

PREMIER PENSIONS MANAGEMENT

TECHNICAL UPDATE: 01/09

Actuarial Considerations in the current Financial Climate

After recording two consecutive quarters of negative economic growth, the UK officially went into recession in January 2009. In conjunction with this, the recent falls in equity markets and the subsequent fall in yields on Government Securities are likely to have reduced funding levels and increased pension deficits.

Trustees and sponsors of pension schemes regularly need to look at the funding of pension schemes – and in view of the current investment market volatility, may be considering an ‘out of cycle’ valuation. They should also consider reviewing the actuarial factors used to determine the pension under different member options. This is to ensure that no additional strain is placed on scheme funding by members exercising these options.

Transfer Value Calculations

Transfer value calculations reflect the expected cost of providing the benefits based on actual investment strategy and current market conditions. This may mean that transfer values have significantly increased since the new regulations were introduced in October 2008 and it may no longer be appropriate to continue to pay full transfer values.

Hence, Trustees must place a high level of importance on undertaking insufficiency reports for schemes which may currently indicate that there is a deficit. The reports look at predicting the funding level of the scheme based on every member taking a transfer of their benefits. Once this is complete this will allow the Trustees to reduce transfer values where applicable and protect the security for the remaining members of the Scheme.

However, before reducing transfer values, the Trustees should consider

- 1) The Company Covenant
- 2) The Recovery Plan they have in place
- 3) The long term objectives of the Scheme
- 4) Whether the Company would consider “topping up” each transfer value as an incentive for individuals to consider transferring

Commutation Factors

Generally, a member taking all of his benefits as pension creates a larger liability for the Scheme than a member electing to take some pension as a lump sum. While there may be pressure to improve commutation rates as a result of improvements to life expectancy this may have a detrimental effect on the Scheme funding as members will receive larger lump sums for less pension surrendered.

In addition, increasing commutation rates will inevitably mean that more members will be persuaded by the lure of a lump sum on retirement. Reducing the long term liabilities may be attractive but paying out larger amounts now may reduce the security for the remaining members. Therefore, the factors used must be calculated taking into account not only mortality rates and market conditions, but also scheme funding.

Summary

In conclusion, we are all aware of the current economic climate. The Trustees and Employer need to be aware of the impact on the UK Pension Scheme overall as well as looking at the underlying transfer value and commutation factors. It is clearly very important to keep tight control over actuarial factors and the underlying assumptions used to ensure that schemes' funding levels and security levels are not adversely affected by members selecting different options, especially in the current financial climate.

If you as a Company or as a Trustee are concerned about the effect of the Economic Climate on your pension fund and what you can do about it, please contact Paul Couchman. We would be delighted to help you with this important and complex topic.

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This update includes general information and cannot be relied upon for individual schemes issues. You should contact your adviser or Paul Couchman at Premier Pensions Management Ltd, Capital Business Centre, Units 14 & 15, 22 Carlton Road, South Croydon, Surrey, CR2 0BS. DL: 020 8916 2129. Email:

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if you require definitive advice