

May 2016

Consultation: Revised Specific TASs

Annex 3: TAS 400 *Funeral Plan Trusts*

The FRC is responsible for promoting high quality corporate governance and reporting to foster investment. We set the UK Corporate Governance and Stewardship Codes as well as UK standards for accounting, auditing and actuarial work. We represent UK interests in international standard-setting. We also monitor and take action to promote the quality of corporate reporting and auditing. We operate independent disciplinary arrangements for accountants and actuaries, and oversee the regulatory activities of the accountancy and actuarial professional bodies.

The FRC does not accept any liability to any party for any loss, damage or costs howsoever arising, whether directly or indirectly, whether in contract, tort or otherwise from any action or decision taken (or not taken) as a result of any person relying on or otherwise using this document or arising from any omission from it.

© The Financial Reporting Council Limited 2016

The Financial Reporting Council Limited is a company limited by guarantee.

Registered in England number 2486368. Registered Office:

8th Floor, 125 London Wall, London EC2Y 5AS

CONTENTS

		Page
1	Scope of TAS 400	1
2	TAS 400 provisions	5
3	Impact assessment	11
4	Invitation to comment	13

1 SCOPE OF TAS 400

Introduction

- 1.1 In this section we describe our proposals for the scope of Technical Actuarial Standard 400: *Funeral Plan Trusts* (TAS 400).
- 1.2 The proposed scope reflects the output of the first two stages of our risk assessment process, in which we identified areas of technical actuarial work where there is a high degree of risk to the public interest and analysed both the risks associated with that work and the effectiveness of existing controls. As a result of our risk assessment, we continue to consider it appropriate that technical actuarial work for funeral plan trusts be subject to a Specific TAS.

Background

- 1.3 Pre-paid funeral plans are either:
 - a) Trust-based – where the plan provider secures that assets required to provide the funeral are held on trust; or
 - b) Insurance-based – where the plan provider secures that the pre-payment is applied towards a whole life insurance policy on the plan holder’s life.
- 1.4 In line with the existing Funeral Plans TAS, the proposals for TAS 400 relate to the actuarial work for the trust established as part of a trust-based pre-paid funeral plan (“funeral plan trust”).
- 1.5 Technical actuarial work for insurers providing whole life insurances which are used to support insurance-based pre-paid funeral plans will be covered by TAS 200.

Regulatory context

- 1.6 To be exempt from regulation by the Financial Conduct Authority (FCA), the funeral plan trust must meet five requirements set out in of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001¹ (RAO). One of the requirements is that the assets and liabilities of the trust must, at least once every three years, be determined, calculated and verified by an actuary who is a Fellow of the Institute and Faculty of Actuaries (IFoA).
- 1.7 The Funeral Planning Authority (FPA) sets operational and governance standards for funeral plan providers. For plan providers registered with the FPA, the FPA’s rules² require that the assets and liabilities of the funeral plan trust must be determined, calculated and verified annually by an actuary who is a Fellow of the IFoA. This assessment of the assets and liabilities is part

¹ Articles 59 and 60

² Rule 4.3.10.2

of the information that the FPA relies on when deciding whether to accept a new applicant for FPA registration and also when deciding whether to renew a plan provider's registration.

- 1.8 The IFoA's Actuarial Practice Standard on Funeral Plans (APS Z1) sets out the professional obligations for its members working for UK trust-based pre-paid funeral plans.
- 1.9 The IFoA has also issued an accompanying guide for actuaries on trust-based pre-paid funeral plans that sets out guidance on issues its members may consider when undertaking work in this area. This guide contains technical and professional guidance and refers to the requirements of the Generic TASs and the Funeral Plans TAS.

