



Response to the Pensions Regulator consultation on Statement of Strategy

The Institute and Faculty of Actuaries (IFoA) is a royal chartered, not-for-profit, professional body. We represent and regulate over 32,000 actuaries worldwide, and oversee their education at all stages of qualification and development throughout their careers.

The Institute and Faculty of Actuaries (IFoA) welcomes the opportunity to respond to the Pensions Regulator's consultation on Statement of Strategy.

We have responded to each of the questions set out in the consultation document in the appendix. Our overall comments and observations on the proposals are set out below.

We note that the Statement of Strategy needs to fulfil two primary purposes:

- For trustees to be able to comply with their legal obligations under the new statutory requirements
- To provide TPR with the information it requires for its role in supervising the DB Funding requirements.

We do not believe the legislation requires any more than this, and we do not believe that trustees will choose to use the statement for broader purposes – such as risk management or member communication – where other, better tools are likely to be available for these purposes.

We also note that the Statement of Strategy will need to be completed by a wide range of schemes with very different circumstances and approaches. Trustees and employers will also not want to need to spend time and money on providing information that is not strictly necessary for the above purposes. We note in this respect that it is not just the very small schemes who will find the time and effort involved in producing the proposed information disproportionate.

We are therefore strongly of the view that the standard information request forming the Statement of Strategy should seek to proportionately fulfil the above purposes and no more. In our view the proposed information required in several respects goes well beyond this proportionate level, and we suggest that TPR reconsiders this approach.

As with the current TPR regulatory process for valuations, we would envisage TPR requiring only the information it needs to do an initial high-level review of the scheme's valuation outcome, with further details then being requested should this indicate that a deeper investigation is warranted. In our view, several of the items currently being requested would fall into this latter category, such that they would only be necessary for a small number of schemes. One area to highlight in this regard is the request for the provision of annual cashflows, split between membership categories, on several different bases. This is time consuming for actuaries to provide, even with good systems generating the underlying data, and goes well beyond the requirements set out in the regulations for the Statement of Strategy. It is also questionable that TPR should be seeking to obtain such an increased volume of data, at significant additional effort and costs to schemes (and potentially TPR), at a stage when scheme funding levels are generally at very healthy levels and a large

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proportion of schemes are heading towards securing members' benefits through a buy-out within a short time.

We support the production of a set of pre-defined templates rather than schemes producing their own formats, although there need to be sufficient templates and/or input options to cover a wide range of scheme situations to avoid unnecessary information being sought. We do not feel the four scenarios currently identified are enough. As an example, the requirements in respect of covenant and investment risk could be significantly simplified where schemes are well funded and do not have a significant reliance on covenant to support investment risk. Other examples of schemes that would not neatly fit the templates include cash balance schemes and shared cost schemes, along with schemes that would otherwise fit the fast-track route but fall into the bespoke category solely due to a lack of affordability.

We note that several items of data requested in the list of data are currently provided to TPR in valuation submissions and scheme returns. It would be beneficial for TPR to carry out a full review of the information it seeks from trustees before introducing the new statement of strategy request in order to definitively avoid introducing a duplication of costs and effort.

Finally, it is important that the templates and any accompanying notes and guidance accurately reflect the legislation and are carefully drafted and tested in advance. We are already aware of significant difficulties being introduced year on year to the scheme returns process where new guidance is unavailable or unclear and we would not want to see this extended to a very large number of data items. Also, in some cases, we believe the Statement of Strategy requirements have been paraphrased in a manner that is misleading. As an example, there is an assumption that technical provisions and low dependency discount rate assumptions will be the same post the relevant date – while this is likely to be true for many schemes, we do expect that some schemes will have “consistent” technical provisions and low dependency assumptions, as required by the legislation, rather than “identical assumptions”.

Yours faithfully

Debbie Webb, on behalf of the IFoA Pensions Board.

Appendix - Response to consultation questions

Section 1: Our approach to the statement of strategy

Question 1: To what extent do you agree that our proposal to adjust the information required of smaller schemes as outlined in the document is pragmatic and proportionate?

Agree.

If anything, we believe that some of the more pragmatic suggestions for small scheme (for example, on how the scheme maturity is expected to develop) should be adopted for all schemes in preference to the more onerous requirements proposed. There are also areas where we do not agree that the information requested is 'pragmatic and proportionate'.

