INSTITUTE OF ACTUARIES

PRESERVATION OF PENSION RIGHTS

A REPORT PREPARED BY
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I. INTRODUCTION

THE Council of the Institute decided that 'a Working Party be set up to advise the Council on the actuarial and other problems arising in connexion with the transferability of pension rights'. The Council of the Faculty accepted the Institute's invitation to be associated with the project and we were appointed to be the members of the Working Party.

2. In considering the subject remitted to us, we quickly formed the view that the description *preservation of pension rights* is more apt than *transferability of pension rights*, for the transfer of pension rights from one scheme to another when a member changes his employment is only one of several methods of preserving the whole or part of his accrued pension rights. We have accordingly used the term *preservation* in preference to *transferability* throughout this report.

3. We have confined our attention to the question of preservation of pension rights as it concerns individual members of pension schemes who change their employment, as distinct from the problem that arises when groups of members are transferred with the work they do from one employment to another, as they were, for example, on a large scale when the nationalized industries were set up; in such cases other problems arise.

Definitions

4. The following terms are used in this report in the senses respectively indicated:

(*a*) *Pension Scheme* or simply *Scheme*—in a comprehensive sense, to mean a recognized arrangement for provision of retirement benefits, but with no particular implication, unless the context plainly requires it, as to the financial basis (funded or unfunded, contributory or non-contributory) or constitution (statutory or non-statutory, privately administered or a life office scheme) of any individual scheme.

(*b*) *Transfer value*—a sum of money related to the value, at the time of a member's change of employment, of his interest in the pension scheme associated with his old employment (called 'the old scheme'), with due allowance for the share of the benefits normally provided by the employer.

(*c*) *Cold-storage benefits*—deferred, or paid-up, benefits in the old scheme, related to the period of pensionable service completed before the member's change of employment, with due allowance for the share of the benefits normally provided by the employer.

5. The *transfer value method* implies payment of a transfer value from the old scheme to the scheme associated with the member's new employment (called 'the new scheme'). The transfer value may be the whole, or some definite proportion—the proportion possibly increasing with length of pensionable service—of the value of the member's interest in the old scheme. In the new scheme, the transfer value may be used

(*a*) to buy what additional benefits it equitably will on an actuarial basis;
(*b*) as a contribution towards the cost of 'deemed' membership equal to the period of pensionable service ranking under the old scheme, or of an additional pension equal to the accrued pension in the old scheme or, indeed, of any other amount that may be agreed. Any cost of the rights conceded in the new scheme in excess of the transfer value received must, of course, be financed in whatever way is appropriate to the scheme concerned.

6. The *cold-storage method* implies retention after the member has left his old employment of rights to deferred, or paid-up, benefits in the old scheme. The amount of the benefits may be the whole, or some definite proportion—perhaps again increasing with length of pensionable service—of the normal benefits related to the completed period of pensionable service.

Views previously expressed on behalf of the Institute and the Faculty

7. In May 1954, the Councils of the Institute and the Faculty, acting jointly, submitted a Memorandum of Evidence* to the Committee under the Chairmanship of Sir Thomas Phillips, appointed by the Chancellor of the Exchequer to consider and report upon the economic and financial problems of the provision for old age. Reference to the question of preservation of pension rights of persons who change their employment was made in §§ 49–55 of the Memorandum of Evidence. These paragraphs are reproduced for convenience in Appendix A to this report but, summarized, the points made were:

(*a*) very commonly, a person who resigns from one employment to enter another, is compelled to withdraw from the old pension scheme and to start as a new entrant in the new scheme; he receives a relatively small withdrawal benefit and loses his accrued pension rights; the pension he receives on retirement falls short of the normal pension for his status and salary;
(*b*) there is no actuarial reason why pension rights should not be preserved on changes of employment, though at some increase, probably less than might at first sight be supposed, in employers' pension costs;
(*c*) apart from vocational or occupational pension schemes, the two available methods of preserving pension rights are the transfer value method and the cold-storage method;
(*d*) there is scope for a wider discussion of these matters, including some appraisement of the nation's best interest in regard to the question of the mobility of labour. If increased mobility of labour were thought to be beneficial to industry, employers might be more inclined to recognize the principle of preservation of pension rights, particularly if some basis of restricted or partial maintenance of accrued benefits were adopted—for example, that no rights should be acquired until after 5 years' service, there

* Reprinted *J.I.A.* **80**, 266 and *T.F.A.* **22**, 416.

after rights to be acquired on a scale increasing with length of pensionable service until full rights were available at the end of, say, 15 years' pensionable service;

(*e*) it would seem that there is scope both for cold-storage rights and for transfer values.

Phillips Committee's Report

8. In a section of their Report devoted to Mobility of Labour (Cmd. 9333, §§ 246–253), the Phillips Committee made frequent references to the question of preservation of pension rights. For convenience, this section of the Phillips Report is reproduced in Appendix B to this report. The Committee's two most important observations for present purposes appear to be:

(*a*) In our view, arrangements whereby the accrued pension rights of a person with substantial service may be preserved on a change of employment, including movement between the public services and private employment, are in the general national interest.... (§ 248).

(*b*) We have, with some reluctance, come to the conclusion that although the practice of granting transfer values and particularly of granting 'paid-up' pensions to employees leaving an employment is spreading, the general climate of opinion is not such that the principle of compulsion should be applied at this time.... We content ourselves, therefore, with recording our general approval of the growing practice of adopting methods to ensure the preservation of accrued pension rights. We hope that employers will give careful consideration to the desirability of making provision on these lines, whether by way of amendment of existing schemes or when new schemes are contemplated (§ 253).

9. Although the Phillips Report was published in December 1954, it has not yet (January 1957) been debated in Parliament. That the subject of preservation of pension rights is one of considerable public interest is, however, shown by the frequent references to it in the discussion of related matters in Parliament, in other forms of public discussion, in the editorial and correspondence columns of responsible newspapers and elsewhere. The Association of Superannuation and Pension Funds also has given consideration to the matter from time to time.

10. It is important to note that in § 248 of their Report, quoted in (*a*) of § 8 above, the Phillips Committee referred to preservation of 'the accrued pension rights of *a person with substantial service*'. The same idea found expression in the Memorandum of Evidence submitted by the Institute and the Faculty. In all the public discussion of the subject which we have observed, it appears to be assumed that the application of the principle of preservation should be restricted in some such way; so far as we are aware, it has never been suggested in any responsible quarter that pension rights should be automatically preserved for all persons leaving pensionable employment, however short their service. This point has to be appreciated if the matter is to be kept in perspective. We consider that however widely the principle of preservation of pension rights might be adopted, it would in practice apply only to a minority of persons changing their employment; in our view, it would be wrong to think that widespread acceptance of the principle would of itself lead to a dramatic increase in the numbers of persons changing their employment after substantial periods of service.

II. GENERAL SUMMARY OF EXISTING PRACTICE

11. It is understood that comprehensive arrangements for preservation of pension rights exist in many European countries, and in Canada and the United States of America. In some countries, preservation of rights if membership of a scheme has lasted more than a certain time is obligatory as a condition of approval for tax relief. We have not studied these arrangements in any detail; we have confined our attention to the position as it is, and the considerations which affect it, in the United Kingdom.

12. Existing practice in the United Kingdom can best be described separately in relation to

(*a*) certain vocational (or occupational) pension schemes;
(*b*) schemes for the public service;
(*c*) privately administered pension schemes;
(*d*) life office schemes.

Vocational pension schemes

13. There are a number of pension schemes which make provision for persons who follow a particular profession or occupation, though from time to time changing from the service of one employer to another. These schemes apply if the employers for their part accept the obligations which the various schemes impose on them. Examples are the Federated Superannuation Scheme for Universities (F.S.S.U.), the National Health Service Superannuation Scheme, the Teachers' Superannuation Scheme, the Merchant Navy Officers' Pension Scheme and a scheme for employees of the flour-milling industry. Methods of finance and constitution vary from one scheme to another, but it is a primary purpose of each of these schemes to enable the members to move in their particular profession or occupation from the service of one employer to another, while preserving continuity of pension rights. There are other such schemes, of more limited scope, in industry and commerce, where groups of associated companies have combined in the establishment and maintenance of a single pension scheme to which employees of all the companies in the group are admitted so that individual employees may move from one company to another within the group without disturbance of their pension rights.

14. Within such schemes, questions of transfer values and cold-storage interests do not arise, but if a member moves to the service of an employer who is not a party to the relevent scheme, special arrangements may have to be made.

Schemes for the public service

15. Arrangements for preservation of pension rights in cases of transfer between the Civil Service and other employment are described in Appendix XI to the Report of the Royal Commission on the Civil Service, 1953–55 (Cmd. 9613) and discussed by the Royal Commission in §§ 696–707 of their Report. §§ 16–25 of this report are based thereon.

16. Four principal types of arrangement are relevant for present purposes. They are:

The 'Public Office' Rules.
Approved employment.
Deferred pensions for persons leaving the Civil Service at ages over 50.
Transfer Rules, which apply also to persons in other pensionable employment outside the Civil Service.

In addition, the F.S.S.U. (to which reference has already been made) was formerly used for scientists employed in the Civil Service to enable them to return at intervals to university work if they wished, without sacrifice of pension rights. F.S.S.U. has, however, been abandoned for permanent civil servants recruited from 1 January 1953 onwards, because it was considered that post-war developments of policy in favour of interchangeability among the various forms of public and semi-public employment made appropriate and, indeed, better provision for the permanent scientists. F.S.S.U. is still used for scientists employed temporarily and for those of the permanent scientists who elected to remain in F.S.S.U. instead of transferring to the normal Civil Service superannuation arrangements when they were given an option.

17. *The 'Public Office' Rules.* The 'Public Office' Rules date from 1911 and were made under S. 7 (1) of the Superannuation Act, 1909. These Rules empower the award to persons who have served continuously in the Civil Service and in one or more public offices of either

(*a*) a single pension calculated on the officer's whole service and final pensionable salary, the cost of the pension being apportioned between the employers concerned. (This method is applied where the employers concerned operate superannuation schemes which are similar in form and provide comparable benefits to those which normally apply to civil servants, e.g. the Metropolitan Police (for civil staff), the Crown Agents for the Colonies and the Forestry Commission); or

(*b*) two or more separate pensions calculated on service under each employer and on the final pensionable salary of each employment. (This method is used where method (*a*) cannot reasonably be adopted, because the superannuation schemes involved are dissimilar. It applies to Civil Service combined with, for example, service in respect of which a pension is payable from the revenues of British Colonies and British Protectorates.)

Both methods are restricted to persons who serve continuously in the Civil Service and in 'public offices'.

18. *Approved employment.* Under S. 4 of the Superannuation Act, 1914, if a civil servant is transferred to employment other than employment in a public office, the Treasury can, in the circumstances described in § 19, 'approve' such employment. In that event, the pension or gratuity earned by his previous civil service becomes payable at age 60 or at the date of retirement from approved employment, whichever is the later, or on death before retirement.

19. The criterion for Treasury 'approval' is that the post is such that it is in the interests of the State for a civil servant rather than anybody else to be appointed to it. For many years, this arrangement was sparingly used, but

policy has developed over the years. More recently a wide view has been taken and employment will now be 'approved' if the Treasury is satisfied that it is not of a private or commercial character and that the officer's transfer thereto is in the widest sense in the public interest; the arrangements have, for example, been applied to civil servants transferring to Universities in the United Kingdom, N.A.T.O., the British Sugar Corporation, Singapore City Council and the Royal Canadian Navy.

20. The traffic is one-way and restricted. The arrangement applies only to persons leaving the Civil Service to enter employment which is approved and not to persons entering the Civil Service from other employment.

21. *Deferred pensions for persons leaving the Civil Service at ages over* 50. The Superannuation Act, 1949, provides for persons who leave the Civil Service at ages over 50 to receive deferred pensions commencing at the age of 60, related to their completed period of Civil Service and the rate of pay last received. This right is virtually absolute; it is not linked in any way to the nature of any employment the former civil servant may take up after leaving the Civil Service. The traffic is again one-way; the arrangement applies only to outgoing civil servants.

22. *Transfer Rules.* S. 2 of the Superannuation (Miscellaneous Provisions) Act, 1948, marked a major development covering not only persons who leave the Civil Service, but also persons who enter the Civil Service and others who enter or leave certain other forms of public employment. This section empowers the appropriate Minister or Ministers to 'make rules... with respect to the pensions payable to and in respect of' certain classes of people, namely,

(*a*) those who leave the Civil Service, the Metropolitan Police, local government service, and teaching, and enter other pensionable employment;

(*b*) those who leave other pensionable employment to enter one of the classes of employment mentioned in (*a*);

(*c*) those who transfer from one of the classes of employment mentioned in (*a*) to another.

