Deregulation

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The Review

- Reviewers appointed Dec 2006
- We were asked to seek consensus
- Advisory Group
- Process we followed
- Consultation document March 2007
- Deregulation or better regulation?

Risk-sharing – our aims

- Facilitate a middle course on risk
- Enable employees to be guaranteed a minimum pension or specified adjustments
- Don’t permit reductions in pre-2007 rights
- Avoid a new risk-sharing regulatory regime

Risk-sharing currently allowed

- DB+DC
- DB with automatic adjustments
- DB for minimum benefits + augmentation
- Cash balance

DB+DC

- Very straightforward
- Sponsor bears 100% of risk on DB part
- Employees bear 100% of risk on DC part
- Sponsor has option to top-up DC part at retirement

DB with automatic adjustments

- Longevity adjustments
- Investment performance adjustments
- Effect of section 67

DB for minimum benefits + Augmentation

- Base normal contributions on higher benefits than those specified
- E.g. specify NRA 70 but hope for 65
- Or specify 80ths and hope for 60ths
- Effect of section 67
- Employees bear 100% of top-slice of risk
- Sponsors bear risks on specified benefits
- Cost escalation for sponsors less likely

Cash balance

- Employee is guaranteed a fund at retirement, based on salary
- Employee bears 100% of conversion risk at retirement (i.e. longevity changes before retirement, and interest and longevity assumptions after retirement)
- Sponsor bears 100% of the salary and investment risks pre-retirement

Risk-sharing – our conclusions

- Existing law permits many risk-sharing designs
- Would help if Government would confirm our understanding of section 67
- The post-retirement LPI requirement prevents “targeted” increases
- PPF compensation and levy should take more account of risk levels
- We should like sponsors to look at risk-sharing again if regulatory environment improved

Topping-up DC schemes

- Big risks for employees in DC schemes
- Sponsor can top-up at retirement but may not then be willing or able
- We recommend that sponsors should be allowed to pre-fund discretionary top-ups, with tax relief, without going into the DB regime

Post-retirement increases

- Remove mandatory LPI requirement?
- Against removal – too soon, pensioners need LPI, would increase burden on State, sponsors would just remove it to save cost
- For removal – other design requirements have been freed up, not required for DC, some pensioners prefer higher spending-power initially, removal would permit more risk-sharing designs.
- We did not agree
- A possible half-way house?

Surplus

- Refunds should be allowed when scheme’s funding target reached
- Remove requirement that surplus return should be in the members’ interests
- Advance agreement in principle should be permitted but refunds should be subject to trustees’ final agreement at the time

Debt on employer

- One year’s grace should be allowed after last employee leaves
- Some group reconstructions should be easier
- Where covenant remains strong, no debt should arise
- Where covenant weak, we disagreed.
- Recent draft regulations accept our first point

Principles-based regulation

- Prescribe outcomes only
- Give helpful guidance but permit other ways of achieving the outcomes
- Include sunset clauses on any parts of future regulations going beyond outcomes
- Use plain English and avoid cross-referencing
- No need to amend schemes already compliant
- Start with disclosure and then establish rolling programme

Trustees

- Make trustee knowledge and understanding a group rather than individual requirement
- Enable personal legal expenses of trustees to be reclaimed from scheme

Conclusions (1)

- Don’t worsen pre-2007 accruals
- Make regulatory environment more sponsor-friendly
- Facilitate risk-sharing
- Facilitate reclaims of surplus by sponsors
- Make “debt on employer” regulations less draconian
- Base regulations on outcomes required

Conclusions (2)

- Our thanks to all respondents
- Need for ACA to make its views known
- If our changes are implemented, sustainable occupational pension provision will be greatly facilitated
- Many sponsors may then choose their own occupational scheme in preference to reliance only on personal accounts