ASSOCIATION OF
CONSULTING ACTUARIES

As the US model for the UK's Pension Protection Fund reports a deficit of $8.8 billion, the ACA cautions the government to begin its scheme with a modest package of benefits…

ACA MAKES RECOMMENDATIONS TO GOVERNMENT ON HOW PENSION PROTECTION FUND SHOULD WORK

30 October 2003 – The Association of Consulting Actuaries (ACA) has today published its views on how the proposed Pension Protection Fund (PPF) should be designed. This follows on from the Government's announcement in June 2003 that it would establish a PPF - a compensation arrangement for private sector defined benefit scheme members whose firms become insolvent with unfunded liabilities in their pension scheme.

If the PPF is to be established, and the ACA has expressed its concerns over the additional costs falling on defined benefit schemes and the additional regulation involved, its structure should encourage good funding and investment practice and minimise moral hazard. Also, there should be clarity on who is carrying the risk.

"The economic cost of the insurance should be carefully quantified and projections of the costs under various scenarios should be provided. Risk projections should also be carried out if it is the intention that the PPF is invested in non-matching assets, such as equities. We have offered assistance to the government in these areas," commented ACA Chairman, Gordon Pollock.

"We also believe the government should act as Guarantor or be open and honest that no absolute guarantee can be provided and detail examples of the circumstances in which PPF benefits may be cut back".

The ACA is alarmed that the model for the UK scheme – the US Pensions Benefit Guaranty Corporation (PBGC) - has just announced that its deficit has increased to $8.8 billion. The PBGC now provides benefits to over 800,000 US members in over 3,000 terminated schemes, with a maximum benefit of around £27,000pa.

The ACA says that the US situation is very worrying and underscores the need for careful costing of the UK's PPF and a careful approach to the benefits offered. The ACA is fearful that the government's £340 - £375 million per annum costing could be optimistic, particularly if economic circumstances deteriorate and the number of company insolvencies increase.

"The best chance of making the PPF work is if its benefits are initially set at a modest level with reductions for all members unless the assets of the scheme can provide a higher level", commented Gordon Pollock.

The ACA also believes that there should be a prudent funding standard with minimum contributions to target PPF benefits, for example, a gilts basis.

The ACA also says that the levy on pension schemes should be based on a sound assessment of the risks using as much information as is possible having reference, for example, to asset distribution, funding level, credit rating of sponsoring employer (if available) etc. and this should apply to small schemes as well as large schemes. There should be no intended cross-subsidy between large and small schemes.

The ACA says there should be restrictions on participating employers leaving liabilities in pension schemes which wind-up in the following 3 to 5 years with an insolvent employer. There should also be a debt on a UK or overseas employer whose UK subsidiary becomes insolvent with an under-funded pension scheme. For example, this debt could be equal to the shortfall of the assets over the PPF liabilities.

The ACA also says that the PPF's objectives should specify the degree of care it owes to members of failing schemes and levy paying employers as a group.

The ACA is surprised at the length of time taken to open consultations on a new priority order and hence the date of its introduction, which had now drifted into 2004. The ACA adds that the regulations regarding winding up and continuation as a closed scheme will need revision in view of the limitations in the insurance market.

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Note to Editors:

Members of the **Association of Consulting Actuaries (ACA)** are advisers to UK pension schemes with assets in excess of £650 billion, including the vast majority of larger schemes and thousands of smaller arrangements. The ACA forms the largest national grouping of consulting actuaries in Europe.