The 'rules' are settled by agreement between the authorities concerned and embodied in Statutory Instruments made by the appropriate Minister or Ministers. The 'other pensionable employment' referred to in (*a*) and (*b*) is not restricted by the Act to public employment, but in practice the arrangements that have so far been made are restricted to various forms of public employment, using the term in its widest sense to include such authorities as, for example, the Port of London Authority, the National Dock Labour Board, and some, but not all, of the nationalized industries.

23. These comprehensive powers have been used in a variety of ways and extensive reciprocal arrangements for preservation of pension rights have been made between various public authorities. Their scope is constantly being extended to include other authorities. Generally, the rules provide for the authorities concerned to exercise discretion in deciding whether to apply the benefit of the special arrangements to individual cases; for example, a civil servant transferring to any of the employments mentioned can benefit only if his transfer has the consent of the head of his Department, though the policy is that such consent should not be withheld without good reason.

24. Some of the Statutory Instruments provide for the payment of transfer values between schemes, and some for setting up cold-storage rights. In either case, the arrangements for preservation of pension rights can be, and frequently are, coupled with a provision that the period of pensionable service in the old employment will rank for the purpose of determining qualification for benefit in the new employment. Certain of the rules covering outgoing civil servants go so far as to require the Treasury to pay transfer values to other authorities in respect of the accrued (but unfunded) pension rights of the outgoing civil servants.

Views of the Royal Commission on the Civil Service

25. In §§ 696–707 of their Report the Royal Commission on the Civil Service discussed the arguments for and against extension of the existing arrangements within the public service, to transfers to and from private employment. They concluded that 'the balance of present advantage lies with making no change in the existing arrangements' and so recommended.

Local Government Service

26. In the local government service, each local authority of any appreciable size maintains its own fund; the smaller authorities combine with larger authorities for this purpose. Transfers of employment (of which there are many) of local government officers and servants from one local authority to another entail transfer of membership between the appropriate superannuation funds. There is statutory provision for the payment of transfer values between the funds, the transfer values being calculated on a prescribed basis in relation to the employee's period of pensionable service and salary with the authority whose service he leaves.

27. Transfers from local government service to other pensionable employment, or in the reverse direction, can be and, where it seems to the authorities concerned to be appropriate, are dealt with under the powers contained in S. 2 of the Superannuation (Miscellaneous Provisions) Act, 1948.

Public Boards, Nationalized Industry, etc.

28. Transfers between the service of public boards, nationalized industry and various other forms of public and quasi-public employment, and the forms of employment specified in S. 2 of the Superannuation (Miscellaneous Provisions) Act, 1948, can also be dealt with under the Act. But transfers to and from other forms of employment and, in particular, employment in commercial undertakings, would have to be dealt with, if at all, with due regard to the provisions of the rules of the relevant superannuation schemes.

General observations

29. Such, then, are the principal types of arrangement for preservation of pension rights in the public service and in quasi-public service. It is evident that the principle of preservation has long been recognized. With the passage of time, the area of its application within the public service has constantly been extended, in recent years on a rapidly increasing scale. S. 2 of the Superannuation (Miscellaneous Provisions) Act, 1948, gives scope for further substantial enlargement.

Privately administered schemes

30. The methods adopted for preservation of pension rights in the public service are not necessarily appropriate for privately administered schemes, since the terms of individual schemes differ widely from one another and each scheme is financially self-contained.

31. No precise or up-to-date information exists as to the number of privately administered schemes which make provision for preservation of pension rights, or as to the extent to which such powers are exercised where they exist. In a questionnaire issued to its members by the Association of Superannuation and Pension Funds in December 1950, one of the questions asked was 'Has your fund power to transfer monies to other pension or superannuation Funds approved by the Inland Revenue?' The statistics compiled from the completed questionnaires are difficult to interpret, but so far as we can estimate, it would appear from the replies that at that time only about 70 privately administered funds, or about 15% of the privately administered funds replying to the question, had power to pay transfer values. No information is available as to the current position; our impression is that it has become more common to include such powers in the Trust Deed and Rules, but that the powers are only sparingly used.

32. Although we do not know of any information having been assembled on the subject, we also believe it is extremely rare for trustees to have power to grant cold-storage rights to members transferring to other employment, except in cases where special relations exist between the old and new employers. Where such power exists, the grant of cold-storage rights may be conditional on the member having completed a stated period of pensionable service in the old employment.

33. In respect of incoming members, the rules of some schemes empower the acceptance of any sum paid in respect of termination of membership of another scheme, whether it be a transfer value in the formal sense or simply a normal withdrawal benefit. Additional benefits and, possibly, a period of credited membership may be granted in consideration of the payment received.

Life office schemes

34. As in the case of privately administered schemes, the methods adopted for preservation of pension rights in the public service are not necessarily appropriate to life office schemes.

35. The usual provision in life office schemes is for a member withdrawing voluntarily to be given an option to take a surrender value in cash in respect of his own past contributions, or the corresponding cold-storage benefits in the form of a paid-up policy. If the member elects for the cold-storage benefits, the employer may, if he thinks fit, agree to grant additional cold-storage benefits in respect of the employer's contributions, but this is probably seldom done in practice. If, as occasionally happens, an employer wishes to give this additional pension as a right, the Inland Revenue will agree, as a concession, that appropriate provision may be made in the rules of the scheme.

36. For members who are dismissed from the employer's service for reasons other than fraud or misconduct, the Inland Revenue authorities

require that in a scheme where there are no trustees an employee who takes cold-storage benefits for his own contributions must be given the right to claim the additional cold-storage benefits arising from the employer's contributions, so that in these cases the matter does not rest on the employer's discretion.

37. It should be added for completeness that in the case of pension schemes approved under S. 388 of the Income Tax Act, 1952, the rules may provide for a withdrawing employee to have the option to continue to pay premiums to secure a pension up to the full amount he would have received under the scheme if he had remained a member up to retirement without further change in salary. In such circumstances, the employee would be entitled to life assurance relief in respect of the premiums subsequently paid by him after withdrawal from the scheme.

38. In practice, employees withdrawing from pensionable employment covered by life office schemes almost always take a surrender value in cash so that, in fact, the cold-storage arrangements do not operate to any substantial extent.

39. Provision is not normally made in life office schemes for payment of transfer values from one scheme to another.

III. THE POSSIBLE ENLARGEMENT OF EXISTING ARRANGEMENTS

40. From Section II of this report, it is apparent that arrangements of wide scope for preservation of pension rights exist within the public and quasi-public services, and that power exists in S. 2 of the Superannuation (Miscellaneous Provisions) Act, 1948, to widen them still further, *inter alia*, to include transfers to and from private employment. In private employment, however, it is exceptional for arrangements to be made to preserve pension rights on a voluntary change of employment.

41. From time to time, statements have been made on behalf of the Government favouring the extension of such arrangements. Any substantial development in the field of private employment would depend on

(*a*) acceptance by employers of the principle that employees changing employment voluntarily have a right to the share of accrued pension rights provided, or promised to be provided, at the employer's cost; in practice, the application of the principle might be restricted to employees who have completed a minimum period of pensionable service and, in individual cases, to the employer's consent to the grant of some or all of that part of the accrued rights;

(*b*) willingness of employees changing employment to forgo payment of withdrawal benefits in cash and to be accorded instead either cold-storage rights in the old scheme or payment of a transfer value direct from the old scheme to the new;

(*c*) if the transfer value method is to be used at all freely, removal or at least substantial reduction of certain taxation obstacles which, as will appear from Section VII of this report, at present exist.

42. In private employment, pension provision is made by privately administered schemes and life office schemes. It would be possible to provide

for a substantial measure of preservation by widespread adoption of one or other of the cold-storage or transfer value methods, but to enable really comprehensive preservation arrangements to be made, it would be necessary

(*a*) to make provision in the rules of privately administered schemes for both methods to be applied;

(*b*) to secure more general use of the existing cold-storage provision of life office schemes, and to develop arrangements for the application of the transfer value principle to them.

43. No system for preserving pension rights would be complete unless it also made provision for persons transferring from public employment to private employment and *vice versa*. It has already been mentioned that statutory power exists for such arrangements to be made, that the power has not so far been exercised and that the Royal Commission on the Civil Service has recommended that no change be made in existing arrangements at the present time. It is possible that if preservation arrangements were more widely adopted in relation to private employment, a change of attitude and, with it, changes of practice would be induced in course of time.

44. A few employers have been prepared to concede unilaterally the principle of preservation of pension rights in the pension schemes associated with their undertakings. Rapid and widespread acceptance of this principle is hardly to be expected of employers generally. It is, perhaps, more likely that preservation arrangements will spread by the development of reciprocal arrangements between employers and within groups of employers having a community of interest such as exists, for example, between different firms in the same profession.

45. Experience shows also that when a withdrawing member of a pension scheme can choose, a withdrawal benefit in cash is usually preferred to a cold-storage benefit, even if the latter includes the part of the accrued pension secured by the employer's contributions. It is possible, therefore, that if the principle of preservation were widely accepted by employers, it could be defeated by the employees themselves if they continued to have an option to receive a withdrawal benefit in cash in respect of the interest created by their own contributions. It might be desirable for the introduction of preservation arrangements to be coupled with some restriction of a transferring employee's right to receive immediate payment of a withdrawal benefit in cash.

IV. THE INCIDENCE OF THE COST OF PRESERVATION OF PENSION RIGHTS

46. It is obvious that the adoption of a policy of preservation of pension rights must lead to the payment to some people of larger pensions in retirement than they would otherwise have enjoyed and therefore that some additional cost must be involved.

47. The true additional cost would, however, be less than the total of all the additional pensions specifically derived from preservation arrangements because

(*a*) some of the recipients would never have changed their employment if appropriate preservation arrangements had not existed; they would have continued in their original employments and drawn pensions in respect of

their early periods of service in them, just as, having changed their employment, they would continue to do by virtue of the preservation arrangements;

(*b*) some of the recipients would otherwise have been accorded special pension rights by their new employers, in excess of those which would normally accrue from the period of service in the new employment. The existence of preservation arrangements would reduce the need for special arrangements of this kind.

48. The additional cost arising from particular cases of preserved pension rights presents itself in different ways, according to the type of scheme on which the liability falls and the method by which the scheme is financed.

49. In a public service scheme, the cost of the transfer value or the cold-storage benefits, as the case may be, forms a specific charge on the relevant compartment of the public purse. If the scheme is unfunded, the cost is borne as and when the relevant payments are made. If the scheme is funded, the cost is borne indirectly through the funding charge, possibly spread over a period of years.

50. In a privately administered scheme valued on an actuarial basis which incorporates withdrawal, mortality and retirement as decremental rates, the cost presents itself in the first place either as a reduction in the withdrawal profits, or as an increase in the losses that would have arisen if there had been no preservation arrangements. Normally, the withdrawal rates used in the actuarial basis would be such as to exclude provision for cases of transfer with preserved pension rights. If, however, there were likely to be enough cases of transfer with preserved pension rights to justify such a course, 'transfer' could be specifically recognized in the actuarial basis as a form of decrement and provision made for the special liabilities arising on transfer. In such circumstances, the cost of providing for preservation of pension rights on transfer could be measured and identified in terms of contribution rates and valuation reserves. The disturbing effect on the finances of the fund would then be limited to the difference between actual experience of transfers with preserved rights and that 'expected' on the valuation basis.

51. The responsibility for meeting the cost of preserved pension rights would depend on the financial basis and constitution of the particular scheme on which the liability falls. In a non-contributory scheme, or if the employees' contributions were limited in amount, with or without a formal guarantee of solvency from the employer, the cost would fall on the employer as part of the general cost to him of the scheme. If the cost of the scheme were, in fact, apportioned between employer and employees in specified proportions, the cost to the scheme of preserving pension rights would sooner or later be correspondingly shared.

52. In a life office scheme, the employer is usually credited, by way of set-off to his other liabilities under the scheme, with the surrender values of the benefits created by his own contributions in respect of withdrawing employees who are not entitled to them. Preservation of pension rights on any larger scale than is customary would reduce the amount of the employer's credits and so add indirectly to his costs.

53. Thus, in all but the probably exceptional cases of privately administered schemes where the cost is apportioned between employer and employees in

specified proportions (when the employer would bear his agreed proportion), the cost of any enlargement of arrangements for preservation of pension rights would sooner or later fall wholly on the employer. The amounts involved would depend, first, on the scope of the preservation rights and, second, on the extent to which advantage was taken of them. It has already been mentioned that responsible opinion appears to favour application of the principle of preservation only to persons who leave pensionable employment after substantial periods of service. In that event, as was suggested in the joint Memorandum of the Institute and the Faculty to the Phillips Committee, the addition to employers' costs would be less than might at first sight be supposed.

