

The Actuarial Profession
making financial sense of the future

Current issues in pensions
March 2010



Liability and Risk Management

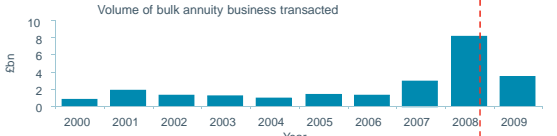
Daniel Harrison

Liability and Risk Management

- Full/partial buy-out/in
- Longevity swaps
- Enhanced Transfer Values
- Early retirement
- Pension increases
- Commutation
- Closing to future accrual
- Benefit strategy
- Group restructuring
- Investment strategy

Buy-out/Buy-in, the rise and fall.....

Volume of bulk annuity business transacted

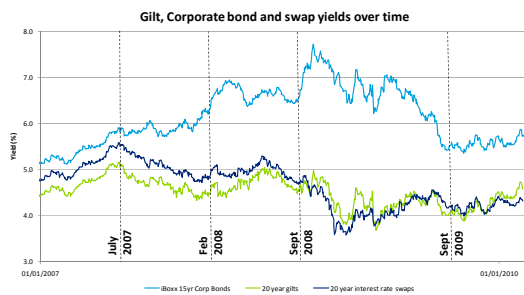


Year	Volume (Bn)
2000	0.5
2001	1.5
2002	1.0
2003	1.0
2004	1.0
2005	1.0
2006	1.0
2007	2.5
2008	8.0
2009	4.0

- From two dominant players to many
- Increased competition and innovation
- More flexible "buy-out" options
- Development of "buy-in" for pensioner liabilities
- Other 'non-insurance' options proposed

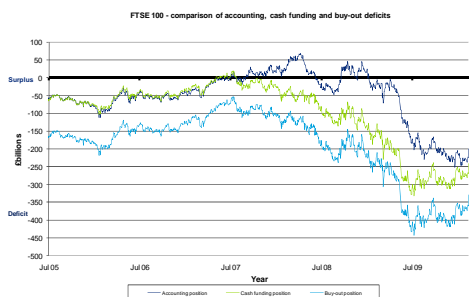
Credit Crunch

Volatile market conditions driving insurance pricing



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Volatile market conditions affecting scheme funding



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Factors impacting upon affordability

Pension scheme

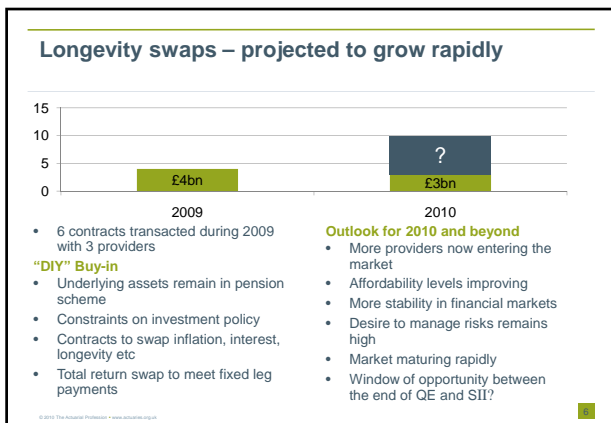
- Asset falls
- Worsening funding position
- Company cash constraints
- Longevity assumptions becoming closer to insurers' assumptions.
- Insurance prices increasing relative to IAS19
- May still compare favourably with ongoing funding reserves



Insurance Company

- Additional reserves required for credit risk
- Greater uncertainty in stress testing
- Capital more scarce and expensive
- Costs/risk of asset valuation and transfer
- Consolidation in market, end of 'first deal' offers
- Impact of Solvency II

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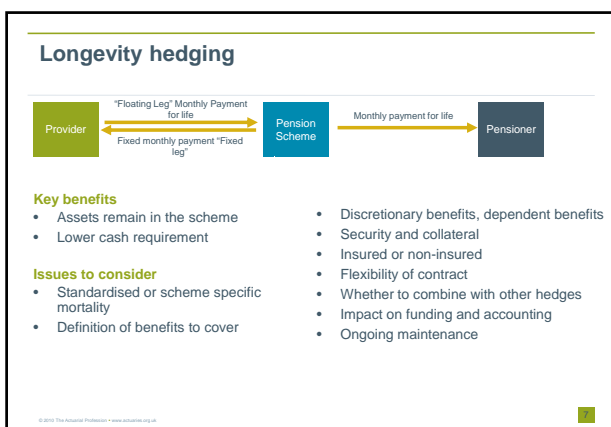
6 contracts transacted during 2009 with 3 providers

“DIY” Buy-in

- Underlying assets remain in pension scheme
- Constraints on investment policy
- Contracts to swap inflation, interest, longevity etc
- Total return swap to meet fixed leg payments

Outlook for 2010 and beyond

- More providers now entering the market
- Affordability levels improving
- More stability in financial markets
- Desire to manage risks remains high
- Market maturing rapidly
- Window of opportunity between the end of QE and SII?



