

**Minutes of a meeting of the Actuarial Council held on Tuesday 14 January 2014 in the Boardroom at Aldwych House, 71-91 Aldwych, London, WC2B 4HN**

**Present:**

Olivia Dickson	Chair of Council
Keith Barton	
Angela Darlington	
David Hindley	
Howard Jacobs	
Paul Johnson	
Martin Miles	(to agenda item 3)

**Observers:**

Rosemary Beaver	Lloyd's of London
Paolo Cadoni	Prudential Regulatory Authority (PRA)
Seamus Creedon	Actuarial Association of Europe (EEA, formerly GC)
Jane Curtis	Institute and Faculty of Actuaries (IFoA)
Stuart Hicks	Financial Conduct Authority (FCA)
Lee O'Rourke	Her Majesty's Treasury (HMT)
Rosemary Ohen	Department for Work and Pensions (DWP)
Chinu Patel	The Pensions Regulator (tPR) (in place of Nigel Peale)

**In Attendance:**

Siân Barr	Project Manager, Actuarial Oversight, FRC
Francesca Chittenden	Council Secretary, FRC
Faye Dyce	Project Manager, Actuarial Policy Team, FRC
Robert Inglis	Project Director, Actuarial Policy Team, FRC
John Instance	Project Director, Actuarial Policy Team, FRC
Paul Kennedy	Director, Actuarial Policy, FRC
Melanie McLaren	Executive Director, Codes & Standards, FRC (from agenda item 2)
Marian Williams	Codes & Standards Director, FRC (agenda items 8-13 only)
Natasha Regan	Project Director, Actuarial Policy Team, FRC
Henry Johnson	Lloyd's of London (agenda item 2 only)
Jerome Kirk	Lloyd's of London (agenda item 2 only)

**1. Welcome and apologies for absence**

- 1.1 The Chair welcomed the observers to the meeting; all attendees present provided a brief introduction.
- 1.2 Apologies were noted from Martin Bradley, Ashok Gupta and Joanne Livingstone (Council Members).

## **2. Monitoring Statements of Actuarial Opinion – Presentation from Lloyd’s**

2.1 The Council received a presentation from Henry Johnson (HJ) and Jerome Kirk (JK) of Lloyd’s which detailed the process developed by Lloyd’s to monitor and review Statements of Actuarial Opinion (SAOs). The Council noted:

- the requirements for SAOs and supporting guidance;
- the process by which Lloyd’s undertakes reviews;
- detail of the scoring system used by Lloyd’s to review SAOs;
- the resource requirements of undertaking reviews;
- the process for providing feedback on the review to the producer of the report; and
- the benefits of the review process.

2.2 Following the presentation there was a question-and-answer session. It was clarified that Lloyd’s also undertakes a wider review of the underlying actuarial information, and that the review process described at the meeting is a review of the written SAO report. It was also noted that:

- the intended user of the report is the managing agent;
- the accuracy and quality of the underlying work does not necessarily reflect the scoring of a SAO report reviewed through the process described but it does help focus the mind of the syndicate actuary;
- whilst the questionnaire used to review SAO reports does adopt a ‘checklist’ approach there is an element of judgement where the reviewer is asked to provide an opinion on specific areas of the report, however, Lloyd’s does provide guidance to assist the reviewer in making the necessary judgements;
- Lloyd’s is looking at developing best practice guidance on how to write up expert judgements as part of a wider project;
- If Lloyd’s identifies that an actuary is not complying with the TASs, action will be taken to address this.

## **3. Update from the November and December JFAR meetings**

3.1 Melanie McLaren (MM) informed the Council that there had been two constructive meetings of the JFAR since the last meeting of the Council; and that it was encouraging that an additional meeting to discuss the development of the shared actuarial risk map was to be arranged for February 2014. The Council noted that the JFAR would look at the level of monitoring of the quality of actuarial work once the work to develop a risk map was more advanced and it can be identified whether there are key areas of risk to the public interest that are not being addressed. The Council noted that whilst the monitoring of the quality of actuarial work is not a direct objective for the other bodies which sit on the JFAR, work is monitored indirectly in some areas through supervision.

