ASSOCIATION OF CONSULTING ACTUARIES

# NEWS RELEASE

## ACA CHAIRMAN SAYS GREATER COMPULSION NEEDED TO ENSURE MORE EMPLOYEES IN THE FUTURE HAVE A COMFORTABLE RETIREMENT INCOME

**24 November 2017: ACA Chairman, Bob Scott, speaking at the Association's Annual Dinner, has outlined remaining weaknesses in the UK's pension system and called for greater transparency over the relative pension position of different age bands in company reports, assistance for employers who are struggling to maintain their DB schemes and greater compulsion in pension saving along the lines of the Australian model. He also called for a national standard scheme design to help in the process of consolidating defined benefit schemes.**

**Bob Scott said:**

"Although auto-enrolment has been a huge success, increasingly the focus turns to the 7.8 million people – a still rising number – who at present are not eligible to be auto-enrolled: the self-employed; low earners; and the workers in the "gig" economy – and to the level of contributions into AE schemes.

"Current minimum contributions are 2% of qualifying earnings, and are set to rise to 5% next April then to 8% in April 2019. An excellent start, but it is clear that the system needs to be developed over the coming years if the eventual output is to be meaningful. And beware what the politicians may do. Recently, former pensions minister Sir Steve Webb has warned that employers who take a minimal approach to AE face being sued, if members receive poor outcomes.

"And Adrian Boulding, Director of Policy at NOW pensions recently commented that we shouldn't worry about the level of charges since, until more adequate contributions are paid, charges don't really matter. In other words, if you have £500 in your retirement pot, what matters isn't whether you're charged 0.75% or 0.5% but how much gets paid in over the future.

"The ACA has for many years said that, in the longer term, government should be setting out its vision for increasing minimum contributions to around 16% of qualifying earnings and do this in a way that will not simply encourage large-scale opting out of pension provision.

"In the meantime, the difference in the level of pension provision between those who joined defined benefit schemes in the 1960s, 70s and 80s and those who enter the workforce today is said by many to be just another symptom of growing intergenerational unfairness. A recent House of Lords paper noted pensioner households now have incomes that are typically £20 a week higher than those of working age households. People born in the 1980s are the first post-war cohort not to start their working lifetimes with higher income than their immediate predecessors. And as we all know, home ownership is in sharp decline amongst younger people, exacerbating this gap between the haves and the have nots.

“The ACA recently surveyed UK employers on a range of pensions topics, including some inter-generational issues. We received over 450 responses from employers sponsoring over 760 pension schemes. The results will be published next week, but here are a few tasters.

“We found 80% of those employers who sponsor defined benefit plans say that funding their plan is having a negative impact on intergenerational fairness, with just over half saying that the costs are having a negative impact on pay rises and 42% that DB costs are having a negative impact on the contributions they can pay to other schemes.

“But what can be done to ease that burden and free up resources to at least start to reduce the pace at which the inter-generational pensions gap is widening?

“Our survey found over eight out of ten employers said that the law should be changed so that defined benefit schemes can reduce pension increases if continuing to provide increases at the level of scheme rules will severely and adversely affect the employer. Certainly, the ACA hopes that the upcoming DB White Paper will commit to legislation introducing this kind of flexibility.

“Separately, the PLSA, the Pensions Regulator and others have advocated consolidation of legacy DB schemes as a way to address a range of issues from poor governance to disproportionate costs. We strongly suggest that a necessary precursor to effective consolidation is a mechanism for simplifying legacy benefit structures. A plain vanilla defined benefit scheme set up in the 1970s will have something like ten different service periods with different statutory revaluation rates and pension increase rates – and most will have made amendments to their scheme over the years as well.

“Moving to a national standard scheme design via a clearly defined conversion process would have many benefits – including, perhaps for the first time, members understanding what their pension entitlement actually was. It would also be easier to display on a dashboard. Our survey showed that only just over a quarter of employers thought that consolidation would work without first simplifying benefits.

“Differential pension provision is just one element of the intergenerational challenge but, as many people will find that their pension is their most valuable asset, addressing the pension issue should be a priority.

“How to address this issue? I make the following policy suggestions:

- **First, disclosure**. Just as firms will soon have to disclose their gender pay gap why not have them disclose pension liabilities and total remuneration in age bands.
- **Second, encouragement** – to employers by helping those struggling with DB schemes and to employees via targeted tax incentives. Whilst we do not support moves by the Chancellor to reduce the total amount of relief granted to long term savings, we see clear benefits in spreading the relief more evenly across the age bands. Over three-quarters of employers in our survey would support this.
- **Finally, greater compulsion**. The Australian system is by no means perfect, but it has, over a period of years gradually increased the level of compulsory contributions. According to a recent bulletin from the Institute and Faculty of Actuaries, Australia now has the 3rd largest pension system in the world for a country of 24 million people - not bad considering that benefits are largely paid out in lump sum form so there are very few annuities.

"Another feature of the Australian system is that people are aware of how much they have saved and where it is invested – they even talk about their superannuation funds at dinner parties. It helps that Australia has been through a period of consolidation, bringing the number of funds down from tens of thousands to under a hundred and that pension provision is almost exclusively DC, even in the public sector. So, presenting an individual's data is relatively simple.

"The ACA supports the project to display people's pension data in a consolidated form on a dashboard – a project, incidentally, where I feel that compulsion is essential for its success.

"However, in the UK, when people change jobs they often leave pensions behind; they have a mixture of DC and DB and the State pension is more significant than in Australia where it is means-tested.
For the dashboard to be effective, the presentation needs to be simple and people who "engage" with their pension provision need to be clear on the actions that they can take.

"Unfortunately, in the UK, those who do wish to engage with their pension come up against regulatory and tax systems that make pensions unduly complex, whether paying contributions, making investment decisions or realising the proceeds.

"It is easy to forget that one of the great attractions of a DB pension was its simplicity. Contrast that with the experience of someone entering the workforce more recently.

"Accordingly, my view is that government and the pensions industry should have as their aim for auto-enrolment that someone who enters the occupational pensions system and is completely disengaged should end up, after a full career, with an adequate retirement income. It would then only be those who aspire to a comfortable level of retirement income who would need to engage to have a realistic chance of realising their goals.

"I am not expecting the forthcoming review of auto-enrolment to have all the answers. But I do hope that it will start to provide some of them and to signal the government's thinking on longer term savings strategy. The inter-generational challenges are real – now is the time to start addressing them on the pensions front."

**For further details**:


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## About the Association of Consulting Actuaries (ACA)

Members of the ACA provide advice to thousands of pension schemes, including most of the country's largest schemes. Members of the Association are all qualified actuaries and all actuarial advice given is subject to the Actuaries' Code. Advice given to clients is independent and impartial. ACA members include the scheme actuaries to schemes covering the majority of members of private sector defined benefit pension schemes. The ACA is the representative body for UK consulting actuaries, whilst the Institute and Faculty of Actuaries is the professional body.




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