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CHANGES IN UNITED KINGDOM SOCIAL SECURITY AND RETIREMENT PLAN REQUIREMENTS

by Peter A. Friedes and John C. Roberts

On May 7th, Barbara Castle, Secretary of State for Social Services, announced major changes in the details of the Social Security Act - 1973. This Act provided for the following principal features:

(a) The abolition of the Graduated State Pension Scheme.

(b) The introduction of a new supplementary state pension arrangement — the State Reserve Scheme — to replace the Graduated State Pension Scheme.

(c) The introduction of earnings-related contributions for all state pensions.

(d) The introduction of mandatory vested rights in all Occupational Pension Schemes.

In order to contract out of the State Reserve Scheme, it was necessary for certain minimum requirements to be met. The provisions of private plans were to be submitted to the Occupational Pensions Board for approval. This Board would also examine the financing media adopted to ensure that minimum benefits were being securely funded for employees who were to be contracted out of the State Reserve Scheme.

The major changes amended by Barbara Castle are as follows:

- The Graduated State Pension Scheme will terminate as of 5 April, 1975, as stipulated in the Act.
- The State Reserve Scheme will *not* come into effect on 6 April, 1975.

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MINORITY RECRUITMENT

by James C. Harrison

This item is intended to present an updated report on the Minority Recruitment Program of the Society of Actuaries—begun in 1969 by actuaries in the New York Area, and taken over by the Society in 1971.

To date, the main effort has been the Actuarial Summer Institute, conducted each summer, from 1970 on, at Lincoln University, Pennsylvania by Professor James Frankowsky, chairman of Lincoln's mathematics department. The purpose has been to prepare disadvantaged minority mathematics students to pass Part 1, and thus to encourage them to embark in actuarial careers. Ten students have gone on to pass Part 1, and five students have since been employed as actuarial trainees by leading insurers. Three are attending graduate actuarial school at Michigan.

But these results, though significant, represent a pass rate of less than 20%. For this reason, the Subcommittee in charge of the program decided to attempt substantial improvements before continuing the Institute for another year. Recruiting was intensified, employment filling out the summer prior to Institute attendance was obtained, and, most importantly, selection standards were upgraded sharply. The result has been a 1974 class of markedly higher quality, judging from initial testing. Another significant change in approach has been to extend recruiting beyond the predominantly black colleges to most quality colleges in the country with minority enrollment.

A graduate scholarship in actuarial science has been offered, commencing in 1973, and the first award has been made.

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CONSULTING PROBLEMS IN THE INTERNATIONAL CONTEXT

By David L. Hewitt

The fourth conference of the International Association of Consulting Actuaries was held in Amsterdam, May 26 to 30, 1974. Consulting actuaries, as advisers to pension plans and insurance companies, are facing serious and surprisingly similar problems in the countries represented. While many topics were covered, the key areas appeared to be inflation, social security, regulations, relationships with accountants and professional responsibility.

Inflation and Its Relationship to Funding

While past salary growth rates of 7% per annum or less, partly reflecting productivity growth, have been dealt with systematically, current inflation rates in the neighborhood of 15% per annum or more create problems and doubts.

Many private pension plans are based on final average salary. Those which are not still have the moral obligation to update benefits before retirement. All of them have the obligation to update benefits after retirement, and few do by the plan rules as written, instead amending from time to time.

High inflation rates require high funding to anticipate the level of benefits which will ultimately be needed. But at the same time high inflation throws into doubt the value of funding: why pay good currency now to anticipate the need for increased benefits payable in future cheaper currency?

This led to an interesting discussion of whether to fund and to what degree. By the end of the discussion we seem to have gotten back to where most of us were in the first place: funding is needed for employee security, including funding

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Consulting Problems

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to meet the effects of future inflation (whether by specific salary scales or by revealed contingency reserves or by hidden contingency reserves as a result of conservative assumptions). Funding is also needed to recognize pension costs as a charge against current operations. Funding is furthermore useful, especially under contributory plans, to make clear to those involved what the cost of plan improvements is. The further comment was made that failure of private pension plans to pre-fund for future inflation has encouraged the lack of adequate funding in some public plans.