V. METHODS OF ASSESSMENT OF TRANSFER VALUES AND COLD-STORAGE BENEFITS

54. As was stated in the evidence given by the Institute and the Faculty to the Phillips Committee, there is no actuarial reason why pension rights should not be preserved on changes of employment. In assessing the amounts of transfer values and cold-storage benefits in individual cases, however, the actuary has to solve some intricate technical problems. These problems vary from one scheme to another and many are specific to individual schemes. A few general observations may, nevertheless, be of value.

Privately administered schemes

55. The questions that arise can most usefully be discussed first in relation to a hypothetical privately administered scheme, assumed to be conducted on actuarial principles and with actuarial advice, in which it may be supposed that the benefits of individual members are related in some fashion to their salaries and that the scheme is financed, at least in part, by contributions specifically related to the members' current salaries.

56. Determination of the principles and methods and of the actuarial basis to be adopted in any particular scheme is primarily the responsibility of the actuary to the scheme. Certain aspects of these problems may involve considerations of policy which must be settled by the managers or trustees of the scheme concerned but if so, it is the actuary's duty to ensure that they understand the implications of their decisions.

57. The basis, or bases, of assessment used in relation to any particular scheme must be such that

(*a*) there is consistency between individual cases;

(*b*) in each individual case, there is a reasonable relationship between the transfer value and the cold-storage benefits; it is desirable for this principle to be kept in mind even if the rules of the particular scheme do not at the moment provide for both methods to be used.

58. As regards (*b*), it is immaterial in principle whether the transfer value be calculated first and the cold-storage benefits derived by calculation from he transfer value, or *vice versa*. The natural link between the two is the appropriate factor, derived from the actuarial basis of calculation, for converting an amount of money payable currently into its reversionary equivalent, with due allowance for the relevant contingencies and the appropriate rate of interest.

59. The transfer value has been defined in § 4 as, in effect, a sum of money equal to the whole or some definite proportion of the value of the member's 'interest' in the scheme at the time of his withdrawal from membership. The practical problem of calculating the value of the member's 'interest' can be approached in either of two ways. One is to calculate the transfer value directly, by reference to the somewhat theoretical conception of the reserve value attaching to the member concerned, a microcosm, as it were, of the fund as a whole but with due regard to the individual member's age, salary history, length of pensionable service, and so on, and then to derive the amount of the member's cold-storage interest (if it is required) from the transfer value so calculated. The alternative approach is to define the amount of the member's cold-storage interest first (whether or not he is to be accorded cold-storage rights) and to derive the transfer value from it. Each of these two alternative approaches will now be discussed in turn.

60. There are in principle two methods by which the amount of the theoretical reserve value can be calculated

(*a*) retrospectively, by accumulation of contributions at interest and with benefit of survivorship;
(*b*) prospectively, by calculation of the difference between the present value of prospective benefits and the present value of future contributions.

61. In a pension scheme, the reserve values calculated by the two methods in respect of an individual member will be equal to one another if, but only if, three conditions are satisfied:

(i) that the contributions brought into the calculations in respect of the member concerned are exactly equivalent over the whole period of pensionable service to the estimated value of the liabilities accruing from his service;
(ii) that the retrospective and the prospective calculations are both made on the actuarial basis which was used for calculation of the contributions;
(iii) that the individual member's salary progression to date has followed exactly the assumed rate of progression incorporated in the actuarial basis.

62. In practice, it is extremely unlikely that all, or perhaps any, of these conditions will be satisfied.

As to the first, contributions to a pension scheme in respect of an individual member are frequently not equal to those theoretically required for that individual because, for example, the employer's contribution is calculated globally as a uniform percentage of salary for all members. If the calculation of the member's 'interest' is based on actual contribution rates, the results may, therefore, be distorted. They can, in certain circumstances, be manifestly absurd, ranging from amounts which are obviously in excess of any reasonable figure in some cases, to negative values in others.

As to the second, the actuary may or may not consider it appropriate to use the contribution basis for the purpose of calculating individual members' 'interests'; generally speaking, and apart from any other consideration, the longer the period that has elapsed since the contributions were calculated, the less appropriate is the contribution basis likely to be.

As to the third, the individual member whose salary progression conforms exactly to the assumed rate of progression incorporated in the actuarial basis seldom, if ever, exists; as an individual he is no more real than the man-in-the-

street. There may be wide deviations in individual cases, particularly if there have been general salary increases during the period of pensionable service.

63. The retrospective and the prospective methods of calculation of the value of an individual member's 'interest' are, therefore, likely to lead to different results.

64. In particular, the prospective method may give a value which has no direct relation to the individual member's accrued rights. Moreover, it raises the whole question whether it is appropriate to apply a technique which is valid for valuation of a scheme as a whole to an individual member whose past career or future prospects, or both, may differ widely from the generalized averages implied in whatever basis of calculation is used.

65. As to the second possible approach of defining the amount of the member's cold-storage interest first, and deriving the transfer value from it, it is usually relatively easy to arrive at an acceptable definition of an individual member's 'interest' in terms of accrued pension rights at a particular point in time. As a simple example, if a scheme's normal pension scale is 1/60th of average salary throughout membership for each year's membership, the accrued pension of a member who has completed t years' membership and whose average salary to date is £x per annum can reasonably be defined as

$$\frac{t}{60} \text{ of } £x \text{ per annum.}$$

If the normal pension scale were 1/60th of final salary for each year's membership, and the member's current salary were £y per annum, the accrued pension could be regarded as t/60 either of £y per annum or of £y per annum 'grossed up' in some manner to take account of prospective salary increases before retirement age; the choice between the two would be a matter of policy to be determined by the trustees or managers of the scheme. The application of the method would vary in detail from scheme to scheme, according to the normal scale of benefits, but there is no doubt that it is a powerful method, capable of use in many different circumstances.

66. The member's cold-storage interest would be either the whole or some definite proportion of the accrued pension rights. The corresponding transfer value could then be taken to be the discounted value of the cold-storage interest with due allowance for the relevant contingencies and the appropriate rate of interest. The aggregate of transfer values calculated by this method for all members of the scheme (if such a conception had any meaning) would be analogous to the past service liability in the valuation balance sheet rather than to the net liability. Valuation profits or losses would, therefore, arise from the adoption of this method but if, as appears likely, the preservation principle were applied only to relatively small numbers of members, the net financial effect would be relatively unimportant. The advantages of this approach are that the amount of the member's 'interest' would be related to his accrued pension rights, assessed on a basis which—at the least—has a commonsense appeal, there would be consistency between one member and another and in individual cases, the transfer value would be in reasonable relationship to the corresponding cold-storage benefits.

67. Whatever method of assessment he decided to adopt in relation to a particular scheme, the actuary would have to determine an appropriate basis

of calculation. Whether he should use the last valuation basis, or some modification thereof, or an experience basis, or some appropriate *ad hoc* basis is a matter for him to decide with due regard to all relevant circumstances. Further points which will arise, involving questions of policy for consideration by the trustees and managers of the scheme, are

(*a*) whether transfer values should be adjusted by reference to the general financial position of the scheme and, in particular, whether they should be increased or reduced if the scheme is in surplus or deficiency;

(*b*) whether the amounts of cold-storage interests should be similarly adjusted by reference to the general financial position of the scheme at the time they are created and, further, whether they should be subject to adjustment in the future if there are general adjustments to the benefits provided by the scheme because of variations in its financial position.

68. In schemes where the employer meets his share of the cost otherwise than solely by contributions related to the current salaries of individual members, the question arises whether the amounts of transfer values and of cold-storage benefits should be adjusted by reference to the degree of funding achieved at the time when the member withdraws from the fund and if so, whether the adjustment should vary with the rate of funding adopted for the future. Arguments can be adduced in support of either view; to some extent, the question is one which involves considerations of policy.

69. It is clear that there is no royal road of simplicity to the assessment of transfer values and cold-storage benefits in privately administered schemes. Whatever methods are adopted, valuation profits and losses are likely to arise, but in relation to the liabilities of the scheme as a whole, they should be relatively unimportant.

Schemes for the public service

70. It will be appreciated from the description of schemes for the public service in §§ 15–29 of this report, that where the preservation arrangements are based on the cold-storage principle, they rely substantially on equitable definition of the officer's interest very much in the manner described in § 65 with due regard to the terms of the scheme, the length of his pensionable service and the amount of his salary over a relevant period of service.

71. Where the arrangements are based on the transfer value principle, the basis prescribed for calculation of transfer values passing between local government superannuation funds has, in fact, also been adopted for transfers between the Civil Service, local government, teaching, the police, the fire services and the National Health Service, except for transfers from the National Health Service, for which special tables are used.

72. Although the benefit scales in the various schemes are basically similar, the schemes differ widely in other important respects, for example, in regard to the normal retiring age, which is much lower in some occupations, such as the police service, than it is in others. In individual cases, there must sometimes be large differences between the value of a transferring member's 'interest' and a transfer value assessed on the local government basis. The transfer value system, as it is applied in the public service, must therefore cause quite substantial stresses and strains between different compartments of the public purse.

Life office schemes

73. In a life office scheme, as in other types of scheme, there is usually no difficulty in arriving at an acceptable definition of the amount of an individual member's accrued pension rights at a particular time, including the amount (if any) provided or promised to be provided at the employer's cost in respect of service completed to date.

74. It has been stated already (§ 39) that provision is not normally made in life office schemes for the payment of transfer values from one scheme to another, other than the normal surrender values. If the transfer value method were to be adopted, it would be necessary to consider whether some special method and basis of calculation should be used, different from those normally adopted for surrender values. The need for consistency between individual cases and for a reasonable relationship between transfer values and the amounts of the corresponding cold-storage interests would be as real as in a privately administered scheme.

VI. ASSESSMENT OF BENEFITS GRANTED IN EXCHANGE FOR TRANSFER VALUES

Schemes for the public service

75. Where transfer values are accepted in the various public service pension schemes, there is usually no actuarial calculation of an equivalent amount of pension or period of pensionable service to be conceded in exchange for the transfer value. Generally the principle adopted is to allow the period of pensionable service in the old employment to rank as service in the new employment for the purposes of the new scheme. The amount of the transfer value may be more or less than the value of the additional rights granted in consideration of the payment of the transfer value. The profit or loss, as the case may be, falls sooner or later on the appropriate compartment of the public purse, though the methods of finance adopted may be such that it is never separately identified.

Privately administered schemes

76. It is a matter of policy for the trustees or managers of the new scheme to decide whether or not the additional rights to be conceded to individual members are to be equal in value to, or greater in value than, the transfer values received. They may decide to grant an incoming member additional benefits in the new scheme equal to the accrued benefits in the old scheme, or to credit him with the period of pensionable service in the old scheme as if it had been pensionable service in the new scheme or, indeed, to accord any other additional benefit that may be agreed, provided it is not worth less than the transfer value actually received. Changes of employment are, of course, frequently accompanied by substantial increases in salary. Even if all other conditions governing the transferring employee's pension rights remained unaltered, the salary increases would usually create a problem, either of apparent inequality between the rights conceded in the new scheme and those given up in the old scheme, or of cost to the new employer if he sought to recognize previous pensionable service in full by reference to the increased salary.

77. If it is decided to grant additional benefits equal in value to the transfer value received, the actuary will be required to advise on the amount and form of the credit to be granted. This is a matter to be determined in the light of all the relevant circumstances of the new scheme. The additional benefits may, however, usually be expressed in one or other of two general forms, either

(*a*) fixed monetary additions to the benefits accruing in the new scheme on the normal scale in respect of future pensionable service, with a credit for a broadly corresponding period of notional service in order to advance the date when the member first becomes entitled to benefits for which a qualifying period of service is imposed; or

(*b*) an appropriate number of 'added years' of pensionable service ranking for benefit on the normal scale in addition to actual future service, and counting towards completion of qualifying periods of service governing entitlement to benefit.

Method (*a*) restricts the value of the additional benefits as nearly as possible to the amount of the transfer value received. In a scheme where benefits are related to the members' salaries, method (*b*) entails some financial risk, for if the member's salary increases by more than is implied by the salary scale incorporated in the actuarial basis, the additional benefits accruing from the added years will be correspondingly more expensive. The converse is also true, but if recent experience is any guide to the future, losses are more likely than profits from the use of method (*b*). The choice between the two methods is again a matter of policy, for decision by the trustees or managers of the scheme, with due regard to actuarial advice as to the implications of the two methods.

78. Whichever method is used, the additional benefits would be payable in the circumstances prescribed by the rules of the new scheme, which would be related to the conditions of the new employment. These might be quite different from the conditions of the old employment, for example, in regard to retirement age. Because of differences in the conditions of membership of the two schemes, the amounts of the additional benefits granted in the new scheme might be very different from the member's accrued benefits in the old scheme, while remaining their equivalent in value.

