Hewitt in Ireland

SPOTLIGHT

April 2006 Issue 7

Calculation of Transfer Values and other recent changes

Regulations introduced in September 2005 require that transfer values paid in respect of preserved benefits from a defined benefit scheme must be calculated in accordance with professional guidance issued by the Society of Actuaries in Ireland (SAI). In practice, this has been the case for a number of years as the relevant Guidance Note GN11(ROI) is classified as a practice standard and is therefore mandatory for actuaries undertaking the calculation of transfer values under Section 34 of the Pensions Act. Section 7A of the Pensions Act provides that actuarial guidance specified in Regulations cannot be amended without the consent of the Minister for Social and Family Affairs.

The SAI has proposed, and the Minister has consented to, a change in GN11 which will take effect from 1 May 2006. The revised version of GN11 is available on the SAI website www.actuaries.ie

The effect of the change is to increase transfer values and, because the liabilities of a scheme in respect of active and deferred members under the funding standard are calculated as the transfer values payable at the effective date, the funding standard liabilities will also be increased.

Details of the change

Appendix 1 to GN11(ROI) sets out the financial assumptions which are used in the calculation of transfer values. In view of the continuing low level of yields on longer term gilts, the SAI considers it appropriate to reduce the long term discount rate post retirement (which is intended to reflect long dated gilt yields) from 5% to 4.5%. It should be noted that for anybody within 10 years of retirement, a Market Value Adjustment is applied to the value calculated on the long term assumptions so that the current lower level of gilt yields is brought into the calculation for such cases.

Impact of the change

The table below gives an indication of the approximate increase in transfer values at various ages, assuming there is a 50% spouse's pension payable on death after retirement. This is shown for a normal pensionable age of 65 and the impact will be greater where normal pensionable age is earlier than this. The percentage increase is the same for males and females. The examples shown relate to a scheme with no pension increases, and to a scheme with guaranteed increases of CPI to a maximum of 5% per annum. Again, the impact will be slightly different where other levels of pension increase or spouse's pension applies.

Age	No increases	(CPI max 5%)
35	6.9%	7.5%
45	6.9%	7.5%
55	6.9%	7.5%
60	3.9%	4.1%

Funding standard

As noted above, a knock on effect of the change is that funding standard liabilities for active and deferred members will increase with effect from 1 May 2006. The extent of the increase will depend on the maturity and age profile of the scheme membership, but for schemes with a relatively young active membership and no pensioners, the increase is likely to be of the order of 4% to 7%. As pensioner liabilities are measured by reference to annuity costs, which have stabilised or even eased slightly in recent months, more mature schemes will be less affected by this change.

While this will not impact on funding certificates or actuarial statements with effective dates prior to 1 May 2006, an actuary who is required to certify that an existing funding proposal is on track at, say, 31 March 2006, should take the new GN11(ROI) into account in assessing the liabilities at the end of the funding proposal period as this will be after 1 May 2006 . Of course, it would be reasonable also to take credit for the relatively strong performance of equity markets over the recent past, which may enable the actuary to certify the proposal is still on track, but this will depend on the circumstances of the individual scheme.

Payment of transfer values

Under the Pensions Act, a transfer value is calculated at the date of receipt of a request to pay the transfer value, or some date selected by the Trustees not more than 3 months before or after that date. In practice, it is not possible to select a date later than the end of the month in which the request is received as the Market Adjustment Factor for the following month would not be known.

Trustees may consider it appropriate to notify former members who request a transfer quotation or payment before 1 May 2006 that the basis of calculation will be changing (to their advantage) with effect from that date and that their application will not be processed until after 1 May, unless they insist otherwise.

For a scheme where transfer values are reduced due to underfunding, the change in GN11(ROI) is unlikely to impact significantly on the amount available for transfer, as the increase in the calculated transfer value will broadly be offset by a reduction in the level of coverage arising from the higher funding standard liabilities of the scheme.

Other recent developments

- The Minister for Social and Family Affairs has issued Regulations specifying the statutory revaluation percentage for 2005 as 2.5%. All preserved benefits entitlements should be increased by this amount at 1 January 2006 (or by a pro-rata amount for those who left the relevant scheme during 2005).
- Revenue have announced a relaxation of benefit limits for late entrants to an occupational pension scheme as set out in the table below.

	Maximum pension as proportion of final remuneration	
Years of Service at Normal Retirement Age	**Old basis**	**New basis**
1	1/60	4/60
2	2/60	8/60
3	3/60	12/60
4	4/60	16/60
5	5/60	20/60
6	8/60	24/60
7	16/60	28/60
8	24/60	32/60
9	32/60	36/60
10	40/60	40/60

For further information please contact your usual Hewitt consultant or:

Rachael.Ingle@hewitt.com
Block D, Iveagh Court, Harcourt Road,
Dublin 2, Tel 01 4189130

John.Cremin@hewitt.com
Dundanion House, Blackrock Road,
Blackrock, Cork, Tel 021 4357880