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The impact of A-day and personal accounts on the pensions landscape

Andrew Stoker, PricewaterhouseCoopers
Rachel Vahey, AEGON Scottish Equitable

Agenda

- Background
  - A-day
  - Pensions reform
- Where are pension markets now?
- Where are pension markets heading?
- Implications
- Conclusion
- Discussion

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Background: Pensions timeline

2004 2005 2006 2007 2008 2009 2010 2011 2012

Turner Report 2004

Pensions and Finance Acts 2004

Turner Report 2005

Pensions A Day (**06/04/06**)

Pensions White Paper (May ’06)

Pensions Bill (Nov ’06)

2^{nd} Pensions White Paper (Dec ’06)

Consultation ends (20/03/07)

Pensions Bill (2007/08)

Changes to State Pension entitlement

Last possible date of next election (05/05/10)

National Pension Saving Scheme begins

Changes to State Second Pension

Earnings link on basic state pension

Abolition of contracting-out of money purchase

Background: A-day

- Pensions tax simplification
  - Started A-day (6 April 2006)
  - Finance Acts: 2004, 2005 and 2006
  - Pre-Budget Report 2006 and Finance Bill 2007 - still changes
- Pensions Act 2004
  - Implemented 2005 and 2006
  - Mainly improving member protection
  - FAS, PPF, scheme-specific funding

Background: A-day – 9 main changes

- Single tax regime replaces eight
- Lifetime Allowance – max fund of £1.5m
- Annual Allowance – earnings up to £215,000
- Tax-free lump sum – 25% of fund
- Trivial Commutation – fund less than 1% of lifetime allowance
- Concurrent membership permitted
- Pensions whilst working permitted
- Retirement age raised to 55
- Alternatively secured pension

Background: Pensions reform

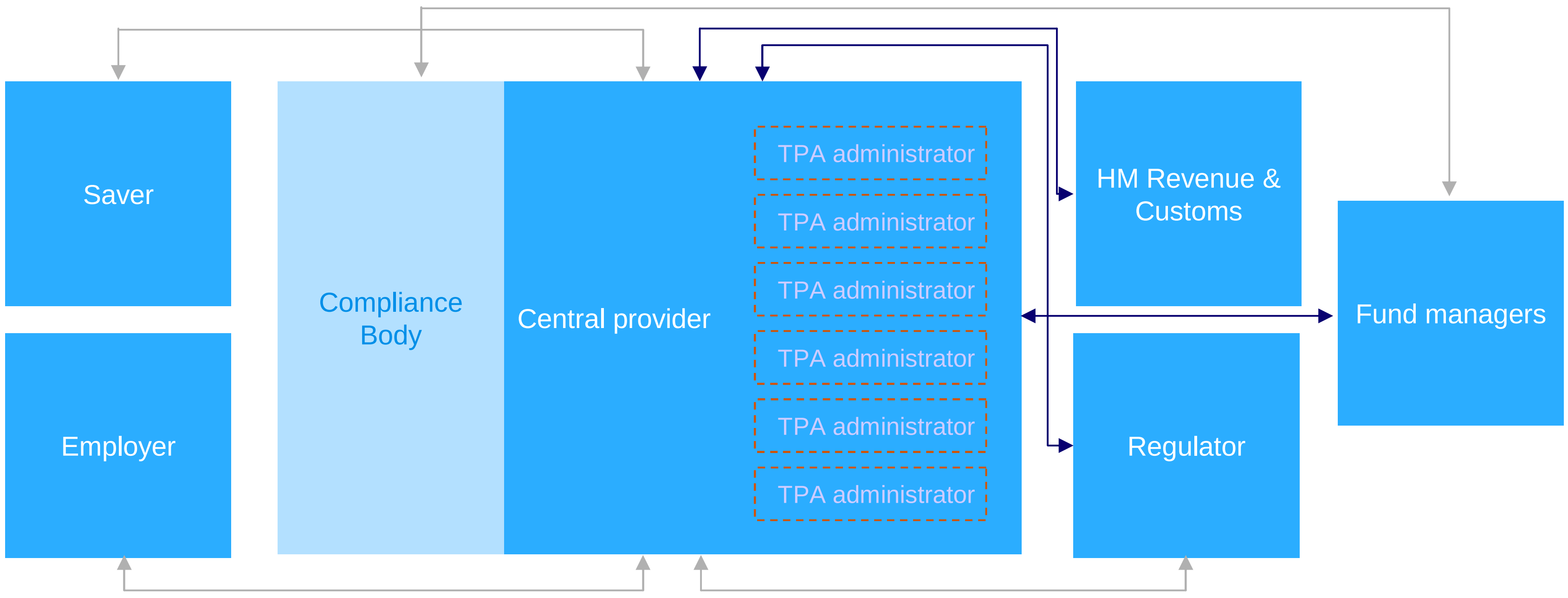
- Turner commission – 3 reports
  - Recommendations in November 2005
  - State pension reform
  - National Pension Savings Scheme
- White Paper May 2006
- Pensions Bill – November 2006
- 2nd White Paper December 2006
  - Responses required by March 2007
- Personal Accounts Bill – later in 2007