Life office schemes

79. If transfer values were to be paid from one scheme to another, no difficulty need arise in assessing the amount and nature of the additional benefits to be granted in the new scheme. The transfer value would, no doubt, be treated as a single premium and used to buy such additional benefit for the member concerned as it would on the basis of a single premium rate appropriate to this class of business. As in the case of the privately administered schemes, the additional benefits would be payable in the circumstances prescribed by the rules of the new scheme and might be very different in amount from the member's accrued benefits in the old scheme.

VII. INCOME TAX POSITION

80. As in so many other aspects of superannuation, income tax considerations arise and exert their influence on practice. The nature of the problems depends on the status of the scheme or schemes concerned in relation to the Income Tax Act, 1952.

81. No special tax problems arise in relation to the creation of cold-storage rights or the payment of transfer values in respect of those of the public service schemes which are unfunded.

82. The funded public service schemes, privately administered schemes and life office schemes, fall into three main groups for tax purposes, as follows:

(*a*) *S.* 379 *schemes.* Schemes approved under S. 379 of the Income Tax Act, 1952, which corresponds to S. 32 of the Finance Act, 1921; they include most privately administered schemes, some of the funded public service schemes and some life office schemes.

(*b*) *S.* 378 *schemes.* Schemes falling within S. 378 of the Income Tax Act, 1952, which corresponds to S. 31 of the Finance Act, 1922. This Section covers schemes established under public general Acts of Parliament, which satisfy certain conditions but are not capable of approval under S. 379.

(*c*) *S.* 387 *schemes.* Other schemes exempted under S. 387, including those approved under S. 388 and related Sections of the Income Tax Act, 1952; these Sections correspond to S. 19–23 of the Finance Act, 1947.

Cold-storage benefits

83. There appears to be no taxation obstacle to the creation of cold-storage interests in any type of scheme in respect of a withdrawing member who is entering other employment.

84. Complications can, however, arise under the cold-storage system when pensions become payable. The present position is that most public service pensions and pensions payable from S. 378 and S. 379 schemes are taxed under the P.A.Y.E. procedure, whereas pensions payable from S. 387 schemes are subject to the DX–DR procedure. In either case, the paying authority's position and responsibility are quite clear. But for a pensioner who has benefited from cold-storage arrangements and who receives pensions from different sources taxable under the two different procedures, the position may be somewhat troublesome.

Transfer values

85. The Inland Revenue authorities do not normally approve rules in S. 379 schemes which provide for payment of more than the normal withdrawal benefit except by way of transfer value. Where transfer values are paid from one S. 379 scheme to another, the authorities waive their right to payment of tax at the time the transfer value is paid, but the trustees or managers of the scheme accepting the transfer value are required to account for tax on the whole of any retirement or withdrawal benefits subsequently paid in respect of the member concerned. If the rules of the schemes permit transfer values to be paid from a S. 379 scheme to a S. 378 scheme or a S. 387 scheme (as defined in § 82), it is probable that a tax liability would fall on the trustees of the S. 379 scheme at the time of payment.

86. Transfer values can be paid from S. 378 schemes where statutory power exists and in such cases it is understood that no tax liability arises.

87. It appears that the Inland Revenue authorities have no power to require tax deductions to be made from transfer values, surrender values or withdrawal benefits paid from S. 387 schemes (as defined in § 82). No tax question

would arise on the making of such a payment to a S. 379 or a S. 378 scheme. If the payment were made to the former employer as trustee and he in turn paid it to a S. 379 scheme, it is understood that tax would not be levied on the employer. But in the case of transfers of membership between schemes approved under S. 388, while the Inland Revenue would not object to a policy being transferred from one scheme to another, there might be tax difficulties if a surrender value were paid to the first employer and passed on by him to the second employer or to the scheme associated with the second employment. These difficulties might be avoided if the first employer authorized payment of the surrender value to be made direct to the trustees or managers of the scheme associated with the second employment.

88. Thus, it is clear that while transfer values can pass in some circumstances without complication arising from tax considerations, there are other circumstances in which difficulties arise or where the position is not clear. Before there could be any comprehensive, or even widespread, adoption of the transfer value system as a means of preserving pension rights on changes of employment, the position would have to be clarified and the existing obstacles removed or substantially reduced. This would probably require legislation.

VIII. COMPARISON OF THE COLD-STORAGE AND TRANSFER VALUE METHODS

Scope

89. The cold-storage method is capable of application to all types of scheme. The transfer value method can be applied to public service schemes and privately administered schemes, but in life office schemes there is at present no provision for transfer values to be paid from one scheme to another, other than normal surrender values.

90. The cold-storage method can be applied equally well whether or not the new employment is pensionable. The transfer value method is applicable only if the new employment is pensionable.

Income tax position

91. There appear to be no taxation obstacles, so far as the schemes are concerned, to the creation of cold-storage interests, but it may be troublesome for a pensioner to receive from more than one source cold-storage pensions which are differently taxed. Transfer values can pass freely without undue tax complications between S. 379 schemes, and in certain other cases. There are, however, cases in which difficulties arise or where the position is not clear. The position would have to be clarified and legislation might be required to remove existing obstacles before widespread transfer arrangements could be made.

Certainty of provision for transferring employee

92. The cold-storage method ensures that the transferring employee (or his estate) will benefit from the provision made. There is, however, no certainty at the time a transfer value is paid that the transferring employee will, in fact, benefit from the payment. If, for example, he were to change his employment a second time in circumstances where there were no arrangements for preservation of pension rights, the transfer value paid on the first change of employment,

or a substantial part of it, might well fall into the fund associated with the second employment. This possibility is likely to weigh with employers considering a choice of method.

Conditions on which benefits are payable

93. Cold-storage benefits granted in respect of a member's original employment will be payable in circumstances related to the conditions of that employment, which may be quite different from the circumstances of the new employment.

If, however, a transfer value were paid, the whole of the member's retirement benefits would be payable in circumstances related to the conditions of the new employment.

94. If, with cold-storage benefits, the pension ages under the two schemes are different, the trustees or managers of the first scheme may be willing to pay an actuarially equivalent pension from the pension age appropriate to the new employment. They are, however, unlikely to be willing to pay the full amount of the cold-storage pension unconditionally from the date of retirement in the event of the member's premature retirement because of ill-health; they may restrict their payment in that event to an actuarially equivalent pension, the amount of which has regard only to the member's age at retirement.

The pensioner's position

95. If a transfer value were paid, in due course the pensioner would draw the whole of his pension from a single source. Under the cold-storage system, he draws more than one pension, each from a separate source. Some of the pension payments may be taxed under the P.A.Y.E. procedure and some under the DX–DR procedure; this may be troublesome for the pensioner.

Administrative considerations

96. No special administrative problems arise in connexion with the transfer value system. Under the cold-storage system, the trustees or managers of the original scheme remain responsible to persons who have left the employment with which the scheme is associated, possibly many years before. Records must be kept and reserves maintained and eventually the beneficiary must claim his pension (or his legal personal representatives the death benefit) and prove identity. The life offices have for long faced similar problems in connexion with paid-up policies, without undue difficulty. There would, no doubt, be instances of unclaimed benefits from time to time over the years, and it would be important to adopt administrative methods designed to minimize the possibility of unclaimed benefits. The problem should be manageable so long as preservation of pension rights applies only to employees with substantial service.

Impact on investment policy

97. Cold-storage benefits payable from a funded scheme (including a life office scheme) could be expected to emerge for payment at a time broadly in consonance with the assumptions on which the scheme's investment policy had

been based, but payment of transfer values might enhance cash requirements at times when prices of securities were depressed. In such circumstances it would be necessary to consider whether the transfer values should be reduced on that account.

The volume of transactions of either kind is, however, unlikely to be sufficient to have any material influence on investment policy.

Actuarial considerations

98. From the actuarial point of view, there is no reason why pension rights should not be preserved on changes of employment, whether by the transfer value method or by the creation of cold-storage interests, although some intricate technical problems may arise. The bases of assessment of transfer values and cold-storage benefits in a particular scheme should be such as to ensure consistency between individual cases and a reasonable relationship between the amount of the transfer value and the cold-storage benefits in individual cases. Whatever method of calculation is adopted, profits and losses are likely to arise in the working of a scheme but if the cold-storage benefits and the transfer values are in proper relationship with one another, there is little or nothing to choose between the two methods on that account; if the number of cases arising is relatively small, the profits and losses should be financially unimportant in relation to the scheme as a whole.

99. No difficulty need arise in defining the amount of the credit to be granted in respect of a transfer value received in respect of an incoming member of a scheme.

A possible combination of the cold-storage and transfer value methods

100. If cold-storage interests were created in schemes which a member had left in the course of his career and held in reversion until his retirement, and transfer values were then paid into the scheme related to his last employment, the member could look to one scheme for payment of the whole of his retirement benefits. Such an arrangement could embarrass the last employer if the employee's total pension from all sources proved to be substantially different from the pension normally provided by the last employer for a retiring employee with a comparable service history spent wholly in his service. In other respects, most of the advantages and few of the disadvantages of both systems would be secured, except that the income tax problems associated with payments of transfer values, to which reference has already been made, would arise.

Influence of the financial condition of the schemes concerned

101. In all the comparisons that have so far been drawn, it has been implicitly assumed that both the old scheme and the new would be in an equally sound financial position at the time of the member's change of employment. If that were not so and the member had any say in the matter, he would presumably wish his accrued rights to be preserved in the scheme enjoying the better financial position at the time and his choice between the cold-storage method and the transfer value method would be governed accordingly.

An opinion

102. Mr V. R. Jackson, Pension Officer of Unilever Ltd, has recorded his opinion in a note in the April 1955 number of *Superannuation*, a paper published from time to time by the Association of Superannuation and Pension Funds:

> We instituted in Unilever after the war a vested right for all staff, Works as well as Office, who leave us after 10 years' membership of the Fund. This vested right includes pensions derived from the Company's as well as the members' contributions. The Rules of our Funds permit the Trustees to preserve pension rights by either allotting paid-up pensions, or by transferring the actuarial reserve to other approved Funds. We do not follow the latter course for reasons into which I need not go here. Suffice it to say to the fearful that we do not regret that we instituted this early vesting, and that after nearly 10 years' experience we find the extra work involved is not worth mentioning. Paid-up pensions look after themselves; there is nothing to add to them and nothing to change. The Trustees can safely rely upon the beneficiaries reminding them when pensions become payable.

IX. SUMMARY

I. *Introduction*

103. Reference is made to the views on preservation of pension rights previously expressed on behalf of the Institute and the Faculty in joint evidence to the Phillips Committee, and to the Committee's observations on the subject in their Report. §§ 7–9 and Appendices A and B.

Responsible discussion proceeds on the footing that preservation of pension rights would apply only to the minority of persons who change their employment after substantial periods of service. § 10.

II. *General summary of existing practice*

104. Certain vocational pension schemes enable members of the professions concerned to change their employment from time to time without disturbance of their pension rights. §§ 13, 14.

Arrangements of wide scope for preservation of pension rights exist within the public and quasi-public services; the cold-storage and the transfer value methods are both used. There is also power (which has not so far been used) in S. 2 of the Superannuation (Miscellaneous Provisions) Act, 1948, for the arrangements to be widened still further to include transfers between public or quasi-public and private employment. The recent Royal Commission on the Civil Service recommended that no change be made in existing practice at the present time. §§ 15–29.

It appears that only in a limited number of privately administered schemes does power exist for arrangements to be made for preservation of pension rights, whether by the cold-storage method or the transfer value method or both, and that where the power exists it is not always used. §§ 30–33.

In life office schemes, the usual provision is for a member withdrawing voluntarily to be given an option to take a surrender value in cash in respect of his own contributions or the corresponding cold-storage benefits in the form of a paid-up policy with, sometimes, in the latter event, the benefit of the employer's contributions in the same form. Most withdrawing members take

a surrender value in cash. No provision is made for payment of transfer values from one scheme to another, other than the normal surrender values. §§ 34–39.

III. *The possible enlargement of existing arrangements*

105. Enlargement of the existing arrangements would require more widespread acceptance by employers of the principle involved, willingness of employees to forgo payment of withdrawal benefits in cash and, if the transfer value method is to be used at all freely, removal or reduction of certain taxation obstacles. The technical developments needed to enable really comprehensive arrangements to be made, include wider provision for the cold-storage and transfer value methods in privately administered schemes, and for the transfer value principle to be applied in life office schemes as well as the cold-storage principle. §§ 40–45.

IV. *The incidence of the cost of preservation of pension rights*

106. More general adoption of arrangements for preservation of pension rights would add to employers' costs, but the addition would be less than might at first sight be supposed. §§ 46–53.

