

Plan Design : Post-simplification plan design flexibility

Current Issues in Pensions: 21st October 2005

Design opportunities covered

- Combining OPS and PP
- Flexible retirement with continued work
- Death benefits
- Restructure in line with PPF
- But don't forget, new S67 provisions apply from 6th April 2006, and member consultation requirements (let alone employment contracts and scheme's rules)

Combining Occupational Pension Schemes with Personal Pensions

- FA04 allows accrual in an OPS and contribution in a PP on same pay
- "Layering: DB accrual as safety net on first tier of pay, DC on upper tier of pay"
 - ⊙ limits final salary volatility
 - ⊙ protects lower paid from risk
 - ⊙ DC without the trust risks
 - ? risk benefits? (esp if not using PHI)

Combining OPS and PP: using PP rather than same OPS as DB

- ⊗ Extra administration
- ⊗ Lose the option of Pension Commencement Lump Sum coming from DC as first source
- ⊗ Lose the chance of DB surplus funding DC

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DB flexible retirement: the law

- FA04 allows taking of retirement benefits and continuing in service
- Staggering possible
- but **no PCLS separate from pension** (unless a protected PCLS)
- ☺ Popular – allows part-timer wind down
- ⊗ Staggering loses scheme-protected PCLS

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DB flexible retirement: Design: benefit timing

- all at the same time?
- in 2 stages if still in service, otherwise at same time?
- in multi stages if still in service, otherwise at same time?
- multistage even if not in service?

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DB flexible retirement Design: future accrual

If in service, accrual:

- continues in full?
- in which case, is accrual on new joiner scale?
- discontinues, but full risk cover?
- discontinues, as if leaver?

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DB flexible retirement General benefit/employment fit

- “50% retirement”
 - what pension/salary fit (esp if GMP/ Barber)
 - what risk benefit?
- In practice, “offer all-or-nothing”?
- If treated as “opt out and rejoin”, what if scales are different for new joiners
- Interaction with employment contract
- Selection against the scheme
- IHT?

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DB flexible retirement Impact on employer costs

- ☺ ↓ if “Offer: opt to take benefit early if also opt out of further accrual”
 - but age discrimination?
- ☹ ↑ Barber elements: increased numbers claiming unreduced pension early
- ☹ ↑ if effect on investment strategy is lower/earlier equity investment if more pensioners

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DB flexible retirement For executives to manage LTA

- ☺ Take reduced early pension to reduce BCE valuation, but carry on working
- ☹ But beware:
 - Executives may want guarantees up front to enable planning: use of in-service reserve reductions, ability to retire, what will be offered for subsequent accrual
 - Involves trustees as well as company
 - Wind up issues

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DB flexible retirement Administration a nightmare ☹?

- Traditionally,**
each member has a unique category, and
each category has its own record structure
- Multiple record per member, but linked?
 - Change system's "membership flow"
 - Change audit processes
 - Beware opportunities for error/fraud
 - Comms must acknowledge multiple statuses

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Death benefits Short-term dependant's pension

- Currently: must continue to death, remarriage or when child status stops
- ☺ Post A-day (FA05): No constraints forcing death pension to continue
(cf pension to a Child must stop at age 23)
- eg "DIS spouse pension four years only"
 - ☺ better focussed benefit
 - ☺ lower longevity risk
- Section 67 means for new members only??

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Death benefits: the law Lump sum versus pension

- Defined Benefit LSDB
 - unlimited
 - tax: 0% to outstanding member LTA, 55% on excess
 - only on death before age 75
- cf Dependants pension
 - unlimited if paid on death before age 75
 - tax: recipients' marginal IT rates

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Death benefits: DIS design "4x LSDB + 2/3 pension → 8x LSDB "

- ☺ Tax efficiency
- ☺ Flexible – can buy PLA if required
- ☺ Less mortality risk for scheme
- ☹ Trustee onus to choose recipients for large sum
- ☹ Insurance especially free cover limits
- ☹ Contracting out
- ☹ S67 issues maybe if for current members

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Restructure Scheme benefits in line with PPF benefits

- Aim: members' benefits match what they expect
- Convert pre 97 pension increases to extra accrued pension
- Use new Section 67? or obtain member consent
- ☺ If scheme enters PPF, members get higher benefits, closer to what they expect
- ☺ No expected benefit cost to the Company

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Restructure Scheme benefits in line with PPF benefits

- ⊗ If scheme never goes into PPF then little point
- ⊗ Higher PPF levy (on current formulae)
- ⊗ Would the PPF Board unwind this?
- ⊗ Risk of PPF Structure changing
- ⊗ Initial cost of communications, administration
- ⊗ Blocks in scheme rules/contracting-out

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