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The ACA has issued its 'manifesto for pensions reform' with policies to boost State and private pensions. This is published alongside the ACA's latest Pension Trends Survey 2005 report...

ACTUARIES SAY POLICY PRIORITIES ARE TO REFORM STATE PENSION AND TO REVERSE THE DISINCENTIVES THAT ARE PREVENTING WORKPLACE PENSIONS

6 October 2005: The latest published results of the Association of Consulting Actuaries' (ACA) *2005 Pension Trends Survey* underscore that employers' greatest concern for the future is the impact of legislation on benefits and funding costs. These worries, in the light of ongoing pension scheme deficits equating to over £130 billion reported by the survey¹, run ahead of all others and underpin employers' pessimism about the effect of the *2004 Pensions Act* measures on occupational pension provision. To address these concerns, the ACA has published its own pensions manifesto (see *Note for Editors*) as its final representation to the Pensions Commission recommending a radical review of the State pension and an incentive-led strategy in its forthcoming report due at the end of November 2005.

Commenting on the survey findings at the ACA's Annual Dinner, Chairman, Adrian Waddingham, said:

"The number of employees covered by any form of occupational pension scheme is in rapid decline - this is not disputed. The policy-mix must be wrong for this to be happening. 68% of employers say present policies to promote occupational pensions are not moving in the right direction²."

"Our survey has shown the immense efforts being made by many firms to meet the cost of pensions¹ by way of larger contributions - costs that have increased far beyond what was expected when they set up their schemes. Increasingly, we are worried that the delayed Scheme Funding regulations may place further harsh funding pressures on employers, thereby speeding up scheme closures.

¹ *UK Pension Trends Survey Report...2: Trends in Scheme provision, contributions and scheme deficits, published by the ACA, see www.aca.org.uk (Policy Statements page, June 2005)*

² *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)*

"The survey found this was the biggest area of concern on pensions around the boardroom table. The thinking behind tough new regulations may be well-meaning, but this short-term approach can only damage ongoing pension provision and undermine employers' desire to offer good schemes".

"For the public's sake, the Government simply cannot afford to make any further mistakes in its approach to pensions. There is considerable agreement across the pensions industry on what needs to be done to improve State and private pensions. Consolidation of the State Pension at a higher level, a move over time to later retirement ages and new incentives to boost private pension saving are policies voiced by many organisations. We expect the Pensions Commission report to draw many of the threads together. New incentives to boost private savings on top of a better State pension will be essential - we believe this is a much better approach in a free society than compelling employers and people to save. However, what would be disastrous is if the Government moves ahead with its own half-baked 'pet' ideas - and there are signs that it may be tempted to - in advance of the report's publication," concluded Adrian Waddingham.

The third and final ACA survey report published today in the **2005 Pension Trends Survey** series, completed by 392 firms with scheme assets exceeding £131 billion and with over 2.8 million members, looks amongst other matters at investment and pension taxation issues.

It reports that overall 38% of defined benefit pension schemes are expecting to reduce their UK equity holdings (and overall 24% their overseas holdings) over the next year, with holdings of corporate bonds, gilts, property, private equity and hedge funds set to rise. Looking at the investment spread of the growing number of defined contribution schemes, the report expresses a concern that one-quarter of these schemes offer 5 or fewer fund options and half offer just one fund manager. The ACA says that this may mean 'choices are too limited to reflect the different risk and reward strategies appropriate to the needs of members...restricting the ability to spread investments across a number of managers achieving a range of investment returns'.

The slow finalisation of new pension tax regulations to apply after A-Day has led to 41% of employers saying that unsatisfactory progress has been made in advising their schemes on the changes needed to successfully implement the new tax regime on time from April 2006.

51% of firms say they are intending to increase the amount of pension that can be converted to a tax-free lump sum at retirement, but across a range of other new flexibilities a minority of firms are looking to act. However, despite the administrative complexities involved, 1 in 4 schemes are considering introducing flexible retirement options where only part of the accrued pension is drawn. The new tax regime is likely to have a considerable impact on unapproved pension arrangements that have hitherto bolstered the packages of pension-capped high earners. 63% of unapproved arrangements are expected to cease, with many employers offering salary increases instead.

The survey report also considers auto-enrolment, where employers automatically enrol employees into their pension scheme, rather than looking to employees to 'opt into' the scheme. The Government has expressed support for this approach. Whilst the survey found 46% of defined contribution schemes and 39% of defined benefit schemes would consider moving to auto-enrolment, the ACA expresses scepticism about this actually happening unless the reform is accompanied by a package of new incentives targeted at employers to encourage occupational provision. Without these, the ACA says firms grappling with increasing pension costs - particularly those running defined benefit schemes - are unlikely on a voluntary basis to, turkey-like, 'vote for Christmas' adding still further to pension costs and forward liabilities.

Other findings highlighted in the *2005 Pension Trends Survey* are:

- **62% of employers say the measures in the 2004 Pensions Act will reduce occupational pension provision and 82% say they will add to costs.**
- **89% of employers are supportive of measures to pay a higher consolidated State Pension, with 72% saying contracting-out should be abolished.**
- **63% of employers back measures to promote lower-cost defined benefit schemes**, with 69% favouring a better balance of risk between individuals, employers, financial services firms and the State.
- **Defined benefit contributions on average 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%. Almost without exception, this increase in contributions is not funding benefit improvements but, rather, is going towards reducing scheme deficits.
- **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.**
- **Although there are signs of some increases in contribution rates as larger employers have opened defined contribution schemes, contributions still on average equate to 10% of earnings - under half that going into defined benefit schemes.** In many cases, the eventual emerging pensions are likely to fall short of members' expectations.

The third and final report of the ACA's *2005 Pension Trends Survey* is available at www.aca.org.uk on the 'Policy Statements' page. Printed copies are available from the ACA, Warnford Court, 29 Throgmorton Street, London EC2N 2AT,

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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 Manifesto on pensions reform

Reflecting the ACA submission to the Pensions Commission and the inadequacies of the *2004 Pensions Act*, the ACA has published its recommendations on how State Pensions and private pensions can be improved:

- **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 with the savings on future rebates used to help this comprehensive reform of pensions.** 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. Schemes in deficit should also be able to suspend Limited Price Indexation until they remove their deficit.
- **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. If the Government finally resolves that there should be some minimum compulsory contribution from employers - say up to 5% of earnings matching an equivalent employee contribution - it is important that this is introduced alongside reductions in employer costs through tax or NIC contributions.
- **On grounds of equity, the cost of public sector pensions must be addressed.** It is unacceptable that the private sector - firms and individual taxpayers - should support the rapidly rising costs associated with most public sector pension arrangements. A long-term strategy to cap rising costs needs to be implemented.
- **The State's encouragement of private pension provision above the higher consolidated Basic State Pension should continue by way of cash incentives for the lower-paid and tax relief,** with longer-term saving attracting a higher rate of relief than shorter-term saving products.
- **It is important that public policy, in responding to calls for greater compulsion, is supportive of employers and schemes that offer superior arrangements to any proposed compulsory regime.**