Question 2: To what extent do you agree with the two definitions proposed for smaller schemes depending on whether we are requesting actuarial or investment information?

The definitions appear reasonable, although the asset definition is not generally used to define a small scheme in legislation.

Question 3: To what extent do you agree with our proposal to have pre-defined templates for the statement of strategy to help trustees provide information that is proportionate, relevant and specific to the circumstances of their schemes?

Broadly agree with the concept, if not the implementation proposed.

Since the purpose of the statement is to comply with the legal requirements and provide information to TPR, we agree that pre-defined templates are an appropriate way forward. As noted above, we do not believe trustees are likely to use the statement for other purposes (although if the aim is that the Statement is more widely meaningful and useful, we believe there would need to be additional flexibility in its completion).

The information that needs to be included in the statement must however be consistent with the requirements in legislation and should include sufficient flexibility to enable schemes to appropriately record their decisions and agreement. In our view, this may mean adding further optional open boxes for input on many items, so that schemes have an alternative where none of the pre-populated options quite fits their circumstances. Otherwise, the exercise will become tick-box and the overall picture for a scheme may be difficult for TPR to determine.

There also need to be sufficient templates to cover most scenarios, and we are not sure the identified four are enough for this purpose. We have provided some examples – e.g. where well-funded and derisked schemes could adopt a lighter and more pragmatic approach to some of the information requested. Consideration could also be given to providing a template specifically for open schemes where new accrual is expected to be substantial (e.g. because they are open to new entrants).

Finally, further consideration may be needed for more unusual schemes – such as purely cash balance schemes or shared cost schemes, or schemes whose only deviation from fast track is due to affordability (where higher data collection costs could directly impact the security of members' benefits).

Question 4: To what extent do you agree with the benefits we expect to see by providing a pre-determined statement of strategy?

Broadly agree, although as noted it is important that the templates do not require detail and information that goes beyond what is legally required and what is essential for TPR's oversight role.

Question 5: To what extent do you agree with the key differences in the information we ask for between the four proposed templates?

Partially agree.

Also see our comments on Q3 above.

For 'Bespoke' schemes in particular, the information required appears disproportionate in some instances. We do not believe full cashflows should be required for any schemes, and we suggest that the approach outlined for smaller schemes – relying on the scheme actuary's calculations of maturity over time to evidence how the scheme is expected to mature – would be an appropriate way forward for all schemes. Indeed, unless TPR plans to carry out an approximate valuation and maturity calculation for every scheme – which seems totally disproportionate to the risk it needs to manage – it is difficult to see why voluminous cashflow inputs would be justified or necessary.

Question 6: Are there any scenarios that the proposed four templates are not suitable for?

See above.

As previously noted, we believe the number of templates may well need to get extended so that what is asked for is appropriate and proportionate to each scheme's circumstances in order to minimise the collection of unnecessary and disproportionate information. Sufficient flexibility to enter alternatives to the pre-selected options will also be necessary to ensure individual scheme circumstances can be covered.

Question 7: To what extent is the example Bespoke template a clear tool that supports trustees' long-term planning and risk management and facilitates engagement between trustees, their employer and TPR?

We do not anticipate that many, if any, schemes will use the statement of strategy itself as a long term planning and risk management tool, or a tool for communication other than with the Regulator. Clearly there will be much engagement between trustees and sponsors on the key content of the statement of strategy, though we anticipate much of this will have occurred before the statement is formally drafted and documented as part of the final regulatory submission process.

Question 8: Do you have any further comments on our general approach to the statement of strategy template?

Please provide any considerations you have on particular challenges, the impact these may have, any unintended consequences and any proposed alternatives you have.

Please see our comments in the covering letter and the points covered above.

A further point is that it is really important that the templates don't misstate or incorrectly paraphrase the underlying legal requirements, and that schemes have the flexibility to reach agreement and document any strategy permitted by the law, even if some of those are not the Regulator's preferred approach (clearly, for Fast track, the Regulator can be more rigid given its purpose, although the constraints of fast track should themselves allow TPR to seek less information). Two examples to highlight in this respect are:

- the Government pointed out clearly in its consultation response that "the Regulations do not constrain actual investments and even mature schemes can invest in a wide range of assets". It is therefore quite possible that for some schemes there will be differences between the investment strategy documented in the FIS and the actual investment strategy followed, with resulting commentary required in part 2 of the statement. The templates should include the flexibility for this approach.
- The legal requirement is not for all the assumptions (including the discount rate) to necessarily be the same after the relevant date for the technical provisions and low dependency basis, but instead that they are "consistent". The templates should therefore anticipate that schemes may (and are permitted by legislation to) choose different assumptions for each of these.