Key benefits

- Assets remain in the scheme
- Lower cash requirement

Issues to consider

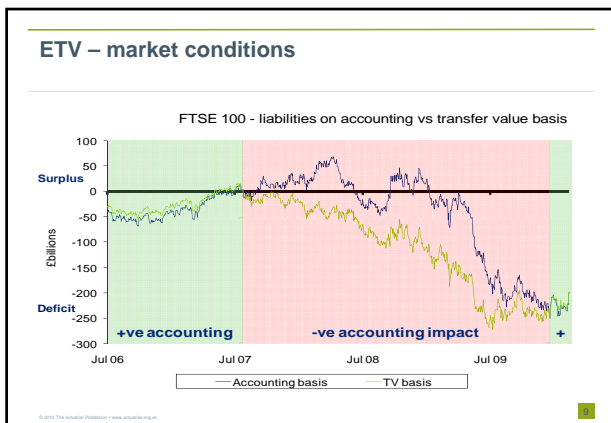
- Standardised or scheme specific mortality
- Definition of benefits to cover

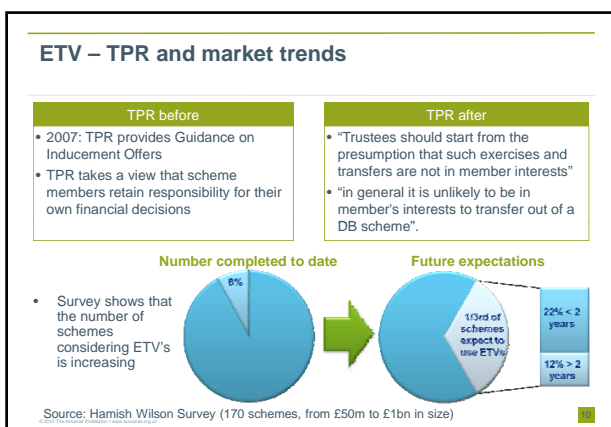
- Discretionary benefits, dependent benefits
- Security and collateral
- Insured or non-insured
- Flexibility of contract
- Whether to combine with other hedges
- Impact on funding and accounting
- Ongoing maintenance

Enhanced Transfer Value Exercises (ETV)

Advantages	Considerations
Significant risk reduction	Reputation/ethical risks
Reduces pension liabilities	Requires cash up-front
Reduces funding volatility	Cost vs risk of poor take-up rates

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- ### Early retirement
- Members encouraged to retire before NPA by offering enhancements to the benefits.
 - Accelerated cashflows
 - Reduced volatility and uncertainty
 - Window of opportunity prior to April 2010 for members aged between 50 and 55.
 - Attractive to members through access to cash lump sum
 - Ties in with flexible working towards "final" retirement
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Pension increases

- Reduce pension increases to statutory minimum
- Increased flat pension or cash sum in compensation
- Legislation permits LPI 2.5%
- Reduced service cost
- Reduced volatility and uncertainty
- Could be attractive to members to provide more income in earlier years of retirement
- Need for financial advice
- Inflation and longevity risks understated?

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Closing future accrual

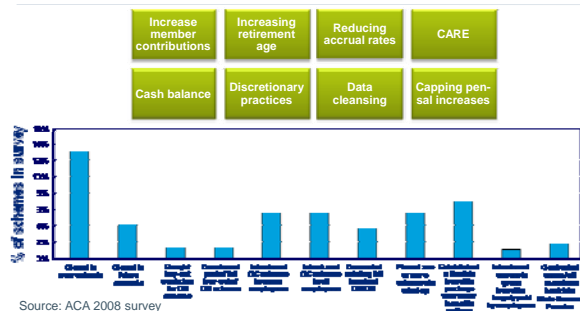
Issues to be considered

- Trust Deed and Rules
- Section 75
- Employment contracts
- Compensation and future pension provision
- Consultation
- Funding and accounting impact
- Investment strategy

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Other options



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Data cleansing

Admin

Pensioner and dependant existence

Fraud and duplication

Deferred member addresses

Data validation

Advantages

- Consistent with good governance
- Straightforward to implement
- Reduce long term costs / management time
- Increases efficiency of administration systems
- Vital preparation for future buy-out / in

Considerations

- cost of implementation

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Group restructuring

- Section 75 debt can be triggered when a participating employer in a multi-employer scheme ceases to employ active members
- Group restructuring can be used to shield the group from S75 debt
- Regulated apportionment allows insolvency in one subsidiary to release ongoing "NewCo" from pension scheme liabilities

Issues

- Abandonment!
- Need to demonstrate insolvency is inevitable
- PPF requires cash and shareholding in NewCo
- TPR refuses approval for Readers Digest after agreement with PPF

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Investment strategy review – trends in asset allocation

- Investment risks typically outweigh all other liability risks
- Average UK pension scheme asset allocation has developed since 1962:
 - Reduction in equity allocation
 - Increase in more complex pension assets: alternatives / derivative based solutions

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Where now?

- Pensions risks remain a key issue
- Innovation in the market has developed a wide range of options to manage/transfer pension risks
- Increased focus on security
- Longevity hedging and "DIY buy-out" could be attractive for many
- Insurance remains the 'gold standard' for securing and ultimately discharging liabilities
- Need to prepare to take advantage of market conditions
- Regulatory attention and intervention likely to increase

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Questions or comments?



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