



## EXPLANATORY MEMORANDUM TO PROFESSIONAL STANDARD 407

### SOLVENCY MANAGEMENT OF DEFINED BENEFIT SUPERANNUATION FUNDS

May 2010

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#### **A. About this Explanatory Memorandum**

1. The Institute has released Professional Standard 407 – Solvency Management of Defined Benefit Superannuation Funds (“PS 407”). The standard replaces Guidance Note 461 (Funding and Solvency Certificates) last issued in December 1994.
2. This Explanatory Memorandum has been prepared to assist Members in understanding the key features of the new standard.

#### **B. Background**

3. On 1 March 2006, the Institute issued a Policy for Drafting Professional Standards (the “Policy”) which was subsequently amended in June 2006. The Policy is designed to ensure that all Professional Standards use consistent and objective terminology such that mandatory duties and requirements for members are clearly defined and understood.
4. As a result, all existing Professional Standards and Guidance Notes are to be re-drafted in accordance with the Policy as either a Professional Standard or Practice Guideline. The new PS 407 reflects that requirement.
5. Members’ attention is drawn to the fact that a Professional Standard:
  - (a) details mandatory practice requirements (including the duty to exercise a discretion and a duty to properly explain an exercise of such discretion) in an area; and
  - (b) contains principles and/or directions from which it would be unprofessional to depart.
6. By contrast, a Practice Guideline is issued to formally capture and document generally accepted actuarial practices and techniques to assist members to



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deliver competent Professional Services. Practice Guidelines are non-mandatory, not connected to Professional Standards and must not be used to interpret a Professional Standard.

**C. Consultation**

7. On 19 February 2010, an Exposure Draft of PS 407 was released for member comment. Comments closed on 19 March 2010.
8. One submission was received proposing that the title of the standard make specific reference to "defined benefit" superannuation funds, for clarity. The suggestion has been reflected in the final standard.

**D. Key features of PS 407**

9. PS 407 updates Guidance Note 461, without making substantive changes to the majority of its concepts. Sections or concepts no longer considered relevant have been removed.
10. The section most heavily rewritten concerned Notifiable Events, with some new material added. In relation to the requirement concerning trigger points, an example is that of a trigger point of an investment return of worse than -5% being defined as a Notifiable Event. In such a situation, the Member must be satisfied that the Fund would remain solvent if an investment return equal to -5% occurred in that period. (This, of course, does not rule out the possibility that the Fund may become Technically Insolvent if an investment return of worse than -5% occurred in that specified period. However, in that event, the FSC would lapse.)

**END OF EXPLANATORY MEMORANDUM**