increase	Parity Pay Increase
-1.0%	0.20%	0.60%
0.0%	0.60%	1.20%
1.0%	1.20%	2.00%
2.0%	2.00%	2.75%
3.0%	2.75%	3.40%
4.0%	3.40%	3.75%

Annual Floor of 0%, Annual Cap 5%

PI	Index Linked Increase	Parity Pay Increase
-1.0%	0.20%	0.60%
0.0%	0.60%	1.25%
1.0%	1.25%	2.05%
2.0%	2.05%	2.95%
3.0%	2.95%	3.75%
4.0%	3.75%	4.35%

For other rates of PI, and/or other annual caps, the appropriate fixed rate increase must be determined by linear interpolation of the above rates. When interpolating across both PI and the cap, the intermediate results should be calculated to at least three decimal places and the final result rounded to two decimal places.

In other circumstances, such as, for example, where the floor on annual pension increases is greater than 0%, or where any historic negative inflation is allowed for before any increase is applied, the Scheme Actuary must calculate the fixed rate increases using a consistent methodology to that employed to derive the tables above. For more detail on the methodology employed, please read the paper *Financial and Economic Assumptions 2020* at https://web.actuaries.ie/press-publications/financial-and-economic-assumptions

Explanatory Note

The changes from version 4.0 (effective 01.01.2013) are as follows:

1) The use of a pair of reference bonds to calculate the assumed rate of price inflation has been discontinued in favour of the use of the Euro-inflation swap curve.

2) The methodology used to calculate the fixed rate of pension increases has been updated to reflect the methodology set out in the Financial and Economic Assumptions 2020 paper prepared by the Finance and Investment Committee.

3) In addition, there are some minor wording updates including references to the Pensions Authority, updated reference to legislation and guidance and to make the ASP gender neutral.