



Risk sharing Current developments in UK pensions

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Main changes in workplace provision over last decade or so

- Massive closure of final salary schemes
 - to new entrants
 - to future accrual
- Major growth in DC arrangements



Main reasons for swing away from final salary schemes

- Longevity risk
- Investment risk
- Company accounting standards
- Increased legislation
 - benefits eg mandatory indexation
 - administration
- S75 debt
- PPF levy
- Mobility of labour

Replacement schemes

- For new entrants
 - primarily DC
- For future accrual
 - reduced DB
 - DC
 - combination of DB and DC

Making DB more affordable

- Reduce future service accrual
- Change to career average
- Increase member contributions
- Increase NRA
- Worsen early retirement terms

Problems with DC for modest earners

- Choosing risk/reward trade-off
- Variability of results between members with time
- Investment strategy depends on retirement date being known

Risk sharing – current position in UK

- Combining DB and DC
- Deregulatory Review – report published late July 2007
- Too much legal uncertainty
- Radical extension of risk sharing required

Government's pension reforms

- Changes to State pension scheme
- Introduction of Personal Accounts

Why conditional indexation?

- A natural step
- Career average schemes with targeted increases – backed by “prudent” reserves – “conditional indexation”
- Avoids leakage of any funding surplus
 - no abatement of employer future service contributions
 - “passed” increases reinstated out of future surplus
- Change NRA, with protections, if life expectancy increases
- Requires modest changes to the law – amendment to current Pensions Bill

Conditional indexation

From employer's perspective

- Gives control of contributions
- Lower cost of £1 pa of pension than DC
- S75 debt excludes targeted increases
- PPF
 - lower levies: as better funded than DB
 - separate from DB: to avoid cost of legacy
- Less volatile numbers in company financial statements
- Could have level % employer contributions with age-related member contributions

Conditional indexation From member's perspective

- More stability of provision than under DC
 - sharing of risks with employer
 - pooling with other members

Important for modest to mid earners
- Employer takes first 'hit' when experience is adverse
- Age-related member contributions align with many lifestyles
- PPF compensation is 100%, but excluding targeted future increases: avoids "cliff edge"

Conditional indexation - positioning

- Needs modest change in legislation – APL - NOW
- Similar to The Netherlands
- Addresses public sector vs private sector polarisation on pensions in UK
- Leave more radical risk sharing to a future Pensions Bill

Where will conditionally indexed schemes come from?

- Medium to large employers
- Future service benefits
- Initially – final salary schemes about to be closed to future accrual
- Subsequently – upgrading of existing DC schemes
- Evidence of interest from employers

The campaign – so far

- ACA membership
- Occupational Pension Schemes Joint Working Group: ACA, ABI, NAPF, IMA, SPC, APL
- Employer and trade union representative bodies eg CBI, TUC
- Media
- Politicians – Government, Opposition, Members of Parliament

What's been achieved – so far

- Has increased the profile of risk sharing pensions in the public arena
- Pensions Bill currently before Parliament
- ACA's role compared to Actuarial Profession



This is a once in a lifetime opportunity for
revitalising workplace pensions in the UK