Section 2: Part 1: funding and investment strategy

Question 1: To what extent do you agree that the long-term objective options (buy-out, run-off, move to a superfund or alternative consolidator) capture most long-term objectives for a scheme?

We agree that this broadly covers the long-term objectives for most schemes.

We understand that there have been concerns expressed about whether sponsors will be comfortable formally agree “buy-out” as their option, as some auditors may take the view that this will require different accounting treatment in the company’s accounts. We therefore suggest wording is agreed for this option which would not have such unintended consequences or otherwise discourage trustees and employers from agreeing to this.

We also anticipate that some negotiations will lead to more nuanced or unusual objectives, so it is also important that there is an “other” box for schemes whose objectives do not neatly fit into the main categories identified above. An example would be schemes whose shorter term objective might be to run on, but whose longer term objective might be buy-out. This might be a more popular choice for schemes that are already close to significant maturity but not yet funded at a buy-out level.

Question 2: To what extent do you agree that the three broad categories of growth, matching and hybrid assets gives sufficient breakdown of the low dependency investment allocation?

Broadly agree.

We note that this is very high level, but appreciate that this high level approach respects the trustees’ powers regarding investment decisions. We do think guidance will be needed, especially for the “hybrid” category, as we could otherwise envisage two schemes with very similar underlying investments choosing to record them quite differently, depending on their individual approach to what is “hybrid”.

Question 3: To what extent do you agree that it is sensible to include all three funding bases (low dependency funding, technical provisions and buy-out)?

Agree that total liabilities on all three bases are easily available following a valuation and that it would be sensible to include them, although noting that some bases may be the same for some schemes.

It should not however be necessary to disclose all assumptions and/or the cashflows on each basis.

Question 4: To what extent do you agree that the standard wording in the proposed statement of strategy template is adequate to outline the funding journey plan?

Agree.

As stated above, it is not a requirement of the FIS regulations for the technical provisions discount rate to converge with the discount rates used in calculating the liabilities on a low dependency funding basis – though this is what the standard wording implies. The legal requirement is instead for “consistency”.

Question 5: To what extent do you agree that the discount rate approach options (horizon method, different rates pre-retirement and post-retirement, constant addition) include the majority of options available?

We agree that this covers the majority of options available. As previously noted, an “other” box will still be needed to capture any unusual approaches.

Question 6: To what extent do you agree that the selections of gilts, swaps, inflation or other cover the main underlying yield curves used when setting technical provisions and low dependency funding basis?

Agree.

We note that there are different approaches to deriving these curves, but assume that the Regulator would not need to know the details of the individual curve construction for this purpose.

Question 7: In respect of the underlying yield curves, indicate the extent to which you agree with the approach proposed of providing the forward discount rate curve, or for small schemes the appropriate single rate?

For most schemes, a forward discount rate curve would be appropriate, but for small schemes or where a different approach is followed, an equivalent single discount rate may be the most easy to obtain and communicate.

We do question whether full 100 year yield curves are necessary – information curtailed at a rather shorter duration – say 50 years or even 30 years – would still give the key information to TPR to understand the basis and approach adopted.

Question 8: In respect of the addition/premium to the yield curve, indicate the extent to which you agree with the approach proposed to provide the forward discount rates?

Agree.

As noted previously, the templates should allow for schemes to follow a different approach to setting the discount rate for technical provisions and for the low dependency target, and not assume the assumptions will be the same after the relevant date.

Question 9: In respect to the addition/premium to the yield curve for schemes that use a pre- and post-retirement discount rate methodology, indicate the extent to which you agree with the approach proposed of providing the appropriate single rate?

See our response to Question 7 in this section.

Question 10: To what extent do you agree with the proposed approach to capture information on inflation and pay increase data?

Disagree.