V. *Methods of assessment of transfer values and cold-storage benefits*

107. There is no actuarial reason why pension rights should not be preserved on changes of employment. The technical problems that arise in the assessment of transfer values and cold-storage benefits in privately administered schemes are discussed in general terms. §§ 54–69.

In schemes for the public service, cold-storage benefits are usually based on equitable definition of the officer's accrued interest in respect of past service. Transfer values passing between local government superannuation funds are calculated by reference to appropriate scales, but the same scales are also applied to other schemes for which they are not strictly appropriate. §§ 70–72.

In life office schemes, an acceptable definition of accrued cold-storage benefits can usually be arrived at without difficulty. If the transfer value principle were to be introduced, the basis and method to be adopted for calculation of the transfer values would require consideration. §§ 73, 74.

VI. *Assessment of benefits granted in exchange for transfer values*

108. When transfer values are accepted in schemes for the public service, the period of pensionable service in the old employment is usually allowed to rank for superannuation in the new scheme and there is no actuarial calculation of the amount of the benefits to be granted in exchange for the transfer value. § 75.

In privately administered schemes, certain questions of policy may arise for determination by the trustees or managers of the scheme accepting the transfer value, with the benefit of actuarial advice. Once decisions have been reached on the relevant matters of policy, the requisite calculations can be made without difficulty. §§ 76–78.

If transfer values were to be paid between life office schemes, it appears that no difficulty need arise in assessing the nature and amount of the corresponding benefits to be granted in the new scheme. § 79.

VII. *Income tax position*

109. There appears to be no taxation obstacle to the creation of cold-storage benefits in any type of scheme. A pensioner benefiting from cold-storage arrangements may find part of his pension taxed under the P.A.Y.E. procedure and part under the DX–DR procedure. §§ 83, 84.

Transfer values can be paid from one S. 379 scheme to another without undue tax complications, and in certain other cases. There are, however, cases in which difficulties arise or where the position is not clear. Before there could be any comprehensive, or even widespread, adoption of the transfer value system, the position would have to be clarified and the existing obstacles removed or substantially reduced. This would probably require legislation. §§ 85–88.

VIII. *Comparison of the cold-storage and transfer value methods*

110. Finally, a comparison is made, point by point, between the cold-storage and the transfer value methods. §§ 89–102.

Acknowledgement

111. When the Working Party was set up, it was arranged that Mr H. W. McLellan, F.I.A., should act as Mr Bromfield's alternate in the Working Party's discussions. Mr McLellan has, in fact, attended all our discussions and we are greatly indebted to him for the contribution he has made to the preparation of this report.

APPENDIX A

Extract from Memorandum of Evidence submitted by the Councils of the Institute and Faculty to the Phillips Committee

Pension schemes and the mobility of labour

49. One of the major problems involved in the operation of pension schemes at the present time is the disposition of the pension rights of a person who changes his employment. Very commonly, a person who resigns from the service of one employer to take up an appointment with another is compelled to withdraw from the pension scheme attached to his former employment and to start as a new entrant in the scheme attached to his new employment. On withdrawal from the old scheme, the employee's own contributions (often subject to a deduction for income tax) are usually returned to him. The employer's contributions, however, frequently fall into the fund and are lost to the individual on whose behalf they were originally paid. Thus, on resigning his original appointment, the individual may well lose his accrued pension rights in return for a relatively small sum of money and, unless special provision is made for him by his new employer, his pension on retirement may fall short of the normal pension for his rank and salary.

50. There is no actuarial reason why pension schemes should not be designed in such a manner that individuals do not forfeit their accumulated benefits on leaving their employers' service. Naturally, preservation of accrued rights would add to employers' costs. At the same time, it has to be

remembered that the major part of labour turnover occurs after short periods of employment. Thus, the effect upon costs is probably less than might at first sight be supposed. Conversely, we doubt whether labour turnover would be appreciably increased by the extension of transferability of pension rights.

51. Two methods are available of providing for the non-forfeiture of accrued pension rights by a resigning employee. The first method is to give him a pension, based on his years of service to date, but payable only when he reaches pension age. This deferred pension, or paid-up pension, has often been graphically described as a 'cold-storage' pension. It is the method commonly employed in life office schemes but is also found in privately administered schemes. It is particularly suited to the case of an employee transferring from pensionable to non-pensionable employment. Since the employee's subsequent remuneration is no concern of his old employer, the cold-storage pension is naturally based on his salary at the date of transfer; it will depend on the nature of the pension benefits under both schemes whether this is a disadvantage or not; usually it will be. A further disadvantage of the cold-storage system is that the individual employee who has changed his job several times during his career will, on retirement, have to collect his pension from a number of different sources which may well be subject to differing qualifying conditions. Moreover, every pension scheme would have to maintain records and pay pensions to persons who had long left the employment to which the scheme applies.

52. The second method is to arrange for the payment of a transfer value from the pension scheme attached to the old employment to the scheme attached to the new employment and to grant to the employee concerned appropriate past pension rights in the new scheme. Power to pay and to receive transfer values is already quite common in privately administered schemes. This power is often exercised even in cases where the schemes are dissimilar in character. With the more frequent interchange of staffs in public employments in recent years, arrangements have been made over a wide field—comprising the Civil Service, Local Government, Teaching, Police and Fire Services, and the National Health Service—whereby a pensionable employee who transfers from one to another of those services carries his accrued pension rights with him and a corresponding transfer value passes from the old to the new employer. In view of the general similarity of the superannuation schemes, transfer values on a standard basis have been adopted, except in the case of transfers from the National Health Service. These arrangements have been extended to cover transfers between any one of the above services on the one hand and the majority of the nationalized industries and various public Boards on the other. The transferability of pension rights between the various nationalized industries is a matter for mutual agreement, but in some of them, at any rate, a somewhat similar procedure has been adopted. One manifest advantage of the transfer system is that it enables an employee to draw the whole of his pension from one source when he retires. Nevertheless, the employee who frequently changes his employment would, if always entitled to transfer rights, occasion some further administrative work.

53. Arrangements for transfer values on the lines indicated in § 52 could probably be negotiated over a wide range of other employments for which the superannuation schemes were not widely dissimilar. From the technical point

of view, the main consideration is that the transfer value payable by the transferring fund may be assessed by reference to the employee's accrued rights in that fund and the resulting sum of money may be used in the transferee fund to buy such additional benefits as it equitably will.

54. Further, whatever the technical differences between two funds, it would be quite possible for a new employer to accept whatever transfer value is forthcoming and give to the employee either the amount of his accrued pension in the old fund or the amount of the pension which would have accrued for the benefit of the employee had he served throughout with his new employer or indeed any amount that might be agreed. In short, just as the level of pension benefits is of interest to a new employee, so would the new employer's practice in regard to accrued rights be of interest to a transferring employee. He might decide to go to the new employment either because his accrued pension rights would be at least maintained or because other conditions were so attractive as to outweigh the fact that little or no credit would be given for his earlier service.

55. Manifestly, scope exists for a wider discussion of these matters, including some appraisement of the nation's best interest in regard to the question of the mobility of labour. Many employers regard the restraint which a pension scheme exercises on staff turnover as beneficial and it is noteworthy that in recent years concern has been expressed in various quarters because labour turnover is too high. On the other hand, mobility of labour is sometimes felt to be a desirable thing in itself. The situation needs to be clarified. If it were generally considered that increased mobility of labour would be beneficial to industry, employers might be more ready to incorporate in their pension schemes conditions permitting the transfer or maintenance of accrued pension rights. Such a development might be more acceptable to employers if some principle of restricted or partial maintenance of accrued benefits on transfer were adopted. For example, it might be provided that no rights should be acquired until after, say, five years' service. Thereafter, rights might be granted in respect of a fraction of the accrued pension, the fraction increasing with length of service until full rights were available at the end of, say, fifteen years. It would seem that there is scope for both cold-storage pensions and transfer values; each system has advantages and disadvantages depending on circumstances.

19 *May* 1954

APPENDIX B

Extract from Report of the Committee on the economic and financial problems of the provision for old age (*Cmd.* 9333)*

Mobility of Labour

246. In § 120 of the First Report of the National Advisory Committee on the Employment of Older Men and Women, reference is made to the fact that some loss of accrued pension provision ordinarily occurs in private industry upon voluntary resignation in order to enter another employment. In private schemes, whether financed through an internal fund or insured through a

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life office, a withdrawing employee may receive not more than a sum represented by his own contributions (usually accumulated at interest and less a deduction in respect of income tax), the value of which is much lower than the capital value of his accrued pension rights. The loss of rights thus incurred, which may be heavy in the case of those whose length of service is considerable, was thought by the National Advisory Committee to restrict the mobility of labour by limiting the opportunity of workers to transfer to other employment as they become older.

247. This issue, although raised by the National Advisory Committee in connexion with the employment of older persons, has wider implications. Mobility of labour is obviously desirable if the economy is to remain flexible and progressive. But a measure of stability in the employment field is also desirable, and in conditions of full employment there is perhaps a tendency towards an excessive turnover of labour rather than the reverse.

An employer can also reasonably claim that where skills have been taught at his expense his undertaking should benefit from the training so given. Indeed, a primary motive of employers when introducing pension schemes in the past has undoubtedly been to encourage and reward continuity of employment with a particular firm. Since the practice of providing superannuation cover has been spreading rapidly there has been some change in emphasis in the outlook of employers in relation to the need to make pension arrangements for their staffs. As we have already indicated, about one-third of the working population is covered for superannuation benefits and the number continues to increase. In these circumstances, especially under conditions of full employment, such schemes are becoming an important factor in the recruitment of staff. There is, moreover, a growing tendency to regard pension provision as 'deferred pay' and, as a corollary, certain measures have been adopted to preserve an employee's accrued pension rights if he should elect to enter another employment. With the spread of pension schemes and the growing acceptance of the principle of 'deferred pay', free movement from one employment to another without the penalty of a loss of accrued pension rights may well become a commonplace. There will be transfers to as well as away from particular employments so that transfer values will be received which will offset transfer values paid out; incoming staff will have received training in their previous employment which will compensate, at least in some measure, for the costs sustained by an employer in the training of staff who subsequently leave his service. Whether this is true in particular cases or not, under present-day conditions the national interest in its widest sense requires industry to respond rapidly to changes in demand and technological advances. The readjustment of manpower which will be entailed ought not to be impeded by any artificial restrictions arising out of pension arrangements. If the economy as well as the individual is to benefit from the free circulation of ideas and talent, it is particularly important that the technical and administrative staff in the higher posts should be able to change their employment without undue difficulty. If the position were ever reached in which virtually all employment offered superannuation rights, there would be reluctance on the part of employees to leave one employment for another, as well as reluctance on the part of employers to engage older staff, who would have to be fitted into pension schemes at late ages, unless there were adequate means of preserving pension rights on a change of job.

248. In our view, arrangements whereby the accrued pension rights of a person with substantial service may be preserved on a change of employment, including movement between the public services and private employment, are in the general national interest and would facilitate the employment of older persons to which the National Advisory Committee has directed attention.

249. Where, as is usually the case, membership of a scheme is confined to the staff of a particular employer, the preservation of accrued pension rights can be effected in two ways. Under the first method, which is widely followed in the public services, a 'transfer value', representing the value of the individual's interest in the fund associated with the employment which he is leaving, can be passed to the fund associated with the new employment, and applied to purchase, so far as it will go, back-service rights in that fund. Clearly such arrangements should be on a reciprocal basis as between one employer and another and can only be applied where the new employment has a pension scheme. There is an extensive system of reciprocal arrangements of this type in the public services, e.g. as between the civil service, local government services, teaching, and nationalized industries, to provide for the transferability of pension rights. Although the provision of transfer values is not at present common in private employment it has tended to become more prevalent. The second method of achieving the object in view takes the form of granting the withdrawing member the right to the accrued pension based on his actual service, which is placed in 'cold storage' until he reaches the normal retiring age for his old employment, when the pension so conserved becomes payable. We understand that this method is being increasingly employed in private industry, and it is analogous to that adopted in the Civil Service in relation to transfers of civil servants to particular occupations which are styled 'approved employment'. 'Cold-storage' pensions are particularly convenient in the case of pension schemes associated with life offices and such schemes already not infrequently include such a provision.

250. Our attention has been directed to two large superannuation schemes applicable to employees of private firms in large sections of a particular industry or trade, namely employees of the flour milling industry and officers in the Merchant Navy. An employee who transfers from one firm to another in one of these schemes carries his accrued rights with him and the need for the passage of transfer values or the provision of 'cold-storage' pensions does not arise.

