ASSOCIATION OF ACA CONSULTING ACTUARIES

NEWS RELEASE

The failure of public policy in preserving and promoting quality pensions in the private sector cannot continue, says the ACA, as survey results point to more and more employers closing good schemes. It's time for a standing Pension Commission that will challenge the legal and regulatory hurdles standing in the way of sensible long-term pension designs...

MAJOR WORKPLACE PENSIONS SURVEY FINDS:

- **87% OF DEFINED BENEFIT SCHEMES NOW CLOSED ...**
- **59% OF EMPLOYERS SET TO REVIEW PENSIONS AHEAD OF 2012 ...**
- **24% OF EMPLOYERS WILL CONSIDER PENSION BENEFIT REDUCTIONS WHEN THEY HAVE TO AUTO-ENROL ALL EMPLOYEES INTO A SCHEME ...**
- **JUST 6% OF EMPLOYERS SAY GOVERNMENT'S STATED POLICY OF SUPPORTING QUALITY PENSIONS IS WORKING ...**

4 January 2010: The final results of a survey on pension trends[1] in firms with combined total assets of £139bn conducted by the Association of Consulting Actuaries (ACA), published today, has found 9 out of 10 defined benefit schemes (DB) in the sector are closed to new entrants with 1 in 5 now also closed to future accrual (double that of 4 years ago). The position continues to deteriorate, says the ACA. Just 6% of respondents say the Government's stated policy of supporting quality pensions is working – this is a real crisis which the next Government needs to tackle as one of its top priorities after the General Election.

Contributions into defined contribution (DC) schemes are increasing slowly, but still over half of all DC schemes reporting to the survey are attracting employer contributions of less than 6% of earnings and less than 4% from employees. As a result, given much lower investment returns in recent years and longevity improvements, pension outcomes for an increasing number of private sector employees are likely to worsen significantly in coming years. Concerns over the affordability of auto-enrolment[2] are a genuine threat to existing schemes of all types, with 59% of employers set to review arrangements ahead of 2012 and a quarter considering benefit reductions to offset the cost of increased membership via auto-enrolment.

With taxes on business and individuals likely to rise over the next few years, it is difficult to see anything other than a deteriorating climate for pension savings unless there is a radical change of approach, says the ACA.

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[1] The survey, conducted by the Association of Consulting Actuaries (ACA), was carried out during June and July 2009. The survey was completed by 309 firms with combined assets of £139bn. For further details see *2009 ACA Pension trends survey results* attached or at www.aca.org.uk (Publications or Research pages).
[2] From 2012, larger employers (and later all employers) must enrol all employees over age 22 into either Personal Accounts or a qualifying pension scheme at least equivalent to Personal Accounts.

The ***2009 ACA Pension trends survey***, collected responses from over 309 employers of all sizes. Key findings featured in the results are as follows (the full statistical analysis is separately attached):

- **stated public policy of supporting quality workplace pensions isn't working**
  Just 6% of employers say the Government's stated policy of supporting quality workplace pensions is working*, down 32 points from two years ago.*

- **open defined benefit schemes are all but extinct**
  87% of the defined benefit schemes are closed to new entrants with 18% of these closed to future accruals*. A third of these schemes are currently under review, with changes in forward accrual (39%) and a move to career average (35%) being considered.*

- **defined benefit scheme funding deteriorates**
  at the time of the survey, 91% of schemes were in deficit, with the average ongoing funding level at 79%*, down 8 points on two years ago. A fifth of schemes reported recovery periods of over 10 years.*

- **pension costs climb for employers**
  employers funding defined benefit schemes are on average contributing over 3 times as much per member *(average 23.2% of earnings) compared to those funding defined contribution pensions (average GPPs - 6.0%; DC Trusts - 6.7% of earnings)*[3]*.*

- **support for new 'middle way' pension designs**
  76% of employers say public policy should be more supportive of 'middle way' designs*. Half of employers would consider such a scheme, if legislation allowed.*

- **one-quarter of employers say they will level-down pensions ahead of 2012**
  24% of employers expect to reduce their existing pension scheme benefits to mitigate the cost of higher auto-enrolled membership*, beginning in 2012.* ***15% are considering closing their scheme altogether, including 41% of smaller employers***[4]*. Only 32% of employers have budgeted for the costs of auto-enrolment.*

- **personal accounts should target replacement income with a passive approach**
  47% of employers say the personal accounts' default fund should target replacement income *and should predominantly use passive managers.*

- **investment: defined benefit schemes**
  Just 49% of defined benefit scheme assets are now held in equities as funds switch into bonds*. Swing to passive management continues. Wider number of fund managers being used – 14% of schemes use more than ten managers.*