## **4. Development of shared monitoring arrangements**

4.1 Siân Barr (SB) introduced a report which attached a draft paper for the JFAR. The draft paper set out an initial analysis of the findings of an engagement exercise undertaken to identify monitoring activities together with proposals for how to use the information collected. The Council was invited to comment on the categories of

actuarial work analysed, the monitoring or research priorities and the next steps to take to the JFAR. In considering the proposals it was noted that there is a need to ensure the FRC is clear on how the quality of actuarial work would be measured before steps to enhance the quality of actuarial work and to address concerns about the quality of actuarial work could begin.

- 4.2 The Chair commented that the FRC, as a standard-setter, might need to be able to explain how it had formed a view on the quality of actuarial work. The Chair suggested that the draft paper for the JFAR might be revised to include a context/scene-setting introduction which would highlight the benefits of achieving a collective view on the quality of actuarial work for each of the regulators involved with JFAR. Although the benefits of collecting monitoring information on the quality of actuarial work would vary for each of the regulators involved, ultimately, all on the JFAR have a shared purpose and interest in ensuring high quality actuarial work, even if it is not their direct objective.
- 4.3 MM reminded the Council that the FRC had previously considered whether or not to establish a monitoring function for actuarial work and had concluded that further information on the levels of monitoring undertaken by others and the associated risks relating to actuarial work would be needed before such a decision could be taken; MM added that the FRC is now collecting this information and would be in a position to address this question in due course.
- 4.4 It was noted that many professional firms monitor adherence to the Technical Actuarial Standards (TASs) internally. The Council noted that in response to the 2008 Professional Oversight Board review the IFoA is developing a voluntary quality assurance scheme for firms and that, in due course, this might be a source of information about the quality of actuarial work being undertaken.
- 4.5 The Council discussed whether or not the FRC should encourage the use of a grading approach to monitoring in order to promote the quality of actuarial work and compliance with the TASs. Whilst the Council identified a number of benefits for implementing a grading system the Council expressed the need to base any grading system on evidence and ensure that qualitative factors were adequately captured and scrutinised.
- 4.6 The Council was pleased to note that the PRA had recently produced a letter to be sent to firms participating in its ICAS+ process (which dovetails its current Individual Capital Adequacy Standards and Solvency II internal model assessments) specifying that they should explain how their ICAS+ report complies with the TASs.

## **5. Shared actuarial risk map**

- 5.1 Natasha Regan (NR) introduced a paper which set out three proposed FRC 'actuarial public interest risks' for discussion at the next JFAR meeting. NR informed the Council that the FRC has been co-ordinating the identification of risks to the public interest with the IFoA and other regulators. The Council noted that the risks proposed had been identified following discussion with the FRC's Actuarial Risk Sub-group, discussion with the FRC's Conduct Committee, brainstorming sessions with various

working groups of the IFoA and with regard to the FRC's mission statement and supporting strategies. The Council noted that the three proposed FRC risks would sit alongside twelve other risks that would be identified by the four other members of the JFAR.