251. We are advised that there are no technical difficulties in the adoption of the 'cold-storage' device. As regards the transfer value method, there may sometimes be technical difficulties, though we are assured that they should not prove insuperable. The method may well be unacceptable to many employers in the present climate of opinion, even though they may be disposed to adopt the 'paid-up' pension or 'cold-storage' method. Transfer arrangements are common form in other countries where occupational pension schemes are firmly established, e.g. in the United States. In some countries, notably Canada and the Netherlands, their provision, if membership of a scheme has lasted more than a certain number of years, is obligatory as a condition of approval for tax relief. In Canada, for example, the employee's prospective rights in the fund must, if relief under the Income Tax Acts is to be secured, vest absolutely when he attains age 50, subject to a minimum of 20 years' service.

252. We have given much consideration to the suggestion that it should be made a condition of approval or recognition by the Commissioners of Inland Revenue that schemes should include provisions to ensure that if an employee who has reached a particular age, such as 40, or completed a specific number of years, for example, 20, of pensionable employment, transfers to another employment with an approved scheme, a transfer value should pass; where there is no approved scheme in the new employment he should be entitled to a 'paid-up' pension placed in 'cold storage'. We appreciate that the question of approval for income tax purposes does not arise in connexion with the non-contributory and unfunded statutory scheme for civil servants. Provision is already made on an extensive basis so far as transfers within the public service field are concerned, but we presume that if it were national policy to ensure the preservation of substantial accrued pension rights on a change of employment, the Government would pursue a similar policy in relation to those of its own staffs who left for, or came from, private employment.

253. We have, with some reluctance, come to the conclusion that although the practice of granting transfer values and particularly of granting 'paid-up' pensions to employees leaving an employment is spreading, the general climate of opinion is not such that the principle of compulsion should be applied at this time. With the continued growth of pension schemes, however, the time may not be far distant when the idea of general transferability or the provision of 'paid-up' pensions will come to be widely acceptable. Such a development, by preserving accrued pension rights must tend to mitigate the demands on the Exchequer, whether by way of reducing the calls on national assistance or by limiting the demands that will be made from time to time for increasing the standard rate of retirement pension. We content ourselves, therefore, with recording our general approval of the growing practice of adopting methods to ensure the preservation of accrued pension rights. We hope that employers will give careful consideration to the desirability of making provision on these lines, whether by way of amendment of existing schemes or when new schemes are contemplated.

27 *November* 1954

ABSTRACT OF THE DISCUSSION AT THE INSTITUTE*

Mr A. E. Bromfield, in presenting the Report, said that the basis on which transfer values might be calculated could have been the subject of an entire report in itself, and the Working Party had been relieved that it did not come entirely within their terms of reference.

One of the criticisms of the Report made in the discussion at Edinburgh had been that it might have been more definite in either recommending or opposing the general adoption of transferability. The Working Party had felt strongly, however, that it was not their function to make such a recommendation, nor was it desirable that the Institute or the Faculty should take sides on the question. Their object had been to investigate whether preservation was practicable, and it was satisfactory that they had been able to come to the conclusion that in principle it was practicable, particularly since there had been some misinformed criticism in the Press of pension schemes as acting against the mobility of labour.

It was indicated in the Report that a distinction should be drawn between the application of preservation to everyone who changed employment and its application only to those who changed after a reasonable period of service. In theory there might be no distinction, but in practice there could be great differences as regards the cost and the amount of administrative work involved. Practical difficulties might be successfully handled in dealing with a relatively small number of people who transferred after a reasonable period of service, but they would amount to a formidable total if applied universally. In addition, from the point of view of the employer, it might be considered reasonable that he should grant pension rights to an employee who had given him a period of valuable service, but it might be considered quite unreasonable to give those rights to someone who left after a short period which might have been spent mostly in training.

Those were presumably the reasons which had led the Phillips Committee to recommend in its Report that preservation should be applied only to employees who served for a reasonable period. There might, for instance, be a graduated scale, such as giving 10% credit after 5 years' service, increasing to 100% after perhaps 14 years' service. It was a graduated scale of that kind which the Working Party had had in mind.

Mr P. I. Clemow, in opening the discussion, said that the preservation of pension rights had become a subject of public discussion, and it was probably the aspect of retirement arrangements generally which was most needful of attention. Previous opinions, as indicated in Part I of the Report, generally tended to the view that preservation of pension rights was desirable, at any rate for employees with substantial service.

The question might be asked in a slightly different form: 'Who wants pension rights to be preserved?' By considering the interests of the nation, employers and employees separately, they would be in a better position not only to answer the earlier and basic question, but also to see what obstacles stood in the way of a wider adoption of the principle of preservation of pension rights.

There had been in the past considerable difference of opinion whether it

* The discussion at the Faculty of Actuaries on 18 March 1957 is reported in *T.F.A.* **25**, 166.—Eds. *J.I.A.*

would be in the general interest to encourage mobility of labour. That question was considered by the Phillips Committee and their opinion, quoted in Appendix B to the Report under discussion, had been that greater mobility was desirable and that for that reason the preservation of pension rights was desirable. It might also be taken as socially desirable that employers should provide for the retirement of their employees and that the cost of that provision should be shared between them in an equitable manner. Consequently, he approached the subject with an eye to a greater extension of the principle of preservation of pension rights.

When reading through the Report, he had been impressed by the thoroughness with which the facts of the situation had been set out and the various practical implications of any change in the existing position discussed. They must all be grateful to the authors for having prepared such a firm foundation for the discussion, although he would add that he agreed with the opinion expressed at the Faculty meeting that the authors might well have indicated their personal views instead of restricting themselves to the bare facts of the situation.

When improvements to an existing structure were envisaged, one of the first matters to consider was the question of cost, referred to in Section IV of the Report. The first sentence read: 'It is obvious that the adoption of a policy of preservation of pension rights must lead to the payment to some people of larger pensions in retirement than they would otherwise have enjoyed and therefore that some additional cost must be involved.' The authors then pointed out that the true cost was less than the cost of all the additional pensions resulting from the adoption of that principle because the recipients might not otherwise have changed employment and because there would be less need for special arrangements for late entrants. He was not entirely convinced by that argument.

If preservation of pension rights were adopted as a universal principle, then it might well be postulated that the total contributions to retirement arrangements by employers and employees should remain unchanged. Since, in the long run, what came out in the form of benefits corresponded to what went in as contributions, the over-all quantity of benefits provided would remain approximately the same. From that standpoint the principle of preservation of pension rights was seen as a redistribution rather than an augmentation of benefits. The redistribution was between one employer and another according as the rights given to seceding members were greater than or less than the special arrangements previously made for late entrants. It was also between some employees and others according to the extent to which their eventual benefits depended on withdrawal profits. Finally, it might be between payments in cash and payments in pension form.

In any particular scheme it might be that the existing contributions were insufficient to provide what were regarded as sufficient benefits after including allowance for preserving rights on early termination of service; in that case, an increase in the contributions might be needed to restore the level of benefits and he agreed that an additional cost was then involved.

When an employer set up a pension scheme, which did he decide first, the level of the contribution or the level of the benefit? There was no certain answer, but probably the cost was the ultimate deciding factor. In determining the structure of a scheme, the employer had to decide on two related points. What pension rights should a withdrawing employee be permitted to take with him? What level of benefits should be provided for an entrant at an advanced age who

would not be able to complete a full period of service? In theory, to be consistent, an employee who withdrew and was immediately re-engaged should be in the same position as if he had remained continuously in the service.

In an 'average salary' scheme, if full rights were given on transfer, the answers to the two questions were determined automatically and the results were consistent. There was, however, no necessity for consistency and an employer, who gave little or no benefit to a withdrawing employee and at the same time gave no special treatment to late entrants, could provide a higher level of benefits on actual retirement for a given level of contributions. Another advantage of giving less generous treatment to withdrawing employees was that the employer might thereby be able to maintain a more stable staff. That, of course, was a deliberate hindrance to the mobility of labour, which was assumed to be in the national interest, but, if an employer's own interest conflicted with the national interest, what was he to do? Furthermore, even if the pensions granted to withdrawing members were consistent with the treatment of late entrants, there was a great advantage in making sure that the employees to benefit most should be those who were in that employer's own service at retirement. Every employer probably felt some moral obligation to make pension provision during service: the question of whether the provision was adequate could only be seen at retirement. By giving generous treatment to late entrants and low withdrawal benefits, rather than the other way about, the pensions produced would seem to be most adequate.

The point he wished to make was that the employer who unilaterally granted generous vested rights early in service suffered in three ways as compared with an employer who granted none. In the first place, he in effect granted a subsidy to other employers in the matter of pension provision; in the second place, he encouraged his own employees to leave him if they could obtain more satisfactory terms of service elsewhere; thirdly, he deployed part of his pension effort on those who would not be in his service at retirement. Those considerations, he thought, underlay the conclusion reached in §44 of the Report.

The granting of generous vested rights was a step in many ways similar to the earlier step of setting up a pension scheme. The employer felt he had a moral duty to provide for the retirement of his staff and he expected his rewards in a better ability to attract new staff and in increased loyalty of his existing staff. It seemed to be right and proper that retirement provision already made should not be conditional on continued employment, and the employer might well expect the same sort of rewards for embarking on a policy of granting vested rights after a suitable length of service.

The attitude of the Civil Service was of interest, since it was in many ways regarded as the model employer. Since its scheme was unfunded by nature, it was quite logical that no rights should vest, but he thought it was a pity that the extensive reciprocal arrangements being extended within the public services were not accompanied by the earlier granting of vested rights.

In §41 the authors pointed out three obstacles to the extension of arrangements to preserve pension rights in the private field. The first related to the employer, whose point of view he had just discussed. The second concerned the employee, who had by convention the option to surrender such paid-up rights as he might be granted in exchange for a return of contributions, with or without interest. It was a tradition in Britain that if a scheme was contributory the members should be entitled to a return of their own contributions, the only major exception being the case of schemes by endowment assurances. He could

see no particular logic in the tradition, but it was difficult to persuade a layman otherwise.

The absurdity of the popular conception could be readily demonstrated by taking an example. In a scheme in which the employee's contributions ranked as an expense for income tax and surtax purposes, it made no difference to the net cash position of either employee or employer how the joint contributions were divided, provided that the salary was appropriately adjusted. However, in the contributory scheme withdrawing employees would expect a cash sum on withdrawal of a return of their own contributions and in the non-contributory one they would not.

From what he had already said it followed that if preservation of pension rights was to become more general, one type of redistribution was likely to assist in great measure. If the disposal of pension scheme assets in cash payments to withdrawing employees was avoided, the funds left available could be used to increase pensions payable at retirement.

Coming back to the question, 'Who wants to preserve pension rights?', they were faced with a rather odd situation. If employees changing employment were given the choice between a return of their own contributions and full accrued pension rights from retirement age, the great majority chose the return of contributions. For that body of employees, they had the following paradox: (1) In order to encourage mobility of labour, they required to preserve pension rights. (2) In order to preserve pension rights, they needed to prevent employees surrendering their accrued rights for cash. (3) If cash payments on change of employment were refused, mobility of labour would be discouraged.

He would not pursue the fallacy in that argument. It raised the question whether frozen benefits should be forced on employees who preferred cash. In order to ensure that pension rights were carried on from one employment to another, it would be necessary, as pointed out in §45, to limit in one way or another the options of employees to surrender them.

Section V was, from an actuarial point of view, the most important part of the Report. He heartily endorsed the contents of §57: no one was likely to question the correctness of any basis adopted as long as anomalies between individual cases were avoided. It was also important that whether the transfer value method or the cold-storage method was used, the two benefits should be equivalent in value.

He would, however, disagree with a sentence in §65, where it was suggested that the trustees or managers of a scheme should decide which of two alternative bases was appropriate for determining a paid-up value. In his view, the basis to be used should be clearly defined in the terms of the scheme, since otherwise there was scope for argument and dissatisfaction.

The expression 'full accrued rights' was liable to be taken as meaning something specific, but that it had no innate merit as a measure of the proper paid-up pension to be preserved was seen by considering four different methods of determining benefit. If there were four pension schemes based on the same salary scale and service table, all providing the same pension at retirement for a normal salary career, different values of the accrued right at any earlier time would be given according to whether the benefits were calculated on an average salary, a final salary, a flat or a money purchase basis. If the system used gave an unduly high accrued pension, it was quite reasonable for the frozen benefit to be only a portion of it, as suggested in §66.

There arose a further problem which was to some degree bound up with the

extent of the accrued rights given. That was to determine the period of service after which cold storage rights should be granted. In the Report the expression 'substantial period of service' was frequently used, but he would like to ask what in fact was meant by 'substantial'. As stated in § 102, one large employer allowed full vested rights after 10 years. Personally, he would regard 15 years as the maximum time that should be allowed to elapse before granting a full scale of frozen benefits. At lesser durations over, say, 10 years a reduced benefit might be given. It might also be appropriate to couple more generous frozen benefits with a longer qualifying service and *vice versa*.