Proposed scope

- 1.10 We are proposing that the scope of TAS 400 is limited to technical actuarial work concerning the determination, calculation and verification of the assets and liabilities of a funeral plan trust required by either the RAO or the FPA.
- 1.11 We consider that, given its role in exempting a trust-based funeral plan from FCA regulation, the technical actuarial work in determining, calculating and verifying the assets and liabilities of the trust required under the RAO is a crucial tenet of the regulatory framework for these arrangements. The technical actuarial work has a high degree of public interest and plays an important role in assisting trustees in assessing and managing the financial position of the trust.
- 1.12 The initial and annual assessment of assets and liabilities required by the FPA provides important regular information that assists the trustees in managing a trust to meet its purposes of keeping client monies safe and to be in a position to meet the costs of funerals as they fall due. This regular actuarial assessment for the FPA is an important safeguard within the current regulatory regime and therefore this work has a high degree of risk to the public interest.
- 1.13 We consider that the application of technical actuarial standards to both the assessment required under the ROA and that required by the FPA is an important element of the regulatory regime by ensuring that the trustees of a funeral plan trust receive relevant, comprehensible and sufficient information about the assets and liabilities of the trust.

<p>F.1.1 Do you agree that technical actuarial work concerning the determination, calculation and verification of the assets and liabilities of the trust required by legislation or the FPA's rules should be in the scope of TAS 400?</p>
--

Work not in scope

Advice on investment

- 1.14 Trustees may seek advice to support them in making decisions on investment strategy, for example, when they are developing a statement of investment principles to be followed by the investment manager appointed to manage the assets of the trust.

- 1.15 The technical actuarial work on the valuation of liabilities and assets provides useful information to trustees to support their decisions on investment. However, other information is also important, for example, advice on the expected returns from assets and the risks and uncertainty associated with those returns. This information might be obtained from actuaries with the appropriate competencies or from other investment professionals.
- 1.16 We do not propose to include technical actuarial work relating to investment advice in the scope of TAS 400. We consider that that the proposals in TAS 100, supplemented with proposed requirements in TAS 400 for the communications to include a quantification of the expected future liability cash flows are sufficient to ensure that trustees get sufficient information in this area of work.

F.1.2 Do you agree that technical actuarial work relating to investment advice is adequately covered by TAS 100 and should not be in the scope of TAS 400?

Advice on pricing

- 1.17 The risk of inadequate pricing usually falls on the funeral director or the plan provider rather than the trust. Therefore, in respect of funeral plan trusts, we do not consider there is a high degree of risk to the public interest associated with this work.
- 1.18 To the extent that funeral plan pricing is technical actuarial work, we consider that such work will be adequately covered by TAS 100 and should not be included in the scope of TAS 400.

F.1.3 Do you agree that advice on pricing is adequately covered by TAS 100 and should not be in the scope of TAS 400?

Advice on plan providers' liabilities

- 1.19 The obligations of the trust are governed by the trust deed but the contractual obligations of the plan provider may differ, and will be governed by the terms of the contract between the plan provider and the plan holder.
- 1.20 The limited nature of the existing regulatory requirements and their focus on the assessment of the assets and liabilities of the trust could give rise to risks of mismatch and it has been suggested that the scope of TAS 400 should be widened to require some form of the assessment of the plan providers' liabilities. However, we do not consider it practical or appropriate for the FRC through the scope of TAS 400 to attempt to extend the remit of the actuary's role beyond the requirements under the RAO or the FPA's rules.
- 1.21 We consider that trustees should be made aware of any potential differences between the trust's obligations and those of the plan provider and have included a draft provision to this effect (see paragraph 2.19).
- 1.22 Any technical actuarial work for the plan provider on the financial implications of their obligations will be covered by TAS 100. Additionally, APS Z1 requires actuaries to report material shortfalls in the trust or in the trust's liabilities compared to the plan provider's liabilities to the plan provider, escalating to the auditor and the FPA where appropriate.

F.1.4 Do you agree that the scope of TAS 400 should not be extended to require an assessment of the plan provider's liabilities?

2 TAS 400 PROVISIONS

Introduction

- 2.1 In this section we discuss the proposed provisions of TAS 400.
- 2.2 The proposals reflect the output of the third stage of our risk assessment process in which we determined what additional requirements could mitigate the identified risks effectively.
- 2.3 In summary, the proposed provisions of TAS 400 are broadly the same as existing requirements in the Funeral Plans TAS with the proposed addition of four new requirements requiring communications to include:
- an explanation of the difference between actual and assumed experience over the period since the last assessment of the assets and liabilities of the trust;
 - an explanation of the obligations under the trust deed underpinning the estimate of the liabilities of the trust, and a description of where those liabilities may differ from the contractual obligations underlying the liabilities of the trust-based funeral plan;
 - a description of how the nature, term and characteristics of the liability cash flows compare with the cash flows from the current assets of the trust; and
 - an indication of the risks to the financial position of the funeral plan trust over an appropriate time period.
- 2.4 As with TAS 100, we have not included much of the supporting text in the existing TASs which provided background information and guidance.
- 2.5 All provisions in TAS 400 apply to all technical actuarial work in the scope of TAS 400 and support the principles in TAS 100.