Background: Personal accounts

- Automatic enrolment for eligible employees with freedom to opt out
- Minimum overall level of contribution on difference between upper and lower earnings limits:
  - 3% compulsory contribution from employer
  - At least 4% from employee
  - 1% basic tax relief on employee contribution
- Proposed contribution cap of £10,000 in the first year, £5000 thereafter
- Opt-in access for self-employed and those not in paid work?
- Portable and flexible accounts
- Very low charges – 0.5% falling to 0.3% in long term
- No transfers to or from personal accounts until 2020

Background: Administration model for personal accounts

- The November white paper has decided that the NPSS model is likely to be the most effective.



Background: the delivery authority

- Delivery authority set up by Pensions Bill
- Objectives to be set by Personal Accounts Bill in November 2007
- To be completely independent
- Three stages
  - Advisory delivery authority
  - Executive delivery authority
  - Personal Accounts Board (PAB)
- Question over what delivery authority decides, and what Government decides

Background: Pensions reform timetable

December 2006	Personal Accounts White Paper
April 2007?	Royal Assent given to Pensions Bill (state pensions / OPS)
First half of 2007	Advisory delivery authority set up
November 2007?	Personal Accounts Bill
2008	Executive delivery authority
2008 – 09	Tender for contracts is set
2008 – 09	Exemption test is set
2012 (earliest)	Go live date

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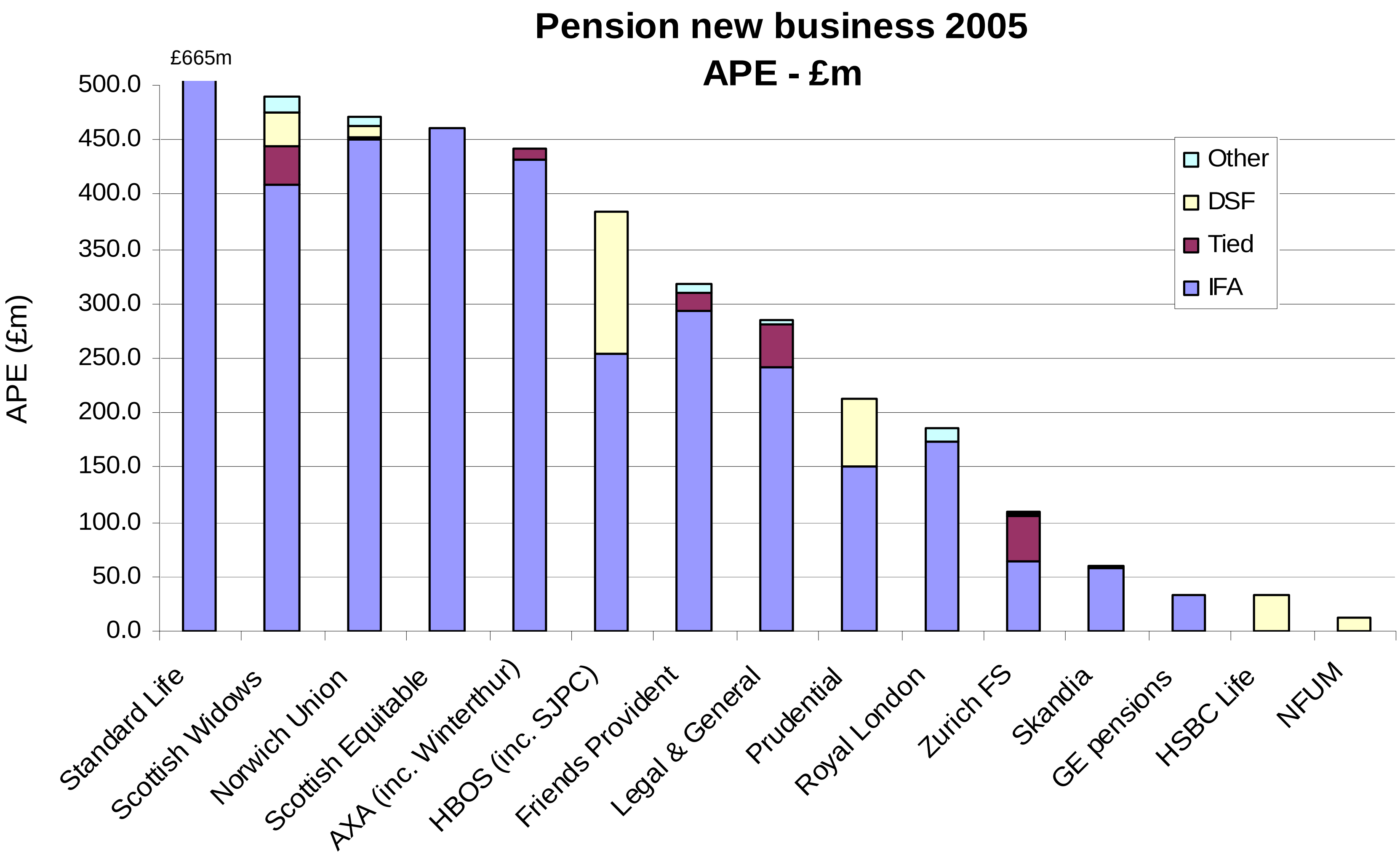
Where are pension markets now?