Section VII of the Report was devoted to the income tax position. It was perhaps noteworthy that the authors should contrive to do so without mentioning the Millard Tucker Report. It was there proposed that, in all future approved schemes, refunds of contributions on withdrawal should be taxed at the standard rate, subject to a refund of tax if the cash were subsequently paid into another approved scheme. He thought such a move would be a good thing since, as he had pointed out earlier, the attraction of the cash sum on withdrawal was strong. If, in fact, the conditions for approval of schemes made the maximum cash return to an employee equal to a return of his own contributions less tax, then he thought employees' resistance to preservation of pension rights would be largely eliminated. His personal opinion was that, as a condition of Inland Revenue approval, the Rules of any pension scheme should contain a provision for preservation of pension rights on a minimum basis after a minimum period of service. By preventing anomalies between employers it would be likely to lead to a wider acceptance of the principle of preservation of pension rights amongst employers, with practical effects far in excess of the minimum bases prescribed.

He would not like to leave the impression that he was in favour of effecting changes only by new legislation. He believed that much could be done, as it had been in the past, by the efforts of individuals and of companies under private management, but some official encouragement would not be unwelcome.

The authors confined their attention to the position in the United Kingdom, but it was not entirely inappropriate to consider the position in other countries. The conditions might not be the same, but they might yet learn from the experience of others in dealing with the same problems.

(1) In Canada, a member of a contributory pension scheme who had reached age 50 and completed 20 years' service had to be given the full benefit of the employer's contributions; in practice, it was usual to allow a partial vested right at earlier ages so that the vesting was gradually built up. In non-contributory schemes no benefit was normally given on early termination of service.

(2) In France, the compulsion on employers to grant withdrawing employees the benefit of the employer's contributions to a retirement benefit scheme was almost complete, however short the employee's period of service had been.

(3) In Holland, after 5 years' service, withdrawing members of pension funds had to be given the full paid-up pensions arising from their own and the employers' contributions. Those pensions might, however, be commuted if they were small in amount, or if the member was emigrating, or if the member was a woman leaving the service to marry.

(4) In Belgium, any pension rights accrued in an insured scheme had to be granted in full on withdrawal after 3 years. Although private funds were not currently subject to legal compulsion in that respect, they could obtain taxation advantages by following the same practice, and it was usual for them to do so.

Forthcoming legislation was expected to make the position the same for all pension schemes.

(5) In Denmark, a withdrawing member of an insured pension scheme had a right to the policy on which he and his employer had paid the premiums, but if he decided to surrender it the excess over a refund of his own contributions with interest was paid to his employer. Otherwise, he might continue premiums or make it paid-up. In private pension funds the employee acquired a full vested right, after 5 years, to the actuarial reserve, calculated retrospectively, subject to the conditions that if he entered pensionable employment he must pay it in to the new pension scheme, and that if the amount exceeded 1 year's salary it must be used to purchase a deferred annuity.

The countries which he had cited had been chosen at random and largely for the reason that he had most easily been able to obtain information on them. The examples he had given summarized the attitude towards preservation of pension rights on change of employment in some of the most civilized countries in the world, and it was necessary to consider whether Britain should follow the example of those countries in lending official sanction to the practice of preserving pension rights.

Mr R. W. Abbott said that in the past the general attitude towards pension rights had been governed by the provisions of S.379 of the Income Tax Act, 1952, where it was stated that the main object of an approved pension fund must be the provision of pensions on retirement at a specified age, which was commonly understood as the age of retirement from the employment concerned, and not on retirement or withdrawal at a much earlier age. That was usually the employer's attitude, he thought, to the question of 'frozen' pension rights, and it was usually the employee's attitude as well. As the authors of the Report pointed out, many employees preferred to have a cash refund on leaving the service rather than some kind of frozen pension or transfer value.

He wondered, therefore, whether they had been in error, as actuaries, in adopting for many years the terms which the layman used, terms such as transferability, preservation, portability or vesting of pension rights. It seemed to him that the multiplicity of terms suggested some uncertainty as to the principles involved. All those terms connoted the protection and maintenance of rights which existed at a given point of time. They did not convey what he thought needed to be conveyed—that what they were concerned with was the creation of a new right, namely the right to receive a deferred pension on withdrawal. He thought that, if they were not to prejudice the issue by assuming what they wanted to prove, it would be helpful if they considered the matter from the point of view of the creation of new pension rights rather than the preservation of rights which already existed. If they thought in terms of the creation of new pension rights, they might be better able to make clear to the layman the actuarial implications of what was proposed in the title of the Report.

On what principle should the creation of new pension rights rest? In Appendix B of the Report there was a reference to the principle of deferred pay. If the principle of treating pension benefits as deferred pay was admitted, it did not seem to him to be proper to deprive employees of that pay if they left the service of the employer after a short period of years. He wondered whether the authors had not avoided some of the deeper issues involved by stating that it had not been suggested in any responsible quarter that pension

rights should be automatically preserved for all persons leaving pensionable employment, however short their service. He recalled that a Minister of the Crown, when talking to the Association of Superannuation Funds some 2 years earlier, had said: 'A pension is, after all, deferred pay, and I should have thought as a principle that the more freedom the individual has to decide at what stage in his life he will get the payment for the work he is doing, the better for all concerned.'

Could they, then, be content to treat the problem simply as a problem of providing pension rights for employees who left the service of the employer after a substantial number of years' service, even if they defined 'substantial', as Appendix A tended to do, as 5 years?

There were four things to bear in mind. First, he thought that Governments, of whatever political complexion, which were concerned with problems of technological advance and questions of automation and transferring employees from one employment to another, would find it necessary to make various exhortations to private industry about the need to preserve pension rights irrespective of service. Secondly, it was becoming rather fashionable in certain political quarters to denigrate occupational pension schemes on the ground that they did not all provide full transferability. Thirdly, there was the question of competition between employers, and he did not think that it was at all impossible that employers, having found that with pension schemes they did not attract the labour they wanted, might find that in order to do so they must offer fully transferable pension schemes. Fourthly, there was the question of public policy. It was sometimes said to be wrong that tax relief should be given to pension funds and to employees and employers contributing thereto unless all the benefits were taxable. It was true that some tax was paid on the withdrawal of a member from a scheme, but he thought it was also true that for the higher-paid employees the tax relief they had had while contributing was greater than the tax which they had to suffer when they withdrew from the scheme and took a refund of contributions. So there were various forces working in the direction of full transferability of pension rights.

On the other hand, as the opener had said, it was the employees themselves who were most strongly opposed to compulsory provision of a deferred pension instead of a refund of contributions. Anybody who had assisted in the rather mournful process of dissolving one scheme and replacing it by another would know that so often employees tended to prefer a return of contributions to a paid-up benefit for the joint contributions, even when quite clearly it was against their own best interests. However, there was a precedent in S.22 of the 1956 Finance Act; a self-employed person could not encash the benefits that he had built up in respect of his own retirement; and perhaps that principle might be extended to employees' pension schemes and employees be prevented from having a return of contributions when they left the service of an employer. He thought it was clear that any extensive creation of pension rights would only be possible if employees themselves were prevented from having a cash refund.

If a pension, whether funded or not, was to be treated as deferred pay, several important results would follow. In the first place, the employer would become more concerned with the amount of the deferred pension which he had to grant or with the amount of the transfer value that he had to pay, and he was not likely to allow the calculation to be left to an actuary to be made when the employee withdrew, since, as the Report made clear, two actuaries might easily

have two different but equally tenable views as to the proper amount of either the deferred pension or the transfer value. It was true that they would normally consult with the trustees, but the trustees were not the employer, and it was the employer who would be financially responsible for the cost of the additional pension rights.

He felt that if full transferability were written into pension schemes, the whole financial basis of the schemes would need reconsideration. The employer would be concerned to know precisely what was the contribution that he had to pay for each employee for each year's service. That seemed to lead back to money purchase schemes, either the old-fashioned type or the life office type; and it might well be that final salary schemes, under which the cost for each employee was not strictly identified, would come to be severely modified, except perhaps for prosperous and large employers.

He suggested that some of those results might follow if they were led on from the principle of deferred pay to full transferability of pension rights; but he thought that there was another approach to the problem, one that the authors of the Report had not dealt with. They had taken it for granted that the creation of the new rights had to be financed by the employer whose service the employee was leaving. Was it inevitable, or even necessary, that that should be so? Was it not equally reasonable that the cost of those rights should fall upon the employer whose fund the employee was entering? It might be said that on that basis mobility of labour would be impeded, but he did not feel that that consideration ought at all times and in all places to govern their attitude to the much wider question of the enlargement of pension rights. In some circumstances and for some people frequent changes of employment might be desirable, both for the individual and for the nation; in other circumstances and for other people frequent changes of employment might be undesirable. However, the employer who recruited the employee was primarily responsible for the loss of pension rights in the first place, and he might therefore be properly charged with the cost of replacing them. Admittedly, an employer would be more reluctant to engage staff, particularly at high ages, if that were to come about as the recognized way in which pension rights should be preserved; but, when skilled labour of all types was scarce, it might not be a bad thing, and, if it led to less than full transferability, he personally would think that that was no bad thing either.

Mr G. W. Pingstone felt that all members would be grateful to the opener for having drawn attention to the position in other countries. In considering questions of superannuation policy, they might learn something from countries which probably in that field were more advanced than Great Britain.

There was some reference to the subject in the third volume of the *Transactions of the 13th Congress*. He thought it was a fact that in Sweden there was no minimum period of service required before an employee acquired vested rights in respect of the employer's contribution. There was, however, complete restriction on the employee in getting his own contributions back.

He was a little surprised that the authors of the Report had made little reference to any previous consideration of the subject. He would mention in particular a paper written by Mr A. S. Owen and discussed before the Insurance Institute of London in November 1952. The subject had also been extensively discussed by bodies such as the Federation of British Industries, the British Institute of Management and the Industrial Welfare Society. Finally, it had

been touched upon by Mr W. F. Gardner in his Presidential Address to the Institute in October 1952.

There was one other omission which rather surprised him in the references to the Inland Revenue. It seemed to him that it might usefully have been mentioned that the Inland Revenue were not without a certain amount of blame for the existing position. In the early days of life office pension schemes—from about 1930 to 1933 or 1934—it had been common practice to allow vested rights in respect of employers' contributions after 7 years' service. The Inland Revenue had killed that by saying that, if there was such a provision, they would hold that the employee had too definite a right in the employer's contribution and would tax him on those contributions. For about 20 years the Inland Revenue had held to that position and it was not until the Committee on the Employment of Older Men and Women had come along that they had shifted their ground and finally agreed to the position as stated in the Report. He felt that that was an aspect which really ought to have been noted, because historically it was important.

With regard to the attitude of employees withdrawing from schemes and the determination of paid-up pension rights which they normally had, at least in relation to their own contributions, he had carried out an examination of a sample some years previously. He had found that 90% of the employees who elected to take their benefits in the form of pension received in addition the benefit of the employers' contributions. Whether that was cause and effect he did not know; but it did perhaps suggest that a change of attitude of employers might encourage employees to do the right thing.

It might also be mentioned that there had been schemes in which, in addition to providing cold-storage rights, life offices had made arrangements, on the surrender-value basis, for transfer values.

Mr M. W. Melton said that the comment that appealed to him most in the Report was that there was no actuarial reason why pension rights should not be preserved. Acceptance of that view, and of the implication that the administrative problems presented no insuperable difficulties, enabled the ground to be cleared, so that the more important decision of whether, and if so how, 'preservation' should be integrated with the nation's planning for old age could be taken without being surrounded by irrelevancies.

It was true that the introduction of transferability would bring many consequential changes to pension methods as currently practised; for example, it would seem to be automatic that some kind of 'clearing house' should be set up to collate the payment of small pensions from similar schemes, whether they were private self-administered funds or life office schemes. The main question could not, however, be considered as a problem *in vacuo*, and must be dependent for its answer on what the future was to bring by way of new design in national pension schemes. Each different possible development would produce a different answer to the transferability question.

In any planning for pensions on a national basis, three parties were concerned, and to each there was a separate but clearly defined appeal: (1) to the State—as a social-cum-political platform; (2) to the employer—as a trade mark of good behaviour in employee relations; (3) to the individual—as a means of assuring more security and equality in old age.

The arguments between the concepts of pensions as deferred pay or reward for long service were to some extent a conflict between the interests of the

second and third of those, and were as yet by no means resolved; but enlightened thought seemed to be veering towards the former view, always provided that complete vesting was deferred until it could be argued that any training costs had been fully offset by work done in the period. It was also considered that employees accepted lower pay where schemes were established, in anticipation of a pension on retirement, and that would seem to be of equal force whether contributions were paid by them or not.