- 5.2 Through discussion it was confirmed that the FRC risks should be risks related to work that is undertaken by actuaries or otherwise involving actuarial work, and may jeopardise the success of the FRC in achieving its mission 'to promote high quality corporate governance and reporting to foster investment', and the relevant supporting strategy that information is trustworthy and will contribute to informed decision making. It was suggested that the language used to describe the risks in the documentation be reviewed to make this classification clearer and place the emphasis on the output of actuarial work.
- 5.3 The Council noted the proposed criteria for the selection of the FRC's risks; it was confirmed that the requirement for the risk to have 'substantial actuarial content' is a reference to the use of actuarial techniques and/or the involvement of actuaries.
- 5.4 The Council discussed the proposed risks and commented on the broad scope of the three risks identified, in response NR confirmed that the risks were intentionally high level so as to enable the JFAR to undertake more detailed analysis to identify the particular pockets of risk within the broad areas identified.
- 5.5 Through discussion of the proposed risks the following observations were made:  
Modelling - the Council agreed that modelling should be included as an FRC risk and that the list of risks associated with modelling should be expanded to include:  
a) the adequacy of data;  
b) inadequate validation;  
c) the appropriateness of models and unintended consequences of models.  
The Council highlighted that there is a TAS for modelling; this is a mitigation tool indicating that there is perceived risk.  
Investments – the Council agreed that this risk should be included, and noted the relevance of this risk to the FRC mission statement and in recognising the increasing role of actuarial input to investment decisions, particularly around asset allocation for insurers' capital management and pension covenant management decisions.  
Financial reporting – following clarification that this risk would relate specifically to corporate reporting as the responsibility for regulating other aspects of financial reporting (such as regulatory reporting) sits elsewhere, the Council agreed that this risk should also be included as an FRC risk.

## **6. AS TM1 Version 4.0 Exposure Draft Consultation**

- 6.1 Faye Dyce (FD) introduced a paper which set out a revised version of AS TM1, draft advice to the FRC Board, and a draft feedback statement. FD also introduced a graph which was tabled at the meeting and provided the Council with a comparison of the fixed interest yield and the adjusted index-linked gilt yield +3% rates from 1991 to 2013. The Council noted that the rates have been much closer since the Bank of England was granted independence and an inflation target in 1998.

- 6.2 The Chair drew attention to the issues which had been identified during the consultation and the corresponding changes that had been proposed to AS TM1. The Council noted that respondents to the consultation had called for clarification that where a provider assumes a lump sum, it should be disclosed in real terms alongside the illustrated pension. The Council was content with the change made to AS TM1 to accommodate this request. The Council noted the concerns expressed that the proposals set out in the ED could result in a) significant costs being incurred by some firms; and b) inconsistency between the figures presented in point of sale information and the figures presented in SMPI reports a year later. In light of those concerns the Council discussed the proposal that providers should be allowed to use the FCA basis for the interest rate for a non-increasing pension if they so wished. Through discussion the following observations were made:
- respondents to the consultation wanted the FRC and FCA to agree a consistent approach;
  - as there is uncertainty about future European directives for Packaged Retail Investment Products (PRIPs) and pension schemes it may be unwise for the FCA to make changes ahead of any change that may be mandated by Europe;
  - the current and historical relationship between fixed interest gilt yields and index linked gilts + 3% appears unlikely to have a significant impact on resultant values in statements. It is difficult to accept the cost–benefit argument as the cost will depend on the flexibility of the system used by firms; however, for many the cost is likely to be small;
  - the Council has previously advised the FRC Board that it should not adopt proposals for the sake of consistency where alternative options are more intellectually sound, and on these grounds, the FRC basis is to be preferred;
  - the concern over consistency between SMPIs and point of sale projections needed to be put in the context that even when identical bases are used the figures presented in SMPIs will always be different from those presented in point of sale projections because the purpose and context of the illustrations differ;
  - any difference in the basis for the interest rate determining the annuity rate, will be less significant in the SMPI than other factors such as the accumulation rate.
- 6.3 In conclusion the Council considered that the proposal to allow providers to use the FCA basis for the interest rate for a non-increasing pension should be included as an alternative to using the FRC basis in the revised version of AS TM1. It was agreed that the advice would highlight that while consistency is an important relevant consideration, any flexibility in this instance must be reconciled with the Council's previous position, and that a pragmatic approach was acceptable on this occasion because the impact of using the alternative basis appeared not to be material to the pension illustration. The Council reiterated its earlier position that considerations of consistency will not usually be allowed to override proposals that are more intellectually sound.
- 6.4 Accordingly, the Council confirmed its advice to the Board that the FRC should publish version 4.0 of AS TM1 as presented, to be effective from 6 April 2014. The Council authorised the Sub-group Chair and the Actuarial Council Chair to support the FRC in finalising the Council's formal advice, the final version of AS TM1 and the feedback statement in accordance with the points raised.

