



Yesterday the Government announced a consultation on risk sharing pensions, but delayed its start so any reforms will miss this year's Pensions Act. This lack of urgency to the safeguarding and the promotion of quality pension schemes is not good enough...

ACA SAYS 'YES MINISTER' TO RISK SHARING CONSULTATION, BUT 'NO MINISTER' TO MISSING OUT ON REFORM IN THE CURRENT PENSIONS BILL

22 February 2008: Yesterday, the Government opposed an amendment to the Pensions Bill that would have added a new clause ending the ban on employers being able to offer new conditionally indexed pension schemes.

The amendment was proposed by the **Association of Consulting Actuaries (ACA)**, with advice on the legal aspects provided by the Association of Pension Lawyers (APL), and was the culmination of work undertaken over the last 2 years in developing an initiative to re-invigorate quality workplace pensions in the UK.

Commenting on the Pension Minister's (Mike O'Brien) rejection of the amendment, **Ian Farr**, ACA Chairman said:

"The Pensions Minister opposed the 'conditional indexation' amendment in the Bill Committee, whilst mounting few arguments against the initiative. Indeed he said (to quote) 'I do not disagree a great deal with the general argument put forward by the Opposition spokespeople'. Instead, the Minister said he favoured a slow-moving consultation on the various approaches to risk-sharing starting in June - a 4 month delay in getting anything moving so all reforms would miss this year's Bill.

"Why cannot the Minister organise a quick final consultation to fine-tune the legislation removing the ban on new conditional indexation schemes as a 'first' step in risk sharing reform to be included in this year's Bill? After all, the idea has already been exposed to a consultation exercise in the last year as part of the deregulatory review of private pensions. Many key features of the personal accounts regime are still under consultation, but the Bill clears the way for these measures to be introduced. Other less well developed risk sharing options can then be exposed in a slower moving consultation exercise as proposed by the Minister.

"It is encouraging that both Conservative and Liberal Democrat members of the Pensions Bill Committee supported the conditional indexation amendment. Hopefully, the Lords will apply pressure to make sure the amendment will still find its way into this year's Bill and Act.

"Unfortunately, if this legislative opportunity is lost to remove the ban with no certainty of another Bill in the near future, it is expected that the decline in DB types of arrangements, coupled with the need of employers to review their pension offerings in the light of auto-enrolment and personal accounts, will mean the near wholesale switch to DC will be completed in a matter of a few years. Once done, the switch back to any form of risk sharing may be slow and difficult – with generations of private sector employees paying the price of a missed opportunity in this Bill", added Ian Farr

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About the Association of Consulting Actuaries (ACA)

The **Association of Consulting Actuaries (ACA)** is the representative body for consulting actuaries, whilst the Faculty and Institute of Actuaries are the professional bodies. The ACA has 1700 members working in around 80 firms. ACA Members are all qualified actuaries and are subject to the code of professional conduct of the Faculty and the Institute of Actuaries. Advice given to clients is independent and impartial. The ACA forms the largest national grouping of consulting actuaries in Europe.

Conditionally indexed pensions

The ACA says new conditionally indexed schemes offer to those many mid-sized and larger employers prepared to share risks with employees¹ a pension arrangement that not only will attract and retain employees, but that also caps employers' costs into the future (a full description of how conditional indexation schemes work is contained in the ACA's *Written Evidence* to the Bill Committee²).

Conditionally indexed schemes offer to employees a far less volatile pension benefit than DC. Pensions are based on career average earnings linked to service. Save on occasions when scheme funding falls into deficit (the 'condition'), pension benefits would be indexed in line with a scheme specific index, typically inflation up to a 2.5% cap per annum. Restoring indexation would be the first priority when a scheme returns to surplus.

Funding would be based, as with existing DB schemes, on the new prudent funding standards set by the Pensions Regulator, who would regulate such schemes, with PPF levies securing further protection for members (but with lower levies based on the lower risk profile of such schemes).

Importantly, under the ACA's amendment to the *Pensions Bill*:

- Conditional indexation would not apply to the benefits offered by existing types of defined benefit schemes – for simplicity, the amendment only applies to new conditionally indexed arrangements set up after the Bill becomes an Act.
- The amendment in no way stands in the way of existing types of risk sharing arrangements (although the reality is that very few have been taken up by employers due to the complexity and limitations of current legislation and the communication issues involved).
- The amendment does not stand in the way of other possible types of risk sharing arrangements that might be identified in the future, but which are not ready for this Bill.

The detail of how conditional indexation schemes would work is far more advanced than the detail of some aspects of personal accounts, where, for example, the administration of collecting contributions and the charging basis are still very uncertain.

An ACA briefing to the Pensions Bill Committee issued this week concluded that 'conditionally indexed schemes are the first important step in re-invigorating quality UK pensions – the only new form of risk sharing pension design that is ready to implement **now**. Country-wide, consulting actuaries, who advise the vast majority of employers who would take up such schemes, are ready to promote the new design opportunity as employers plan the shape of their pension arrangements in the run up to 2012'.

¹ ACA surveys in 2006 and 2007 have found over 70% of employers support risk sharing being promoted by legislation.

² www.aca.org.uk (see 'Recent Publication, 2 January 2008')