



EMBARGO ON PUBLICATION UNTIL: 2 JUNE 2005

The ACA's latest Pension Trends Survey 2005 finds 94% of firms will have reviewed their pension arrangements over a 2-year period...with 43% looking to reduce their pension costs...

ACTUARIES POINT TO SIGNS OF HIGHER CONTRIBUTIONS GOING INTO DEFINED CONTRIBUTION SCHEMES AS BIGGER FIRMS SWITCH FROM DEFINED BENEFIT SCHEMES

31 May 2005: The first sign of higher contributions going into defined contribution schemes is reported following the latest published results of the Association of Consulting Actuaries' (ACA) 2005 Pension Trends Survey. The move from defined benefit schemes shows no slackening in its pace – 68% of such schemes are now closed to new members. However, the ACA says that average contribution rates are rising due to higher contribution rates being paid by firms seeking to reduce defined benefit scheme deficits and by larger firms entering the defined contribution scheme market.

The ACA survey, completed by 392 firms with scheme assets exceeding £131 billion and with over 2.8 million members, found average combined employer and employee contributions into company sponsored defined contribution schemes is now 10% of earnings, an increase from 8.5% since 2002. Whilst this is some encouraging news as the Pensions Commission wrestles with proposals to increase pension coverage and savings, the increase pales against the significant increases in contributions going into defined benefit schemes to fund benefits.

Defined benefit contributions have increased from 15.8% in 2002 to 22% of earnings today. Employer contributions have risen more than employee contributions since 2002 - employers up by 5% and employees by 1.2%, even though 44% of firms having increased employee contribution rates over the last few years. Almost without exception, this increase in contributions is not funding benefit improvements but, rather, is going towards reducing scheme deficits.

The ACA survey found 89% of defined benefit schemes are in deficit, with an average ongoing funding level of 85%. This suggests deficits across UK defined benefit schemes, on an ongoing basis, equate to over £130 billion across both

large quoted and smaller firms (where the ACA found last year, funding levels were closer to 80%).

To address this situation, aside from increases in regular contributions, 27% of firms have paid significant lump sums to reduce deficits. However, 44% of firms expect it will take upwards of 11 years to remove their deficit, with the majority of schemes looking to either 10 or 15-year recovery periods.

The pace of change in the pensions sector must worry both the Government and the Pensions Commission as they deliberate – slowly – over future reforms. The ACA survey shows 94% of firms will have reviewed their arrangements over a two-year period, with around a half currently under review or subject to review in the next 12 months. This suggests firms are finding their own pension solutions at a somewhat quicker pace than Government's response to the 'pensions crisis'. Given the actions already taken by firms, and with a more uncertain economic climate emerging, it may prove difficult to increase pension savings above current levels by either compulsory or voluntary means.

Commenting on the survey results, ACA Chairman, Adrian Waddingham, said:

"As we have highlighted in previous *Pension Trends* surveys and supported by the government's own Family Resources Survey, the number of employees covered by any form of occupational scheme is in quite rapid decline. The policy-mix must be wrong for this to be happening and this view is shared by the vast majority of firms as evidenced by our first report in this 2005 series¹."

"This latest survey report shows the immense efforts being made by many firms to meet the cost of pensions – costs that in many cases have increased far beyond what was expected when they set up their schemes. In part this is down to increased longevity and weak investment returns, but added regulatory and government-led enforced benefit improvements have not helped at all.

"That is why the ACA is calling on the new government to act to improve the Basic State Pension to a level that meets essential living costs, with private pensions built on top of this higher State pension. Additionally, we want to see greater incentives offered to encourage firms to offer schemes of a good standard, including lower-cost defined benefit schemes offering a lower targeted benefit related, for example, to career average earnings.

"What is concerning for the future, exposed by this latest survey, is that firms are more fearful of the impact of legislation on benefits and funding costs than anything else," added Adrian Waddingham.

¹ *UK Pension Trends Survey Report...1: Views on Pensions Policy and 2004 Pensions Act (April 2005)*, published by the ACA, see www.aca.org.uk (Policy Statements page, April 2005)

This second report of the ACA's **2005 Pension Trends Survey** is available at www.aca.org.uk on the 'Policy Statements' page. The first report in the 2005 series and the ACA's response to the Pensions Commission Report, which includes greater details of the ACA pensions strategy (pages 5 to 9) is also available on the same web page, see 'Response to Pensions Commission - January 2005'.

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Note to Editors:

The **Association of Consulting Actuaries (ACA)** has over 1500 members working in around 80 firms. Members are advisers to UK pension schemes with assets in excess of £700 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.

ACA Pensions Manifesto for the new Government

Reflecting the ACA submission to the Pensions Commission and the inadequacies of the 2004 Act, Adrian Waddingham outlined the **ACA's Pension Manifesto**, in May 2005, which the ACA will be seeking to advance with the new Government:

- **Means-tested benefits should be reduced in scope with the Basic State Pension and S2P consolidated into a higher-level Basic State Pension.** This should be set at a level sufficient to cover basic living costs, to be reviewed on an annual basis reflecting earnings growth.
- **A higher State Retirement Age would help finance such a change.** However, it is clear that because to date public policy has opposed such a move, there is much that needs to be done to persuade many legislators and the public that this is part of the correct and needed response to longer life-spans.
- **Contracting-out should be abolished.** The public would find a pension regime whereby private pensions are built on top of a higher consolidated State pension much easier to understand.
- Rather than have firms close pension schemes (or not offer 'good' schemes), **the Government must enact genuine pension simplification, including the right for employers to change scheme rules retrospectively (subject to regulatory approval) to avoid increases in cost due to longer life expectancy**, for example by raising normal retirement age.
- **The State should provide a better incentive to encourage the development of good second-tier pensions**, particularly where employers continue to or decide to sponsor schemes that better a certain standard.
- **The State's encouragement of private pension provision above the higher consolidated Basic State Pension should continue by way of tax relief**, with longer-term saving attracting a higher rate of relief than shorter-term saving products.