6.5 The Council noted that the JFAR had held an initial discussion at its December meeting in relation to the concerns raised by the Council and Actuarial Stakeholder Group in relation to SMPs. The JFAR had recognised that further work in the area is required and noted that some issues would be considered as part of the broader review of AS TM1 later in 2014.

## **7. Joint consultation draft – actuarial standard-setting framework**

7.1 Robert Inglis (RI) introduced a paper which set out the latest version of the proposed Technical Actuarial Code (the Code). RI sought the Council's views on the content and scope of the Code and the approach to the proposed consultation. The Council noted that the FRC's Standards Framework Sub-group had met twice since the last meeting of the Council and that there had also been a working group meeting in December at which 14 practitioners had discussed the proposed framework.

7.2 The Council noted that the section of the draft Code relating to 'scope' was work in progress and that further consideration was required to make it clearer to whom the Code is applicable. In discussing the content and scope of the Code the Council:

- welcomed the opening statement to the scope of application section, which explains that the Code is intended to be broadly applicable, although it is up to regulators and contracting parties to determine whether or not the Code should be applied in particular circumstances;
- welcomed the general approach to defining the obligations of IFoA members by reference to whether they are providing services in a professional actuarial capacity, subject to further consideration by the Sub-group including whether it is necessary to describe what the technical judgement and actuarial skills referred to in the definition are;
- suggested that criteria used to describe the services which would be treated as provided in a professional actuarial capacity might be reviewed to reduce the extent of overlapping;
- suggested further consideration should be given to the communication section with a view to reducing the number of items listed under the heading.

7.3 The Council noted that the FRC had discussed the draft consultation outline with the IFoA's Regulation Team and that the proposals were due to be considered by the IFoA's Regulation Board at the end of the month. In considering the proposals the Chair expressed disappointment that there was not more reference to the vision statement previously agreed by the Council and underpinning the Code, in response, RI confirmed that this would be addressed in the proposed chapter 4 of the consultation paper.

7.4 The Council endorsed the proposed approach to the joint consultation and noted that the FRC's Codes & Committee (CSC) would be asked to consider the draft Code and consultation proposals at its meeting on 15 January. The Chair cautioned that the CSC may suggest separating elements of the consultation to reinforce the independence of the FRC from the IFoA.

## **8. International Standards consultation responses**

8.1 John Instance (JI) introduced draft FRC responses to the following consultations and summarised the rationale underpinning each of the draft responses:

- a) Actuarial Association of Europe (AAE) - GCASP1 Exposure Draft
- b) IAA - ISAP 3 exposure draft
- c) IAA - ISAP 4 Statement of intent

The Council noted the rationale and expressed agreement with the substance of the three draft responses as set out.

8.2 The Council noted that the draft responses would be shared with the UK Forum for International Actuarial Standards before submission to the respective organisations.

## **9. tPR consultation: Regulating defined benefit pension schemes**

9.1 RI introduced a paper which set out a summary of the proposals issued for consultation by tPR and a draft approach on which the FRC should base its response.

9.2 The Council noted the detail set out in the paper. It was agreed that the FRC should support the proposed integrated approach to scheme funding, investment and covenant management and that the FRC should not only suggest that the Code of Practice refers to relevant professional standards but request this. The Council also agreed that the response should highlight relevant areas of the FRC Corporate Governance Code.

9.3 The Council discussed in detail the implications of the proposals on actuaries; through discussion the following observations were made:

- whilst there is broad support for the proposals there is some concern over the length of the material and the number of additional requirements, which, while not new for larger schemes, may be an issue for smaller schemes that may not have sufficient resources available;
- the Council expressed concerns that the proposals might create an expectation from a regulatory perspective that all qualified actuaries are experts in covenant management when this is not the case, this concern will also be greater for smaller schemes;
- whilst the proposals would not necessarily change the role of the actuary, the proposals might result in an extension of the work of the actuary;
- the proposals raise ethical considerations which the IFoA will be required to address and should also be discussed by the Actuarial Stakeholder Group.