- A-day is big business
- ABI: new business figures – Q2 2006
  - Overall new business - £3.9bn APE
  - Individual Pensions - £1.4bn APE – 36% increase
  - Annuities – record £2.3bn – 33% increase
- What proportion is ‘new’ new business?
- What does 2007 hold?

New markets - accumulation

- Consolidation is key
- SIPP
  - Growing market
  - Technological, legislative, customer demand
  - Group SIPP
- EPPs
  - Change terms or switch out?
- S32
  - Still a market for protecting cash
- Pension term assurance
  - But will tax relief still be given to premiums?

Winners of the battle for consolidation likely to be larger players



New markets - decumulation

- Secured pensions
  - Some changes
- Unsecured pensions
  - New limits
- Alternatively secured pension (ASP)
  - Only from age 75
  - PBR proposed 65% minimum income and removing ‘cascading wealth option’

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Where are pensions markets heading?

- SIPP will continue to grow
- Switch from defined benefit to defined contribution carries on
  - 80% of private defined benefit schemes are closed to new members
  - Next stage to shut to further accrual?
- Growing demand to manage DB liabilities
  - More bulk buy-out solutions
  - Pensions Regulator warning of ‘abandonment’
  - ‘Incentives’ to be taxed and Pensions Regulator gives guidance

Where are pension markets heading?

- Decumulation business will increase
  - More DC plans (accumulation and at decumulation)
- Need middle market solutions to balance risk
  - HMT annuities paper ‘opened door’
  - Guaranteed income products?
  - Legislative change?
- Government review of open market options
  - Scene-setting for personal accounts?

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How will personal accounts affect pensions markets – new business?

- Could have big effect on new business
- But depends on design
  - Contribution caps, charges, administration, investment choice, member/employer experience
- Top-up business and SIPPs likely to continue for high earners
- As 2012 approaches there may be planning blight
- Interaction with means-testing will pose questions for some

How will personal accounts affect pensions markets – existing business?

- Exemption test will be critical to avoid levelling down
  - Need ‘auto-enrolment’ for contract-based schemes
- Migration from defined benefit schemes to defined contribution will continue
- All change 2020 when transfers may be allowed?
- Charges reflect value for money?
- Employer experience – how much involvement?
- Need removal of RU64

The NPSS model – a single administrator but a choice of funds

- Unlikely to be single administrator in practice
  - Too much risk
- Instead administrators tender for contracts
  - Delivery authority awards contracts
  - Split by function or by segment of population?
  - Charges set by Government?
- One ‘default’ investment fund
  - Pool experience of several ‘default’ funds?
- Other branded funds allowed as well?
  - Higher charge?
  - Ethical and socially responsible?

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Conclusion

- A-day changes have been good for pension markets in general
- But defined benefit schemes hit by regulation over last ten years
- Decumulation is going to be big business
- Pensions Reform will have a big effect
  - Need to gauge full effect depending on decisions taken now
  - And avoid planning blight

Discussion