

~~RESTRICTED POLICY~~Released under
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Your reference OPP5

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S40(2)

**GOVERNMENT
ACTUARY'S
DEPARTMENT**

2 June 1997

~~WITHHELD~~

S40(2) (OPP5)

Department of Social Security

The Adelphi (11th Floor)

1-11 John Adam Street

LONDON

WC2N 6HT

22 KINGSWAY
LONDON
WC2B 6LE
FAX 0171 211 2640

SWITCHBOARD
0171 211 2600
DIRECT (GTN)
~~WITHHELD~~
S40(2) F2/A

Dear ~~WITHHELD~~
S40(2)

TAX CREDIT ON UK EQUITY DIVIDENDS

Further to my letter dated 30 May 1997, I am just writing with a couple of further thoughts which have occurred to me.

Three of the scenarios (Schemes 2, 4 and 6) had no UK equity investments yet Schemes 4 and 6 suffered a fall in the MFR funding level (after an ACT change) because of an assumed fall in the gross dividend yields of UK equities. In practice, of course, Schemes 4 and 6 might satisfy the criteria for a 'gilts-matching' policy (see MFR Regulations 7(4), (8) and (9)), in which case the liabilities of such schemes would (as in the case of Scheme 2) be immune from changes in the gross dividend yields of UK equities.

The attachments to my earlier letter effectively assume that a gilts-matching policy does not apply. This might not be an unreasonable assumption given that the scenarios selected for illustration were deliberately on the extreme and, in practice, a scheme with a policy of investing even a small amount in equities might not be able to claim a 'gilts-matching' policy.

Further, although we have illustrated the most extreme scenarios of a 20% fall in market prices or gross dividend yields, it is of course not automatic that one of these would be the consequence of an elimination of ACT relief.

Clearly, the effects would depend on the views taken by both gross and net investors (including financial institutions such as pension funds, insurance companies etc) of the relative merits of equities and gilts in the new system. For example, institutions might still regard equities as a better long term bet than gilts, which would mean that, other things being equal, the behavioural change would be constrained. Overall it is difficult to be precise about the likely reactions.

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Finally, we would find it helpful if you would kindly allow us the opportunity to comment on any draft documents (such as draft Ministerial submissions) in which it is proposed to use the figures or advice given by us to you on this issue. This is important because the matters are technically complex (as well as speculative) and you will appreciate that, in any case, we have a professional obligation to ensure that our advice is presented in an appropriate way, particularly to third parties with whom we are not communicating directly.

If you want to discuss any of these matters with us further, please do not hesitate to telephone me or *1774-4*

Yours sincerely *1774-4*

*WITHHELD -
S40(2) FOIA*

Actuary
PENSIONS POLICY, DEMOGRAPHY AND STATISTICS