



ASSOCIATION OF CONSULTING ACTUARIES

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30 August 2017

Elelta Beyene
Department for Work and Pensions
Automatic Enrolment Policy
1st Floor
Caxton House
Tothill Street
London SW1H 9NA

Dear Elelta

Automatic enrolment: defined benefit alternative quality requirement and provisions for seafarers and offshore workers

I am writing on behalf of the Association of Consulting Actuaries in response to the above consultation.

Our comments on the specific questions raised in the consultation are set out in Appendix 1 and relate to Chapter 1 of your call for evidence. We do not have anything to say in relation to Chapter 2.

We hope that you find the contents of this letter of assistance. We would be happy to discuss them further if that is helpful, in which case please contact me on 020 7432 6635 (david.everett@lcp.uk.com).

Yours sincerely

A handwritten signature in black ink that reads 'David Everett'.

David Everett

Chairman, Pension Schemes Committee
On behalf of the Association of Consulting Actuaries Limited

Sent by e-mail to: automaticenrolment.consultation@dwp.gsi.gov.uk

Automatic enrolment: defined benefit alternative quality requirement and provisions for seafarers and offshore workers

Chapter 1: alternative quality requirement for defined benefit schemes

1. Do the alternative quality requirements for DB schemes broadly deliver the intended simplifications and flexibility in contrast to the test scheme standard?

Yes and we were pleased to work with you in 2015 and 2016 to that end on the regulations and guidance.

2. Are there specific scenarios, in particular with the commissioning of actuarial reports, in which the alternative requirements are raising any concerns or unintended consequences?

We are aware of some concerns, such as where the pensionable earnings definition does not map to one of the relevant earnings possibilities. See our comments in 12. below.

3. Definition of ‘relevant earnings’

- **To what extent are the different forms of earnings which a scheme can use to determine pensionable earnings meeting the needs of employers? Are employers taking advantage of these variations?**

We believe that they are meeting the needs of most employers. However, care is needed when comparing scheme definitions with statutory definitions – for example the scheme’s definition of “basic pay” may differ from the statutory definition.

- **Are there any circumstances in which a scheme is unable to satisfy any of the different forms of earnings used?**

Given that we understand it is permissible to check that the scheme’s pensionable earnings are equal to or more than one or more of the definitions of relevant earnings either logically or numerically for each individual, we are only aware of a few cases where the approach is causing difficulty.

4. Definition of ‘relevant members’

- **Does this definition fit with existing practice? Are there any circumstances in which it is causing problems or additional work?**

Given that relevant members are all the active members of the defined benefits scheme of which the jobholder is a member we are not aware of any difficulty with this definition.

- **When applying the test at benefit scale level what difficulties, if any, has the actuary encountered in determining whether there is a material difference in the cost of providing benefits between different groups of relevant members?**

We are not aware of any difficulties, but the issue is unlikely to have been fully tested yet given the transitional easement for formerly contracted out schemes.

We think it would be useful to modify either the regulations or the guidance to make clear that the margin above the minimum contribution threshold (the “prescribed percentage”) can be taken into account in assessing whether there is a material difference in benefit scales. So, if you have a scheme with both a 60ths and an 80ths scale, both of which have a cost of accrual that is significantly in excess of the prescribed percentage, there should be no need to carry out the test at benefit scale level.

5. Actuarial reports:

- **What actuarial reports have schemes been relying on for applying the tests under the alternative quality requirements?**

We understand that most schemes have been relying on the most recent funding valuation report, which until recently would have typically pre-dated April 2016.

- **To what extent are employers commissioning separate reports?**

We are not aware of any situations where this has happened, but that is largely because of the transitional easement. We would hope that subsequent funding valuation reports will as a matter of course contain the results of the alternative quality requirement testing, testing at benefit scale level where necessary.

6. Where employers are choosing to commission reports, are they using TSS or alternative requirements?

In our experience where schemes have been content to use the test scheme standard they have continued to use this. We are not aware of a general move away from using the test scheme standard in favour of the alternative quality requirement for those schemes that were contracted in prior to 6 April 2016.

For formerly contracted out schemes the alternative quality requirement is used in the vast majority of circumstances.

7. The legislation is not prescriptive on who should apply the test. In practice, who is applying the alternative quality requirement?

In practice it is the scheme actuary.

8. Are multi-employer schemes making use of simplifications provided for under this part of the legislation?

We have no evidence to the contrary.

9. Transitional arrangements for certain formerly contracted-out salary related schemes:

- **Are these transitional arrangements being utilised?**

Yes – they were essential in order to prevent unnecessarily detailed compliance work being carried out by thousands of formerly contracted out scheme in the run up to 6 April 2016.

- **What action will be taken by schemes in order to be ready to apply the test at scheme-level once the flexibilities have ended on 5 April 2019?**

The scheme-level testing will form part of the calculations undertaken by the scheme actuary as part of the funding valuation report.

10. DB schemes meeting money purchase quality requirements:

- **DWP is only aware of one scheme which applies the test. Are you aware of any schemes which use this test?**

We are aware of only one scheme which uses this test. We believe this to be the same scheme of which you are aware.

- **What are the characteristics of these schemes?**

Not applicable as we are not aware of any other schemes.

11. Is there anything not covered above which you want to tell us about the operation of the alternative quality test, in particular regarding any burden on schemes and employers when compared to the test scheme standard?

No.

12. In your view, how might the alternative tests be further simplified in order to reduce burden on employers whilst preserving the required level of quality? What are the consequences?

One source of frustration with the cost of accruals test is that it is not permissible to check in £ terms that the cost of accrual is equal to or more than a prescribed percentage of a relevant earnings figure. It is a two-stage process – one must check the pensionable earnings definitions first and only if this is passed are contribution rates compared. So a scheme with a restrictive definition of pensionable earnings, but a generous benefit scale cannot use the cost of accruals test. We understand that this is because of the manner in which the primary legislation has been constructed.

But if it were possible, it would be useful for the legislation to allow for the contribution rate that would apply, if the contributions were calculated using one of the legislative definitions, to be tested against the prescribed percentage. That would obviate the need to fall back on the more complex test scheme standard.

About the Association of Consulting Actuaries (ACA)

Members of the ACA provide advice to thousands of pension schemes, including most of the country's largest schemes. Members of the Association are all qualified actuaries and all actuarial advice given is subject to the Actuaries' Code. Advice given to clients is independent and impartial. ACA members include the scheme actuaries to schemes covering the majority of members of private sector defined benefit pension schemes.

The ACA is the representative body for UK consulting actuaries, whilst the Institute and Faculty of Actuaries is the professional body.

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