Assumptions

- 2.6 Provision 3.3 of TAS 100 requires communications to state the material assumptions and describe their rationale. For work within the scope of the Specific TASs, we consider that for material assumptions communications should go one-step further, and describe how the assumptions have been derived.
- 2.7 For mortality assumptions we would expect this to cover the derivation of both base rates of mortality and future projections. Currently paragraph D.2.13 of the Funeral Plans TAS requires separate assumptions to be used for base rates of mortality and improvements.
- 2.8 Additionally, we are concerned that communications are not always as clear as they might be on specific assumptions for funeral cost inflation, the expenses of the trust and the tax position of the trust.

2.9 We therefore propose to include the following provision in TAS 400:

Communications shall explain the derivation of the discount rate, mortality (base rates and projections), funeral cost inflation, expense, tax and other material assumptions.

2.10 The current Funeral Plans TAS requires that mortality assumptions reflect the current plan holders of the funeral plan trust.

2.11 We therefore propose the following provision which are based on paragraph D.2.14 of the Funeral Plans TAS:

Assumptions for base rates of mortality shall reflect the current plan holders of the **funeral plan trust**.

2.12 Work within the scope of TAS 400 is repeated at regular intervals – assessments under the ROA are required at least once every three years and the FPA requires annual assessments.

2.13 We consider it important that trustees understand how the actual experience of the trust over the period between assessments compares with the assumed experience used to produce the estimates of the liabilities (and if applicable, the assets) of the trust.

2.14 We therefore propose the following new provision:

Communications shall provide an explanation for any difference between the actual experience emerging over the period since the previous exercise (if one exists) carried out for the same purpose with that assumed in that previous exercise.

2.15 Provision 5.4 of TAS 100 requires communications to include a comparison of the results of the previous exercise carried out for the same purpose with an explanation of any differences. Provision 3.4 of TAS 100 requires an explanation of any changes to the assumptions and description of any change in the rationale underlying the assumptions used. Furthermore, provision 4.4 of TAS 100 requires an explanation of any changes to the measures or methods used from the previous exercise.

2.16 We consider it also important that trustees understand the impact of the changes in the assumptions, measures and methods on the estimates of the liabilities (and if applicable, the assets) of the trust. This is currently covered by the requirements of the Funeral Plans TAS at paragraph D.3.1.

2.17 We therefore propose the following provision on changes in assumptions which builds on the requirements of TAS 100:

Communications shall quantify the effect on results of any change in assumptions since the previous exercise (if one exists) carried out for the same purpose.

Models

2.18 Additionally, we propose the following provision on changes in measures and methods:

Communications shall quantify the effect on results of any change in each of the **measures** and **methods** since the previous exercise (if one exists) carried out for the same purpose.

Estimating the value of liabilities

- 2.19 Trustees should be clear about the obligations under the trust deed that give rise to liabilities for the trust. In order to address concerns about the potential mismatch between the trust's liabilities and the plan provider's contractual obligations, we propose the following new provision:

Communications shall explain the obligations under the trust deed underpinning the estimate of the liabilities of the **funeral plan trust** and describe where the liabilities of the **funeral plan trust** may differ from the liabilities of the trust-based funeral plan.

- 2.20 In estimating the value of the liabilities of a funeral plan trust required to be calculated by the RAO and the FPA, judgement should be exercised in order to determine an appropriate allowance for adverse risk and uncertainty concerning the liability cash flows. Any allowance might depend on factors such as the nature and term of the investments of the trust and uncertainty concerning mortality improvements and funeral cost inflation.