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[3] As most DC schemes are contracted-in, employers (and employees) pay higher NI contributions, narrowing the contribution gap. Most DB schemes remain contracted-out, paying lower NI contributions
[4] Employers with up to 249 employees

- **investment: defined contribution schemes**
  85% of defined contribution schemes offer default funds, up 6 points on two-years ago*, with 84% of members estimated to be invested in default funds.* ***Employers say 76% of members are uncomfortable with the DC risks they are taking on*** *and* ***fewer than one in five understand the issues involved****.*

Commenting on the survey results, **ACA Chairman**, **Keith Barton**, said:

"These are worrying times for all those looking to retire in the years ahead. Whilst the Government's Personal Accounts initiative eventually may bring on board more pension savers, it has to be remembered that these accounts are designed to 'fill the gap' with a low-level pension, where no better pension scheme exists. Quality pensions require higher contribution levels.

"Just 6 per cent of employers responding to the survey say they feel the Government's stated policy of supporting quality workplace pensions is working, down from 38% two years ago.

"The huge public policy gap at present is meaningful action to protect good existing private sector schemes and to promote new pension designs that aim to check uncertain and volatile pension outcomes. Our survey found that three-quarters of employers (76%) feel their employees are uncomfortable in taking on the entire investment, inflation and longevity risks that come with defined contribution schemes. However, this is exactly what is happening as defined benefit schemes are replaced by defined contribution.

"In the last year or so, the Government has ruled out changing the law to allow employers to offer pension schemes where indexation of benefits is conditional on a scheme being adequately funded and, more recently, it has blocked collective defined contribution schemes, where there could be efficiencies in provision. The Government seems to think instead that there are lots of 'risk sharing' designs presently available to employers under current law. The reality is that there are very few and these usually involve complexity as schemes are 'manufactured' to meet the different legal requirements of the current DB and DC pension regimes. The vast majority of existing so-called 'hybrid' risk-sharing schemes are in fact no such thing. They are just 'sectionalised' schemes where the DB section is usually closed and just a newer DC section is open.

"Public policy seems to be locked into justifying ever heavier regulation and cost under the banner of protecting accrued benefits for generally older employees, but with scant regard for the future pension security of millions of younger private sector employees. There needs to be a more balanced approach where the rising numbers of under-pensioned in the private sector get a better deal with employers' costs capped and with proportionate protection across all age groups.

"Later this month we will be mapping out a challenge to the political parties ahead of the General Election to take a bolder approach in the next Parliament. We will be looking for a commitment to establish a standing Pensions Commission charged with promoting good pension provision of all types.

"Amongst other roles, we would suggest that the Commission should be charged in its first year to come forward with the legal changes needed to allow employers to offer a wider range of pension designs, where employer costs can be capped in the event of demographic and economic changes, whilst also reducing the volatility in pension outcomes for employees and still protecting pensions in the event of employer insolvency. Surely an essential change will be the common sense acceptance that pension ages must increase in line with longevity improvements and in a timely way. This reform needs to apply to schemes, old and new, so the 'unknown' longevity risk involved in offering a good scheme can be removed.

"Our survey found 76% of employers want public policy to be supportive of 'middle way' pension designs that look to widen the choice of good scheme that employers can offer to their employees."

***Note to Editors**:*

About the Association of Consulting Actuaries (ACA)

The **Association of Consulting Actuaries (ACA)** is the representative body for consulting actuaries, whilst the Faculty and Institute of Actuaries are the professional bodies. The ACA has over 1700 members working in around 75 firms. ACA Members are all qualified actuaries and are subject to the code of professional conduct of the Faculty and the Institute of Actuaries. Advice given to clients is independent and impartial. The ACA forms the largest national grouping of consulting actuaries in the World.

Personal accounts and auto-enrolment

Under the 2007 and 2008 legislation, firms that wish to be exempted from offering **personal accounts** must meet minimum contribution or benefit standards and auto-enrol all employees aged over 22 (and under state pension age) into an exempt pension scheme (existing or new). To secure exemption from personal accounts, an employer's scheme must be at least as good as the personal accounts minimum standard, with an employer's contribution of at least 3% and an employee's contribution of 4% of band earnings (between approximately £5,035 and £33,540 per annum (2006/07 figures, to be up-rated in line with average earnings when introduced), plus 1% tax relief, making 8% of band earnings in total. The earnings calculation is based on overall earnings, including items such as overtime, bonuses and commission, not just basic salary. Personal accounts and contributions are to be phased in, at present, from 2012.

Association of Consulting Actuaries