

NEWSLETTER NO. 31 : MARCH 1995

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Financial Reporting Standard 32

Actuarial Reports for "Defined Benefit" Schemes

FINANCIAL REPORTING STANDARD 32

The New Zealand Society of Accountants has asked me to draw to your attention that copies of FRS32, "Financial Reporting for Superannuation Schemes", are available from:

New Zealand Society of Accountants
Publications Department
P O Box 11 342
WELLINGTON

The cost to non-members of the New Zealand Society of Accountants is \$15.75 including GST and postage.

This standard will affect virtually all registered superannuation schemes, and is applicable for reporting periods beginning on or after 1 April 1995. Trustees may wish to seek confirmation from their advisors that their financial reports comply with this standard.

ACTUARIAL REPORTS FOR DEFINED BENEFIT SCHEMES

1. THE SUPERANNUATION SCHEMES ACT 1989

1.1 Section 15(1) of the Act states:

"If a registered superannuation scheme -

- (a) Operates on the principle of unallocated funding; or
- (b) Provides benefits that are dependent upon the contingencies of human life, and the risks associated with those benefits are not fully insured with a company engaged in the business of life insurance, -

the trustees shall ensure that an actuary examines the financial position of the scheme as at dates that are no more than 3 years apart."

2. GENERAL COMMENTS

- 2.1 Section 15 reports are required for all schemes which are commonly known as "Defined Benefit" schemes.
- 2.2. Under "Defined Benefit" schemes, the amount of benefit payments are generally determined by reference to future salaries and length of scheme membership (or service with an employer); and the contributions paid are not allocated to individual scheme members.

The Act provides for trustees to receive reports about the financial position of their "Defined Benefit" scheme from an actuary. This enables trustees to be made aware of, inter alia, their ability to meet their responsibility for paying the benefits described in the trust deed.

The Act also provides that copies of section 15 reports:

- (1) are available, as of right, to scheme members;
- (2) are to be forwarded to the Government Actuary.

- 2.3 In terms of the Act, section 15 reports can only be provided by a person who is a Fellow of the New Zealand Society of Actuaries.

I have noted that the New Zealand Society of Actuaries has produced a "Guidance Note" dated 31 August 1987 (which does not have the status of a Professional Standard) on the preparation of reports on "Defined Benefit" schemes.

I have also noted that the content of the reports under section 15 of the Act can, and does, vary widely; and that such variation may not necessarily be due to the varying circumstances of the various schemes.

3. BEST MARKET PRACTICE

- 3.1 Appendix 1 to this Newsletter indicates current "Best Market Practice" as determined from a survey of section 15 reports for "Defined Benefit" schemes which have been forwarded to my office.

This survey covers all 26 actuaries who have submitted section 15 reports in the last 18 months; covers all funding methods used; is not biased in relation to size of scheme assets; and covers 51 section 15 reports.

- 3.2 For the purpose of this analysis, a matter is only regarded as "Best Market Practice" if it is included in the surveyed reports of a number of actuaries.

For example: A summary of the actuary's section 15 report which could be included with the trustees annual report (Second Schedule (h)(ii) of the Act refers) has been provided by only three actuaries in the surveyed reports. Accordingly that is not regarded as "Best Market Practice" in Appendix 1.

- 3.3 There is a wide variation in the format of reports which have been provided under section 15 of the Act.

In order to provide a meaningful analysis, it has been necessary for me to determine broad categories of information, and then to determine to which category I should allocate each particular item of information.

- 3.4 Appendix 1 is in the form of a check list. It is not, nor is it intended to be, a Professional Standard.

For example: I note that Professional Standard 400 "Investigations of Defined Benefit Superannuation Funds" issued by The Institute of Actuaries of Australia has, as an Appendix, a more detailed list of matters to be considered.

- 3.5 Actuarial reports can be required for a variety of purposes by trustees, sponsoring employers, and various authorities in New Zealand and overseas. Appendix 1 refers only to a survey of recent reports on "Defined Benefit" schemes under section 15 of the Superannuation Schemes Act 1989. Accordingly, the information shown in Appendix 1 is not necessarily applicable or relevant for other types of reports.

Also, there may be valid reasons as to why any one particular report which has been submitted under section 15 of the Act contains less (or more) information than that indicated in Appendix 1.