- 2.21 In the interests of transparency, we propose to retain the requirement currently covered by paragraph D.4.1(a) of the Funeral Plans TAS. The proposed provision in TAS 400 is:

Communications shall explain how adverse risks to, and uncertainty in, the liability cash flows have been taken into account in the estimate of the liabilities of the funeral plan trust.

- 2.22 There is no regulatory requirement for a prudent estimate of the liabilities of a funeral plan trust to be produced. Moreover, the assumptions and measures that are used are a matter of judgement for the actuary performing the work. The work differs in these respects from the estimation of liabilities for insurers and pension schemes where additional capital is required to cover adverse deviations or where often assumptions are required to be chosen prudently. Additionally, the boards of insurers and trustees of pension schemes are responsible for setting the assumptions.

- 2.23 Trustees should understand the degree of any allowance for adverse risk and uncertainty that has been included in any estimate of the value of the liabilities so that they can make good decisions concerning the management of the trust. It is also important that any change in the allowance is explained to them.

- 2.24 The following proposed provision is an amended version of the existing requirement at paragraph D.4.2 of the Funeral Plans TAS:

Communications which include an estimate of the value of the liabilities of the **funeral plan trust** which is not a best estimate shall include a best estimate of the value of those liabilities; and an explanation of the change to the relationship between the estimate and the best estimate from the previous similar and related exercise, if any.

- 2.25 The trustees of a funeral plan trust usually have the discretion to apply any surplus arising of the value of assets over the value of liabilities to increase

amounts payable from the trust to meet the cost of funerals. This provides protection to the plan holder from the impact of inflation on funeral costs in the period between the date of the pre-payment and the funeral pre-payment purchases.

2.26 We consider it is important that trustees understand what allowance has been made for such discretionary increases in any estimate of the value of the liabilities of the funeral plan trust. This is currently covered by paragraph D.4.1(b) of the Funeral Plans TAS.

2.27 We have retained this requirement in TAS 400 with the following provision:

Communications shall explain any allowance for discretionary elements in the amounts payable from the funeral plan trust in the estimate of the liabilities of the funeral plan trust and how the allowance has changed since the previous exercise (if one exists) for the same purpose.

Illustrating liability cash flows

2.28 Trustees should have sufficient information to understand the expected pattern of liability cash flows. This information will assist them to challenge the assumptions used in the estimate of the liabilities. Where appropriate, we also consider that trustees should understand the potential impact on the liability cash flows of different assumptions on new business.

2.29 Paragraph D.4.3(a) of the Funeral Plans TAS currently requires a quantification of the liability cash flows expected to arise in the first ten years following the effective date of the estimate. We propose amending the requirement so that a quantification of cash flows over an appropriate period is provided with an explanation of the choice of time period.

2.30 Additionally, we propose a new requirement that, where appropriate, cash flow projections are provided assuming the funeral plan trust is closed to new business and assuming it is open to new business. We consider that this additional information will assist trustees in understanding the extent of any cross-subsidies across different groups of plan holders.

2.31 The proposed provision in TAS 400 is:

Communications shall quantify the liability cash flows expected to arise in an appropriate period following the effective date of the estimate of the liabilities of the **funeral plan trust** and explain the time period chosen. Where appropriate, the quantifications shall show both the liability cash flows assuming the **funeral plan trust** is closed to new business and assuming it is open to new business.

2.32 In line with the current provision at paragraph D.4.3(b) of the Funeral Plans TAS we propose the following provision:

Communications shall explain how the estimate of the liabilities of the **funeral plan trust** is derived from the liability cash flows.

2.33 We also consider it is important that trustees have an appreciation of the cash flows expected from the assets held in the trust in respect of those liabilities so they can understand how the future asset cash flows will cover the liabilities and any reinvestment or liquidity risk.

2.34 We therefore propose the following new requirement:

Communications shall describe how the nature, term and characteristics of the liability cash flows compare with the cash flows from the current assets of the **funeral plan trust**.

Estimating the value of assets

2.35 We do not consider that our standards should require that particular types of measures are used to estimate the value of the assets. However, it is important that the trustees are provided with an explanation of the measures used and the reasons for their selection so that they can effectively challenge any judgements made.