We believe the wrong information is being sought here. It is the revaluation and pension increase assumptions that drive the liabilities, not the inflation assumption. Asking schemes to provide detailed inflation curves but not asking how these are adjusted for pension increases appears to us to be overlooking the information needed to actually assess the funding of the schemes.

We appreciate though that there are many types of revaluation and pension increases, including for individual tranches of benefit within a single scheme, as well as many approaches to deriving the impact of caps and floors. We would therefore encourage a pragmatic approach be taken to this issue, for example by requesting the curve and/or single equivalent assumptions for say the two largest tranches of pension by liability, or those covering at least x% of the scheme's liabilities.

For open schemes, we note that salary assumptions may not be homogenous across the membership so again a pragmatic approach may be needed to their collection.

Question 11: To what extent do you agree that it would be useful to provide further information on the mortality tables adopted for the mortality assumptions?

Partially agree.

Many schemes will have calculated life expectancies as part of the valuation process (and indeed for the current scheme return submissions) and we agree they are a useful way for the Regulator to understand the approach and assumptions adopted.

To avoid creating additional work though, the option of simply referring to or summarising the tables in the SFP could also be considered.

Consideration will also be needed as to what information is requested where schemes have segmented the membership and use different assumptions for different groups of members.

Question 12: On allowances for commutation, to what extent do you agree that the options provided capture the majority of approaches used?

The options provided do capture the majority of schemes in our experience. However, we do question whether it is necessary to cover commutation in any detail in the statement of strategy. Allowing for commutation is a valid reflection of the actual demographic experience of almost all schemes. Requiring the figure “ignoring commutation” suggests otherwise – yet it is in our view no different to other demographic assumptions, such as withdrawal assumptions for active members, that have the potential to reduce technical provisions. An issue is only created if the current or expected commutation factors that will actually apply differ materially from that reflected for funding purposes.

We also note that the requirements will lead to additional calculations being required by schemes for the sole purpose the Statement of Strategy, that may not be otherwise of any use or value to schemes.

We therefore suggest that this item is removed from the template. The Regulator will, of course, be able to obtain further information from schemes it chooses to investigate after its initial screening and review, and in our view this is the appropriate time to consider commutation assumptions. The information will also be readily in the scheme funding report that TPR could request.

Question 13: To what extent do you agree with the proposed approach of asking about how the key assumptions differ between the technical provisions and low dependency liabilities?

Agree.

Question 14: Do you have any further views or considerations on the information required for Part 1 of the statement of strategy, including any views on alternative approaches or missing data to support Part 1?

There are schemes for which agreement with the employer to Part 1 is not required – the Regulator may wish to include a facility for schemes to indicate if this is the position that applies for their scheme, and that therefore formal employer agreement has not been obtained.

Section 3: Part 2: actuarial information

Question 1: To what extent do you agree that it is reasonably straightforward to provide the cashflows information listed?

Disagree.

We are aware of a wide range of approaches to calculating and generating cashflows – including simplified 2 d approaches and rather more complex 3 d approaches. While some form of cashflow information is often communicated to trustees as part of the valuation process, this tends to be high level, usually in the form of

appropriate charts showing how cashflow is expected to develop over time. This is unlikely to be produced for smaller schemes.

It is also possible that adjustments will be made at an aggregate level to the liabilities after any cashflows have been generated – for example to reflect a final compromise agreement reached with the employer, or to allow for second order differences between the benefits modelled in the valuation system and the actual detailed scheme benefits.

We also note that the cashflows used to calculate the liabilities will be different to the cashflows used for calculating duration and significant maturity, since these will be based on the different inflation expectations applying at 31 March 2023.

Even if cashflows are available, the work to prepare them in the format required and check all the different subsets for all 100 years will create additional extra time and expense for schemes, that in our view is difficult to justify.

We therefore suggest that the Regulator does not ask for cashflows, and instead (as is already proposed for small schemes) relies on the actuary's calculations of duration as evidence for how the scheme will mature, perhaps accompanied by a qualitative narrative box where the trustee can explain the evidence further, if needed in the individual circumstances of the scheme.

We also note that treatment of insured liabilities needs further consideration and guidance. We note that the scheme actuary is allowed (regulation 3(1)(c) of the scheme funding regulations) to exclude these liabilities in certain situations.