N T Malley
Government Actuary

APPENDIX 1**CURRENT BEST MARKET PRACTICE****CONTENT OF REPORTS UNDER SECTION 15 OF THE SUPERANNUATION
SCHEME ACT 1989**

(For comment, refer to Newsletter No. 31 dated March 1995)

1. INTRODUCTION

- 1.1 The name of the scheme.
- 1.2 To whom the report is addressed.
- 1.3 The purpose(s) for which the report is prepared.
- 1.4 The dates as at which the current investigation and the immediately preceding investigation (if any) were made.
- 1.5 Statement as to whether there are potential conflicts of interest for the actuary who accepts responsibility for the report, of which that actuary is aware; and, if so, a statement of those potential conflicts.
- 1.6 Name, professional qualifications and signature of the actuary who accepts responsibility for the report.
- 1.7 The Date the report is signed.
- 1.8 Table of Contents of the Report.

2. EXECUTIVE SUMMARY

- 2.1 The report contains an "Executive Summary" of the principal matters stated in the report.

3. DATA USED IN THE INVESTIGATION : TRUST DEED

- 3.1 Date(s) of latest trust deed and any amendments thereto.
- 3.2 Summary of material provisions relating to benefits and contributions.
- 3.3 Statement of practice of granting discretionary increases in pensions (if any such practice), since the date of the immediately preceding investigation.
- 3.4 Statement as to whether the actuary's investigation assumes that the above practice of granting discretionary increases in pensions is to continue; and, if so, to what extent.

4. DATA USED IN THE INVESTIGATION : SCHEME MEMBERSHIP

- 4.1 The source of the data.
- 4.2 Summary of the data.

Separate summaries are provided for each of:

- (a) contributing members (the summary includes number of members, average age, average salary and average membership); and
 - (b) pensioners (the summary includes number of pensioners, average age, and average pension); and
 - (c) members entitled to deferred benefits.
- 4.3 Reconciliation of the number of contributing members at the date of the current investigation with that at the date of the immediately preceding investigation, showing the number of new members, and the number of members exiting the "contributory membership" category for each type of exit (retirement, death, etc).
- 4.4 Reconciliation as for 4.3 for each of "pensioners" and "members entitled to deferred benefits".
- 4.5 For persons who were members at the dates of the current and immediately preceding investigations, a statement of the average annual rate of increase in salary over that period.

Where benefits are calculated by reference to a "pensionable salary" (i.e. salary less a deduction, such as the single person's annual rate of New Zealand Superannuation), a statement of the corresponding average annual rate of increase in pensionable salary.

- 4.6 Care has been taken to present the summary of the data in a form which would not contravene the Privacy Act 1993. For example, where the number of contributing members (or pensioners) has been very small, the "data summary" has simply referred to the number of contributing members (or pensioners).

This same care has also been taken with regard to the data in 4.5.

- 4.7 Membership data illustrated by the use of bar charts, pie charts etc.
- 4.8 Statement of the actuary's views on the sufficiency and reliability of the data.

5. DATA USED IN THE INVESTIGATION : SCHEME ASSETS AND REVENUE

- 5.1 The source of the data.
- 5.2 A description of the assets, and the names of the Investment Manager(s).
- The "description of the assets" is either an analysis of investment sector allocation or the names of the Investment Managers investment fund(s) and Units in which the scheme monies are invested.
- 5.3 "Consolidated Account", showing value of scheme assets at "date of current investigation" and "date of immediately preceding investigation", and principal items of income and outgo for that period.
- Care has been taken to avoid a breach of the Privacy Act 1993.
- 5.4 A statement of contingent liabilities which have, or have not, been allowed for in determining the value of the scheme assets at "date of current investigation".
- 5.5 Statement of the average annual rate of investment earnings over the period "date of immediately preceding investigation" to "date of current investigation"; and how this has been calculated.
- 5.6 Statement of the actuary's views on the sufficiency and reliability of the data.

6. OTHER BACKGROUND TO INVESTIGATION

- 6.1 Comment on internal scheme matters which have occurred since the date of the immediately preceding investigation.

This includes comment on:

- (a) The contribution rates paid since the date of the report on the immediately preceding investigation, and whether or not they were in accordance with the recommendations made by the actuary in the report on the immediately preceding investigation.
- (b) Any discrepancy between the trust deed and the trustees practice, of which the actuary is aware.
- (c) Any material developments in the scheme since the date of the immediately preceding investigation.

- 6.2 Comment on external events relevant to the scheme which have occurred since the date of the immediately preceding investigation.

This includes comment on changes in legislation.

7. ACTUARIAL VALUATION METHOD AND ASSUMPTIONS USED BY THE ACTUARY

- 7.1 Explanation of the funding objectives and the funding method used to achieve those objectives.

Explanation of the implications of the above in terms of the stability of future contribution rates and future funding levels.

Statement as to whether there has been any change in the funding objectives and the funding method since the date of the report on the immediately preceding investigation; and, if so, an explanation of the effect of such changes. (The detail of this is covered in paragraph 8.4 (e) below).

- 7.2 Statement of the assumptions made in valuing the assets.