2.36 This is currently covered at paragraph D.4.5 of the Funeral Plans TAS and we propose to retain the requirement in TAS 400 as follows:

Communications shall include an explanation of, and a rationale for, the **measures** used to quantify the value of the assets; and if the **measures** used are not fair value **measures**, an estimate of the fair value of the assets.

Risk and Uncertainty

2.37 Provision 5.5 of TAS 100 requires that, for each material risk or uncertainty faced by a funeral plan trust in relation to work being reported on, communications should state the nature and significance of the risk and explain the approach taken to it.

2.38 In order for trustees to understand the nature of the risks and the uncertainty attaching to any estimates of liabilities, we consider that they should be shown the effect of adverse scenarios. This information should enable the trustees to make better risk management decisions. For example, adverse scenarios might affect the amount and timing of the liabilities or the ability of the current assets to meet the full amount of liabilities as they fall due. This is currently covered at paragraph D.4.6 of the Funeral Plans TAS.

2.39 We also consider that trustees should have sufficient information to enable them to understand the factors and events that could threaten the financial position of the trust over a suitable time horizon. It is important the trustees appreciate the risks inherent in the trust and how they might evolve over time so that they can give due consideration to how to mitigate those risks.

2.40 Management actions may serve to change or mitigate risks and any such actions that have been assumed in the information about the future progress of the trust should be described.

2.41 We therefore propose the following provision:

Communications shall include sufficient **actuarial information** to enable the user to understand the sensitivity of the financial position of the **funeral plan trust** to **material** risks. The information that is provided shall include an indication of:

- the impact of adverse scenarios on the value of liabilities at the valuation date; and

- the potential impact of adverse scenarios on the financial position of the **funeral plan trust** over an appropriate time period with an explanation of the choice of the time period and a description of any assumptions about management actions.

F.2.1 Do you agree with the proposed text of TAS 400 as a means of implementing the proposals presented in this annex?

3 IMPACT ASSESSMENT

Introduction

- 3.1 In this section we consider the impact of our proposals on TAS 400 including the resulting benefits and costs; our analysis focuses on the impact of our proposals on work carried out by members of the IFoA.

Context

- 3.2 The assets of funeral plan trusts exceed £1.7 billion and there are at least 700,000 plan holders. The number of trust-based plans has grown rapidly in recent years and plan providers are optimistic about the future for their businesses³.
- 3.3 The average duration of a plan is currently between five and ten years although in recent years there has been an increase in younger people purchasing funeral plans. The current cost of a new plan is between £3,000 and £4,000.

Benefits

Users and the public interest

- 3.4 TAS 400 has been drafted following a thorough risk assessment process which identified work which has a high degree of public interest. As a result the work in the scope of TAS 400 is of high importance to trustees and are key elements of the regulatory regime for trust-based funeral plans.
- 3.5 We consider that TAS 400 in conjunction with TAS 100 will:
- assist trustees by ensuring that actuarial information provided is relevant, comprehensible and sufficient to support decisions about the funeral plan trust and includes information on risk and uncertainty.
 - support trustees complying with the requirements of the ROA and where appropriate, the rules of the Funeral Planning Authority.

Practitioners

- 3.6 Practitioners will benefit from improvements to the structure, style and content of the TASs which will result in a simpler framework, reduced volume of regulatory material and standards which are easier for practitioners to use and understand.

Costs

- 3.7 The work proposed to be in the scope of TAS 400 is currently in the scope of the Funeral Plans TAS and the Generic TASs on data, modelling and reporting.

³ Figures provided by Funeral Planning Authority

- 3.8 Under our proposals, this work will be subject to TAS 400 and TAS 100. The proposed changes to the requirements effected by TAS 400 and TAS 100 should not lead to material changes for this work. As noted in paragraph 2.4 there are few additional requirements in TAS 400 when compared with the existing Funeral Plans TAS. We consider that the additional costs of complying with these new requirements will be offset by the reduced requirements brought about by the replacement of the Generic TASs with TAS 100.
- 3.9 Evidence collected in our post-implementation review indicated that the transitional costs of implementing the TASs ranged between very small amounts and 10% of the actuarial costs of the relevant organisation. The costs depended on several factors including the nature of the work and the size of the firm. The costs were proportionally higher for smaller organisations.