As an aside, we would be happy to explore with the Regulator other ways in which the Regulator might improve its modelling of the DB pensions universe as a whole, if this is one of the reasons full cashflows are seen as desirable.

Question 2: Is it easier to provide benefit cashflows on a low dependency basis or on a technical provisions basis?

As noted above, we do not believe either should be required. There are no strong reasons for preferring one over the other, but, we would be of the view the technical provisions cashflows would be the most useful and relevant to the Regulator, should a decision be made that some form of cashflow must be provided.

Question 3: To what extent do you agree that you would expect these cashflows to be materially different?

There could be various differences between the cashflows, for example in the approach to some assumptions and reserves.

Question 4: To what extent do you agree that splitting the cashflows into the five categories listed above is a reasonable approach?

If cashflows are to be required, the split appears reasonable, although as previously noted it will generate significant additional work to ensure cashflows can be provided in the form requested, are entered into the system and fully checked.

Question 5: Please provide any further considerations that you have on the actuarial data to be included in part 2 of the statement of strategy.

No comment.

Question 6: To what extent do you agree with the removal of the requirement to provide accounting valuation and s179 valuation data from a valuation submission perspective?

Agree.

Section 4 : Part 2: recovery plan

Question 1: To provide details about post valuation experience, we expect providing an updated estimated deficit would be best. To what extent do you agree that providing an estimated deficit is the appropriate approach?

We agree that this is a reasonable approach, where it is being used to justify a particular Recovery Plan.

Question 2: If providing an updated deficit, to what extent do you agree it would be straightforward to also provide the updated estimates for assets and liabilities, if we require that detail?

We also expect this would reasonably straightforward. We do note though that liabilities will be estimates, and that the assets will also be estimated (as opposed to the audited values available at the valuation date).

Question 3: Share your views on our proposed approach to collecting information on investment outperformance and post-valuation experience, including any alternative questions that should be considered.

There are different approaches to reflecting post valuation date experience in the Recovery Plan. Often, this will be by taking account of the post valuation experience and certifying the schedule based on the position at the date of signing. This is covered by the proposed approach. However, an alternative approach, where the certificate is certified as at the valuation date based on the expectations at that time, is legally permissible but would not be possible to record as proposed.

Section 5: Part 2: investment information

Question 1: We do not envisage schemes will incur significantly more costs in providing journey plan investment risk data. To what extent do you agree with this assessment?

Broadly agree.

Where only very modest investment risk is being taken, it should be sufficient to provide limited and estimated information sufficient to demonstrate that this is the case.

Section 6 : Part 2: covenant information

Question 1: To what extent do you agree that the proposed approach to submitting covenant information will work in practice for different types of multi-employer schemes?

We are not covenant experts, so are not able to comment meaningfully on this. We are aware that the multi-employer scheme arrangements can be complex and that some flexibility will be essential to ensure individual circumstances can be reflected.

Question 2: To what extent do you agree with the proposal that aggregated covenant information should cover employers that account for at least 80% of scheme liabilities?

No comment.

Question 3: We expect employers to work with trustees and provide the appropriate information. To what extent do you agree that information required will be obtainable to understand the level of risk supportable by the covenant?

In our experience, there is often good co-operation between trustees and sponsors on information, although in some situations the level of detail, forward-looking projections and analysis that would be required to fully complete the proposed template may well not be available. We comment further on the information requested in Question 4 below.

Question 4: To what extent do you agree that the covenant information we propose to request for Bespoke and Fast Track valuation submissions is reasonable and proportionate?

Disagree

We understand that for some schemes – those that are poorly funded, taking significant investment risk and/or where deficit contributions are at maximum affordable levels – the detailed covenant information requested will be important, and we would expect that much of it would have been generated as part of the advice to the trustee on the valuation in any event.

But, especially taking into account improvements in funding over the last couple of years, and subsequent steps schemes have taken to derisk, we think this group will be in the minority. For schemes past their relevant date, the Regulations make no allowance for reliance on covenant for funding purposes, so covenant information for these schemes would only be relevant where there is a low dependency deficit. We do not think it necessary for schemes in either of these categories, if they choose a Bespoke approach, to need to calculate all the items required.

We suggest, therefore, that the focus is on the amount of support the scheme requires from the employer, and the evidence the trustee has that the covenant can support at least this level of risk.

END.