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Our response to the FSA guidance consultation on pension obligation risk and the ICAAP, GC 11/06

Introduction

1. The Building Societies Association represents mutual lenders and deposit takers in the UK including all 48 UK building societies. Mutual lenders and deposit takers have total assets of over £365 billion and, together with their subsidiaries, hold residential mortgages of almost £235 billion, 19% of the total outstanding in the UK. They hold more than £245 billion of retail deposits, accounting for 22% of all such deposits in the UK. Mutual deposit takers account for about 36% of cash ISA balances. They employ approximately 50,000 full and part-time staff and operate through approximately 2,000 branches.

Background

2. We are pleased to be able to comment further on the revised guidance and clarification of key assumptions on Pillar II pension obligation risk capital requirement (P2PRC). And we are, of course, grateful to have received feedback on our earlier points on the first draft.

www.fsa.gov.uk/pubs/guidance/gc11_06_bsa.pdf

3. As we said in response to the earlier draft, societies on the whole welcome this clarification. Any detail to help close the gap between the FSA's expectations and societies' own approach is appreciated and necessary in meeting one of the stated objectives of the Basel II framework, namely to facilitate the greater use of firms' own assessments of risk as inputs to capital calculations.

www.bsa.org.uk/docs/policy/prudentialandfinreg/pension_ICAAP.pdf

The P2PRC regime

4. We note in the first paragraph of this section that there will be no changes (previously no *immediate* changes) to the FSA rules and guidance with respect to P2PRC. In an environment of almost constant regulatory change, this assurance is most welcome. But the second paragraph appears to contradict this; it says that the FSA will soon be reviewing its approach to pension obligation risk particularly in light of the introduction of Basel III.

5. Clarification on the permanence of the guidance under consultation and the parameters of the forthcoming review would therefore be helpful.

6. One of our points on the earlier draft concerned the FSA's comment that the trustees' actuarial funding valuation is more likely to provide firms with the most relevant starting point from which to assess their P2PRC. Firms could use a different valuation basis but they would have to justify why they did so. As we said in our last response, there are reasons why the accounting basis may be considered more appropriate as it is less subjective, due to the fixed assumptions used, and hence consistent across firms. We also presented some detailed arguments for the accounting approach from an individual building society.

7. We were pleased to note in the feedback that the FSA had considered these arguments carefully, even if not agreed with them.

8. Given that the FSA does not entirely rule out the accounting valuation, we consider it would be helpful to building societies if detailed guidance could be provided on the sort of scenarios where that approach would be acceptable.

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