The need to fund now for future benefit growth also applies to plans which will achieve this growth by occasional amendments rather than by a built-in approach. Perhaps benefits should be indexed to a wage scale or have a flat percent increase in each year of retirement. There was considerable discussion of the inadequacy of fixed vested benefits. These should grow by a wage index, either at the cost of the current employer or at the cost of the original employer. (Probably the current employer.) The instability of investment values during the current inflation makes matters worse. This also creates a diversity of possible asset values.

Growing Social Security

The growth in Social Security systems in most of the countries represented could squeeze out private pension plans. Much discussion focused on this point. (The Netherlands and Switzerland seemed to be exceptions to this. Private pension plans are providing the growth there.) The fact that Social Security systems are becoming indexed to cost-of-living growth could influence private plans to do the same thing.

Growing Government Regulation

New laws are being proposed in many countries requiring more from private pension plans in the areas of: (1) vesting; (2) funding; (3) reinsurance, which may carry with it making the corporate assets of the employer subject to pension claims; (4) broadened coverage within present industries and companies; (5) broadening coverage to new industries and companies; (6) controlling the quality and mix of investments; (7) disclosures to covered employees.

The U.K. Insurance Companies Amendment Act of 1973 prescribes by law how valuations should be done in areas previously left to the judgment of the actuary. Insurance companies established just before passage of this law are put into a squeeze by the new rules, since asset values are reduced more than liabilities under the new standards for selecting interest assumptions. At the same time, this law provides a basis for promoters to go into the insurance business for quick profit. This provides work for the actuary and places a responsibility on him. U.K.'s entry into the European Economic Community may cause it to revise some of its valuation practices to a uniform basis with the other participating countries.

Relations of the Actuary and the Accountant

The accounting profession is concerned with its responsibilities (and exposure to liability) to shareholders and to potential shareholders. The actuary has traditionally been concerned with his responsibility to his client (and in a general professional sense to the public interest). The accountants (especially in the United States, but also in other countries) are pressing the actuaries as to how assets, liabilities and costs are determined and who should be responsible for this determination. This can lead to conflicts and overlaps in professional responsibilities, and also to doubling up on valuations, depending on whose needs and requirements are being satisfied. In the United States, the audit guide for stock life insurance companies has already been issued by the Institute of Certified Public Accountants, carrying with it the foregoing problems. The Generally Accepted Accounting Principles so defined for United States companies are also affecting some U.K. subsidiaries of such companies.

A proposed audit guide for pension funds is still under discussion in the United States between the actuarial profession and the accounting profession, who are together attempting to work out some of the problems and avoid a showdown. The subject of relations between the accountant and the actuary is also being studied in the Netherlands. A Dutch member commented that each profession probably underrates the other profession and the problems of the other profession.

To Whom is the Consulting Actuc Responsible?

In a pension plan, the alternatives include: (1) the employer who hires him; (2) the covered employees; (3) the government, to whom he certifies certain facts; (4) the public. In an insurance company, one must consider: (1) the insurance company officers who hire him; (2) the stockholders; (3) the contractholders; (4) the individuals covered by the contracts; (5) the government, to whom he certifies certain facts; (6) the public.

Actuarial results can be different depending on their purpose and use, such as: to meet legal specifications; to meet accountant's specifications; to meet tax requirements; to give a true result to the employer for his planning; to give an appropriate result for purposes of a merger; to give an appropriate result for purposes of dividing a terminated fund.

When the actuary certifies a fact under prescribed rules and assumptions, should he also add a statement as to what he believes the appropriate rules a assumptions and the appropriate answe should be, if different? The actuary should identify his client, state to whom he is responsible, and should be accurate and complete. He should not pretend to have abilities he does not possess.

There are potential short run conflicts of interest between a client and the actuary. An unscrupulous actuary could slant his advice to make more work for himself. There are also potential conflicts of interest in the case of mergers of clients. These can be reduced if the actuary can give to each client the correct answer from its point of view.

Raymond C. Palmer, from Australia, commented that a professional should: (1) act in the interest of his client rather than himself; (2) know who his client is; (3) reveal to outsiders who his client is; (4) be an expert; (5) be paid by his client; (6) act in the public interest.

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To this observer, the profession a peared overwhelmed by its problems. We face the future with great doubts. What seems assured, however, is that there will be more work for consulting actuaries as a result of these problems. □