9.4 The Council discussed whether the FRC and IFoA should consider the concerns identified in relation to the monitoring of actuarial work for smaller schemes and concluded that this concern should be addressed by tPR. However, it was noted that the proposals could be fed in to the actuarial risk map. In response to the points raised regarding the impact on small schemes Chinu Patel (CP) explained that tPR would not expect smaller schemes to implement complex processes and that tPR would place less focus on the smaller firms in regulatory supervision terms and provide greater education.

- 9.5 The Council noted that the principles in the Pensions TAS on scheme funding would need to be reviewed in light of the consultation; and that the FRC/IFoA will have to determine whether there should be any technical guidance for actuaries on funding, investment and covenant assessment. MM informed the Council that the FRC would use the principles developed by the FRC's Codes and Standards Committee to determine if there is a need for change, or a need for guidance, and that proposals would be brought to the Council to consider in due course.

## **10. Director's Report**

- 10.1 The Council noted a report which provided an update on FRC activities relevant to actuarial work since the last meeting of the Council.
- 10.2 Paul Kennedy (PK) informed the Council that the draft FRC Plan and Budget 2014/15 was currently out for consultation and drew the Council's attention to the appendix which set out the Actuarial Policy Team's provisional objectives for 2014-15 based on the draft FRC Plan.

## **11. Stakeholder engagement**

### **Annual Actuarial Stakeholder engagement review**

- 11.1 The Chair summarised the paper which set out findings of a stakeholder engagement review led by the FRC. The Council noted that project CAPRI and the establishment of the Joint Forum for Actuarial Regulation had had a positive impact on engagement and relationships with stakeholders.
- 11.2 PK highlighted that the FRC's engagement with a number of stakeholders had improved since 2012 and that whilst the engagement with a small number of major stakeholders was currently listed as amber ('some shortfall in planned levels of engagement'), for 2013 as a whole steps had already been or were being taken to improve those relationships.

### **IFoA Observer report**

- 11.3 Jane Curtis (JC) introduced the IFoA report and provided an oral update on matters referred to in the report. The Council noted that the IFoA planned a consultation on 'APS X1: Applying Standards', and that work in relation to Quality Controls at firms was progressing. The Council also noted that the IFoA Strategy day scheduled for December had been postponed to Q1 2014.

### **Other observer reports**

- 11.4 The other observer reports were taken as read and noted.

## **12. Minutes of the Actuarial Council meetings held on 12 November 2013 and rolling actions**

- 12.1 The minutes of the Council meeting held on 12 November 2013 were approved as an accurate record of the meeting.

12.2 The Council noted the status of the actions listed on the rolling action log. JC undertook to liaise with IFoA colleagues about arrangements for an FRC observer to attend meetings of the IFoA standards framework review working group.

### **13. Council effectiveness review debrief**

13.1 Marian Williams (MW) introduced the report and summarised the actions that had been agreed in response to the findings of the Council effectiveness review.

13.2 The Chair drew the Council's attention to the action log appended to the report; the Council noted that the majority of actions were to be addressed by the FRC staff but that the Chair would be arranging annual meetings with Members to discuss effectiveness on a one to one basis.

13.3 MW reported that work was on-going to establish principles for observers that would be applicable across all three FRC Councils. The Chair highlighted the concerns expressed through the effectiveness review in relation to the large number of attendees at Actuarial Council meetings and the constraints this places on discussion and the effectiveness of the meeting and confirmed that consideration as how best to address this was in hand.

### **14. Working groups review**

14.1 The Council noted the memberships of the working groups.

### **15. Forward Agenda**

15.1 The Council noted the forward agenda.