

Measuring the quality of benefit calculations

The quality of pension scheme administration is typically measured by the scheme administrator's ability to meet the agreed service level agreement but ultimately this gives a measure of timeliness rather than accuracy. Member surveys can give a measure of customer satisfaction and the Pension Regulator's guidance may offer some reassurance for trustees that their data is being properly maintained. However, the ultimate test that benefits have been calculated correctly, and in accordance with the scheme's trust deed and rules, is a benefit audit.

So why would trustees incur the additional cost of such an exercise? For schemes in a Pension Protection Fund (PPF) assessment period this is a compulsory exercise. It enables trustees to assure members and their dependants that their benefits have been calculated accurately over the lifetime of the scheme, avoids any over or under-payments to members and is a good test that the data is accurate for the valuation. Trustees of ongoing schemes may want to offer the same assurances.

Who should undertake the benefit audit?

An audit could be carried out by the appointed administration or actuarial teams, or for an independent review, another third party administrator or consultancy.

What needs to be in place first?

Before an audit can begin, it is essential that there is a detailed benefit specification in place and that the membership data is in good order. The quality of the benefit calculations is only as good as the quality of the underlying data.

Other considerations

Check that any equalisation or scheme closure deeds will satisfy legal scrutiny. It is not uncommon to discover that equalisation or scheme closure has not been correctly documented. In fact it has been identified for a number of schemes when they have started a PPF assessment period.

Selecting a sample of members to audit

There are a number of key areas that need to be looked at when choosing your sample of members. Include a mixture of males and females, different membership statuses and retirement types. Include members with more complicated benefits and members who left under the different revaluation and Inland Revenue maximum regimes. Then consider risk areas such as:

- past changes of administrator
- risk areas identified by the trustees such as a period when manual calculations may have been carried out

- scheme specific issues such as changes in scheme rules or scheme factors, any unusual benefits

Select members for your test sample who will have had their benefits calculated pre and post any of these changes.

Selecting the sample size

Your sample size will depend on the number of categories and risk areas identified above. However, an initial sample size of between 5% and 10% of the total membership is typical. For larger schemes you may want to reduce the percentage if you can cover all the risk areas with fewer members.

Carrying out testing

The testing should be carried out based on first principles and then compared to the benefits shown on the member's record. The reasons for any differences can be noted for each member and patterns identified. The aim is to identify systematic errors.

Controlling the cost

The best way to control costs is to keep the sample size as small as possible while still ensuring that you are testing the majority of the risk areas. If you identify any issues or errors from testing the initial sample, then you can increase the sample size at that point and select more members for testing.

Rectification work

You may want to consider carrying out a Guaranteed Minimum Pension reconciliation prior to the benefit audit. Any rectification work for both exercises can then be combined.

When deciding on any rectification work required as a result of the audit, it is important to consider the underlying data. It may be that historical membership data is missing from the electronic records, for example a history of part time hours. It would not be sensible to recalculate a member's benefits if there is potential for data to be missing. If a systematic error has been identified then there is good cause to correct the benefits.

Summary

A benefit audit may come at a cost but the peace of mind for both members and trustees that benefit calculations have been carried out correctly, or have been corrected following a rectification exercise, makes it a worthwhile exercise. ■



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