- 7.3 Statement of the assumptions made in calculating the actuarial present value of the liability to pay benefits to current members and beneficiaries.

"Beneficiaries" includes contingent beneficiaries, such as spouses of current pensioners who are entitled to a "surviving spouse" pension.

For example:

- (a) Financial and Economic

Future rates of investment earnings (net of tax), salary increases and increases in pensions; and rates of increase in the cpi, National Average Wage, New Zealand Superannuation, etc; where these are relevant.

- (b) Demographic

Future rates of in-service mortality, disability, resignation, retirement, pensioner's mortality, etc; where these are relevant.

Where published tables have been used, reference is made to the published table e.g. 60% New Zealand Life Tables 1990/92, Total

Population Males and Females separately; PA(90) less 3 years for males and 2 years for females.

Where published tables have not been used, examples of the rates at quinquennial ages are given.

(c) Other

Where trustees are directly responsible for the payment of future administration and/or investment expenses, a statement as to how these are allowed for. (Market practice varies - these expenses may be expressed as a percentage of future salaries, a percentage of future contributions, a percentage of future assets, and/or "allowance has been made for these in my assumptions as to the future rate of investment earnings").

- 7.4 Explanations as to why the particular assumptions in 7.2 and 7.3 have been chosen.
- 7.5 Comment on the compatibility of the basis of valuing the assets with the basis of valuing the liability to pay the benefits.

8. RESULTS OF THE INVESTIGATION

8.1 Accrued Benefits

Comparison between the actuarial present value of Accrued Benefits, and the actuarial value of the assets, as at the date of the current investigation. This comparison includes an analysis of the actuarial present value of Accrued Benefits according to the nature of the benefit (e.g. retirement, death, etc. for contributing members; pensions for pensioners (and spouses and dependants if relevant); deferred benefits, for members entitled to deferred benefits).

Corresponding figures given "as at" the date of the immediately preceding investigation.

"Accrued Benefits" are defined.

Comments are made on the above.

8.2 Vested Benefits

As for 8.1, but reference is made to "Vested Benefits" and not "Accrued Benefits" (except that "Vested Benefits" are not analysed according to "Nature of Benefit").

Statement regarding Superannuation Schemes Act 1989, Second Schedule (f).

8.3 Contribution Rates

Explanation regarding future contribution rates.

This incorporates an analysis of the actuarial present value of benefits arising from future scheme membership, according to the nature of the benefit (e.g. retirement etc); the actuarial present value of the actuary's allowance for future administration expenses payable by the trustees (if any); the actuarial present value of members future contributions (if any); and the actuarial present value of the employer's future contributions. (Alternatively, the analysis may be given according to "future contribution rates as a percentage of members future salaries" rather than "actuarial present values"). Some of these items are not shown if the "Funding Method" does not require them.

This also includes comment on:

- (a) The effect of Specified Superannuation Contribution Withholding Tax.
- (b) "Contribution holidays", or amortisation of any actuarial deficiency in the coverage of Accrued Benefits.
- (c) Contribution rates for new members, if this is relevant to the funding method used.
- (d) The stability of future contribution rates.
- (e) Recommendation(s) for future contribution rates.

8.4 Other matters

- (a) Comment as to whether the actuary considers that the assets of the scheme as a whole are suitable for the purposes of the scheme.
- (b) Assessment of the scheme's investment performance.
- (c) Comment on the adequacy of the insurance arrangements, if the actuary considers that insurance of death and disability benefits is appropriate, or if such insurance has been arranged by the trustees.
- (d) Comment as to whether the trust deed may need to be amended, due to changes in legalisation; and, if so, the short title of the Act(s) concerned.
- (e) If there were any changes in:
 - (1) the funding method, or
 - (2) the assumptions used in the actuarial valuations of the assets and liability to pay benefits, or
 - (3) the type and/or amount of benefits as defined in the trust deed,
 since the date of the immediately preceding investigation, a statement of:
 - (i) what changes were made, and
 - (ii) the reason(s) for those changes, and
 - (iii) an explanation of the financial effects of those changes.
- (f) Explanation of the financial effect on the results of the current investigation caused by variations between:
 - (1) the principal actuarial assumptions used in the immediately preceding investigation, and
 - (2) the scheme's actual experience as regards those assumptions;
 e.g. gain (or loss) because the scheme's actual investment earnings rate was higher (or lower) than that assumed by the actuary.

- (g) Explanation of the sensitivity of the results of the current investigation to changes in the principal actuarial assumptions.
- (h) Comment on material events which have occurred subsequent to the date of the current investigation and prior to the date of signature of the report.
- (i) Recommendation as to the date as at which the next actuarial investigation should be carried out; and/or the circumstances which should cause the trustees to seek another actuarial investigation of the scheme.

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