Overall

- 3.10 We recognise that moving to any new regulatory framework will result in costs to amend systems and processes to reflect the revised framework. However, for areas of work within the scope of the Funeral Plans TAS, we consider that the longer term benefits of adopting a more efficient structure by replacing the TAS D *Data*, TAS M *Modelling* and TAS R *Reporting* with TAS 100 and streamlining both TAS 100 and TAS 400, will offset any transitional costs, and potentially result in long-term efficiencies.
- 3.11 Our post-implementation review of the TASs indicated that the long-term costs of complying with the TASs are not significant. We therefore consider that the long-term costs of complying with TAS 400 will similarly not be significant.
- 3.12 We consider that the changes effected through TAS 400 will not be as costly as the implementation of the current TAS framework as this is largely a review and update exercise rather than a fundamental change in the framework.

F.3.1 Do you agree that the replacement of the Funeral Plans TAS with TAS 400 will not lead to disproportionate costs?

F.3.2 Do you have any comments on our analysis of the impact of the changes set out in section 3?

4 INVITATION TO COMMENT

Questions

- 4.1 The FRC invites the views of those stakeholders and other parties who wish to comment on the content of this document. In particular, we would welcome responses to the questions below. Please provide reasons for your response and provide an alternative approach where you disagree with our proposals.

Questions asked in the covering Consultation *Revised Specific TASs (for information)*

- C.2.1 Do you have any comments on the risk assessment process described in paragraphs 2.2 to 2.15?
- C.2.2 Do you have any comments on our proposed approach to risk monitoring (paragraphs 2.16 to 2.21)?
- C.3.1 Do you agree that the design principles described in paragraph 3.3 will help to ensure that the Specific TASs form a coherent and risk-focussed set of requirements that apply alongside TAS 100?
- C.3.2 Do you agree with the proposed style and structure of the revised Specific TASs outlined in paragraphs 3.8 to 3.15?
- C.3.3 Do you have any comments on draft *Glossary of defined terms used in FRC technical actuarial standards*?
- C.6.1 Do you have any comments on proposed implementation of the revised Specific TASs?

Annex 3: TAS 400: Funeral Plans

- F.1.1 Do you agree that technical actuarial work concerning the determination, calculation and verification of the assets and liabilities of the trust required by legislation or the FPA's rules should be in the scope of TAS 400?
- F.1.2 Do you agree that technical actuarial work relating to investment advice is adequately covered by TAS 100 and should not be in the scope of TAS 400?
- F.1.3 Do you agree that advice on pricing is adequately covered by TAS 100 and should not be in the scope of TAS 400?
- F.1.4 Do you agree that the scope of TAS 400 should not be extended to require an assessment of the plan provider's liabilities?
- F.2.1 Do you agree with the proposed text of TAS 400 as a means of implementing the proposals presented in this annex?
- F.3.1 Do you agree that the replacement of the Funeral Plans TAS with TAS 400 will not lead to disproportionate costs?
- F.3.2 Do you have any comments on our analysis of the impact of the changes set out in section 3?

F.4.1 Do you have any comments on the text of the exposure draft of TAS 400?

F.4.2 Do you have any further comments on the proposals in this consultation?

Responses

4.2 A [template for responses](#) is available on the FRC website.

4.3 Comments should be sent electronically to FuneralPlans@frc.org.uk. Comments may also be sent in hard copy form to:

The Actuarial Policy Team
Financial Reporting Council
8th Floor
125 London Wall
London
EC2Y 5AS

4.4 Comments should reach the FRC by **5 August 2016**.

4.5 All responses will be regarded as being on the public record unless confidentiality is expressly requested by the respondent. A standard confidentiality statement in an e-mail message will not be regarded as a request for non-disclosure. We do not edit personal information (such as telephone numbers or email addresses) from submissions; therefore only information that you wish to publish should be submitted. If you are sending a confidential response by e-mail, please include the word “confidential” in the subject line of your e-mail.

4.6 We aim to publish non-confidential responses on our website within ten working days of receipt. We will publish a summary of the consultation responses, either as a separate document or as part of, or alongside, any decision.



Financial Reporting Council

8th Floor
125 London Wall
London
EC2Y 5AS

+44 (0)20 7492 2300

www.frc.org.uk