The subject should be considered in the context of the national pension scheme, and the much publicized proposals that the existing scheme should be expanded so that benefits would be related to earnings; that was being actively canvassed, and it was hardly necessary for him to add a plea for actuarial sanity to prevail in any deliberations on the matter. Such a solution would envisage adequacy rather than subsistence for its goal, and it could then be argued that transferability—which was fully operative in the existing national scheme and so should automatically be included in any further extension—would not logically or equitably be desirable in any private schemes that employers superimposed.

It was debatable whether any financially practicable revision of the national scheme would always remain adequate in conditions containing any inflationary elements; and the temptation in the political arena to increase benefits without maintaining the same degree of funding would be permanently present. An alternative approach might be, not to increase the existing benefit level, but, as had been suggested in some quarters, to merge National Assistance and State pensions under a joint Ministry of National and Supplementary Pensions. That proposal itself could be criticized for absence of funding; but it would remove the stigma of 'charity' which attached to National Assistance and made it operate unfairly; nor should the cost increase astronomically.

If that method of dealing with the national problem were accepted, it might be desirable to include full transferability in all private schemes, but such arrangements could only be introduced satisfactorily if cash payments to employees, either on changing employers or on retiring, were completely eliminated. In those circumstances, pensions received from private schemes should not logically be fully discounted in assessing any supplementary grants to be made.

A compromise approach which might meet with some success would be to require all employers to set up pension schemes providing benefits at a certain minimum level. That could leave the current national arrangements unaltered, but would seem to demand compulsory transfer of private scheme benefits up to the statutory minimum; above that level free choice of withdrawal benefits could be maintained.

Current developments in employer–employee relations demanded that the different aspects of the nation's pension problem should not be settled in isolation, and it had been said that just as no employer should remain in business if he was unable to pay a standard wage, so should the same criterion apply to pensions.

Miss P. E. Merriman said that the Working Party had introduced them to three members of the 'Pension Rights' family. The great bulk of the Report was concerned with their two adopted children, the cash transfer value and the cold-storage benefit, but in § 100 the Working Party had introduced their own offspring, the cash transfer at pension age. Like all parents, the authors no

doubt had their personal preferences, but throughout the Report a strict impartiality had been maintained.

Her own preference was for the cold-storage benefit. The cash transfer value frequently caused mischief on public appearance, creating arguments and disagreements which might even at times lead to criticism of its actuarial parents.

The Working Party described some of the worst pitfalls in §62. The procedure of first ascertaining the cold-storage benefit and then calculating the corresponding transfer value avoided the extremes of excessively large and excessively small (or negative) transfer values. Even with that procedure, however, difficulties might arise if the transfer value was calculated on the valuation basis of the transferring fund. To be more precise, the difficulties arose when the transfer value was paid into another fund with a different valuation basis and the reverse process of converting the transfer value to accrued pension rights was attempted.

If the cold-storage benefit was calculated first and then the transfer value was determined from it, the conditions attaching to the cold-storage benefit might be such that salary increases, withdrawals, and early retirement could be ignored, so that the transfer value would then depend only on mortality in active service and after retirement and on the rate of interest. Even so, large differences might still arise because of the rate of interest assumed. One possible solution would be to tie the transfer values to the market rate of interest, by a method similar to that used to determine the purchase price of Post Office annuities. It might be possible to adopt standard tables of transfer values per unit of deferred pension, depending only on attained age, pension age, and the market rate of interest. It should be even simpler to agree on standard tables of cash transfer values at pension age, in accordance with the suggestions in §100 of the Report.

If it was agreed that the primary conception was that of cold-storage rights, the following alternative procedure might secure most of the advantages of the transfer value method, while avoiding the disadvantages. A member who was entitled to cold-storage rights on leaving pensionable employment could receive a 'cold-storage benefit certificate', which could in no circumstances be converted into cash by its owner, although he would have the right to assign it to the trustees of any approved pension fund to which he might later be admitted in exchange for pension rights from the second scheme, as agreed between the member and the trustees of that scheme. If he later transferred once more, he would reclaim his original cold-storage certificate, together with another one if he had earned further cold-storage rights in the second scheme. The trustees of the final fund from which he eventually retired would collect instalments of pension in respect of cold-storage certificates held and would pay the total pension from all sources to the pensioner. She envisaged that, where the instalments of pension were paid by the trustees of one approved fund to the trustees of another approved fund under such an arrangement, they would be payable gross and the trustees of the final fund would deduct and account for tax on the total pension under the P.A.Y.E. system.

Such a scheme would be advantageous to funds paying cold-storage pensions. They would not have to maintain tax cards in respect of them; furthermore, the payments would be made to the trustees of another fund at a fixed address. If two or more employees were transferred to the same fund, the payments in respect of them could be combined. The trustees of the final fund would shoulder the administrative responsibilities associated with the actual payment of the

pension, i.e. the deduction of tax under the P.A.Y.E. system and the consequent accounting to the Inland Revenue authorities, and maintaining contact with, and ensuring the continued existence of, the pensioner. Apart from the initial claiming of cold-storage rights under the certificates held, the final fund would be involved in little extra work beyond receiving the instalments of cold-storage pensions.

Such a system could also operate as between assured schemes, public service schemes, and privately administered schemes. If the final scheme were a S. 388 scheme, the pension would presumably be subject to the DX–DR procedure. The system could be operated quite satisfactorily, even though the degree of funding in the different schemes varied. If the member's final employment were non-pensionable, he would himself have to claim his cold-storage benefits, in the normal way.

Considering the benefits which might be given by a receiving fund in exchange for a cold-storage certificate, the least favourable treatment would be merely to hand on the benefits previously earned with no further increment. If it was necessary to convert to an equivalent (e.g. if pension ages in the two schemes differed), the entire conversion calculation would be on one actuarial basis and no anomalies could arise. Any change in the amounts of benefit resulting from a change in the conditions of payment could easily be justified to the member, and furthermore, while a member would have the right to assign his cold-storage certificate, he would be under no obligation to do so if he considered the terms in any way unreasonable.

At the other extreme, the member could be given full pension rights, on the scale appropriate to the receiving fund, in respect of his previous service. It was possible that the Inland Revenue authorities might agree in principle that benefits up to the normal scale of the receiving fund could be granted in respect of previous service covered by a cold-storage certificate. That would obviate the need to refer such cases to them under the terms of the undertaking.

Between those two extremes, there were many possibilities. For example, cold-storage rights might be converted to 'added years', which in a final salary scheme would protect a member from the erosion of his cold-storage rights as a result of inflation subsequent to the date of transfer. The adoption of such a system might lead eventually to an extension of cash transfer values. In the meantime, if cold-storage rights were agreed upon in principle, arrangements on those lines could be adopted as an interim measure with comparatively little difficulty.

Mr H. P. Clay expressed his general agreement with the Report, except for its title. He emphasized the point made by Mr Abbott that what was at issue was the creation of new rights rather than the preservation of rights. A member of a pension fund who had not completed the full period of service had a 'contingent right' to a pension, which he thought might be more appropriately described as a 'privilege'. He wanted to combat the idea that if an employee, having contributed to a pension scheme, left the employer's service, he should expect a cash return at least equal to the total of his contributions without any deduction for income tax.

He wished to call attention to the difference between §41 (*a*) and §102. The Working Party suggested that the question whether pension relating to the employer's payments should be granted to an employee should be considered after a period of service, whereas §102 quoted the opinion of a practical man in industrial pensions who spoke of employees who left after 10 years' *membership*

of a contributory fund. He thought that that test of contribution was important. Employers were seeking to assist thrift, and the test when a man left, as to whether he took cash or not, was a valuable test. Another test was whether he gave more than the legal period of notice. If the employer discharged a man whose services were no longer required because of mechanization or some other development, the employer would probably give more than the legal period of notice. He thought that that should work both ways, and that the employee should give more than the minimum notice if he was to receive the benefit of the accrued pension. He felt that it was right that the employer should have the last word in deciding whether pensions for service up to date should or should not be given to an employee who did not take a cash refund. To promise vested rights and to tell a man when he joined that he would have the full accrued pension (including that part purchased by the employer) if he left after, say, 5 or 10 years' service, was undesirable.

Mr J. Edey, referring to §35 and to Mr Pingstone's summary of the changes in the attitude of the Inland Revenue, felt that the Revenue still retained some of their former views. Although they were prepared to allow the full transfer value or the full paid-up benefit in the case of a S. 379 scheme, they were not, he thought, yet prepared to allow it in all circumstances in a S. 388 scheme. He had had that confirmed within the past 18 months quite specifically, and he had no reason to suppose that they had changed their line; they insisted that the employee should not have the right in the event of his dismissal for misconduct.

In §§15–29 of the Report there was a summary of all the provisions for preservation within the Government service, both central and local government. He rather wondered whether the feeling behind that was one of preservation or not. It seemed to him that nearly all those arrangements were to facilitate transfer from one department of the State to another department of the State, as though a large composite employer had got transfer arrangements between his subsidiaries. It did not seem to him quite as though it was a preservation of rights for the employees, but rather a matter of convenience in transferring from one department to another.

Sir Richard Snedden (a visitor) wished to mention one or two practical considerations from the employers' point of view. He agreed with much of what Mr Abbott had said. In considering the position in foreign countries, it was not enough merely to take the private pension schemes alone; regard should be had also to the social insurance economy of the countries concerned. The position in Canada and in the United States was then seen to be very different.

He thought he could say that employers were united in being opposed, not to transferability nor even to cold storage, but to compulsion in the matter, and he was glad to see that the Phillips Committee had supported that point of view.

He thought that some of the confusion in the comments on the Report arose from the fact that they were talking about different types of employees. In giving evidence to the Phillips Committee, witnesses had not really been talking about schemes for office staffs and the like; they had been talking about industrial schemes, mainly designed for what had previously been called manual workers—workers in the machine shops, factories, and so on. That was a very different proposition from the other type of pension scheme which many of them had in mind.

The Report under discussion was interesting and constructive, and above all it was extremely well timed. He need not say to those who were particularly concerned with insurance company arrangements that the extension of voluntary schemes in industry was almost paralysed at the moment, because employers would not consider additional pension schemes while both the great political parties, Conservative and Labour, were in the middle of considering and possibly producing schemes of their own. He noted that Mr Walley, Under Secretary of the Ministry of National Insurance, was present at the meeting, but he did not suppose that Mr Walley would, even if he could, disclose what the Government had in mind; but the Labour Party were going to produce their scheme by the end of the year, and that had a deadening effect on private employers and private industries producing schemes of their own.

He did not know anything about the mechanics of transferability, but he agreed with those who doubted the wisdom of talking about the preservation of pension rights. He agreed that preservation was a better description than transferability, for the reason given in the introduction to the Report, but preservation gave the impression that the rights were already there. The truth of the matter was that the rights were not there already, and what was at issue was the giving of further rights, as had been brought out by Mr Abbott in his remarks.

He had been a member of the Watkinson Committee and he had also given evidence to the Phillips Committee. There were both a moral issue and a social issue involved. There had been a suggestion—made elsewhere—that there was something improper in an employer's retaining the withdrawing employee's share of the contributions, but that was a misapprehension. The employee's share remained in the fund to increase the pensions of those who continued until retiring age. The question was also begged, in his view, by referring to deferred pay. He did not accept the view that the employer's pension contributions were deferred pay at all. Many employers did not take that view; they were willing to finance pensions for employees who remained in their service for a long time. That might not be a proper view to take, but it was a view that was taken and that must be recognized. It was not a question of the employer making off with the employee's share of the contributions; it remained in the fund and benefited the employees who remained with the firm or, it might even be, with the industry. Those were facts that should be taken into account in trying to build up a scheme. If the principle of transferability was carried too far, and was enforced by legislation as some speakers had suggested, the effect would be either to stop private schemes from developing altogether, or to cause them to develop in non-contributory form. That was mentioned in the Report, and he thought it was necessary to consider whether it was desirable. He thought not, if only because contributory schemes were at any rate a form of enforced saving by employees.

He wished to make a few remarks on a personal note. In §250 of the Report of the Phillips Committee there was a reference to the officers' scheme for the Merchant Navy. There was an honourable mention of that scheme, and as he had been one of the joint authors of it in 1938, he was gratified by that reference. But he was a little unhappy about it because, although it was accurate as far as it went, it did not go the whole way. When the scheme had been introduced many of the largest and leading shipping companies had had their own schemes, and although the Merchant Navy officers' pension fund had the power to accept transfers from those schemes, few transfers had in fact taken place, and there

was no transfer in the other direction at all. They had in that scheme, which was the largest one in shipping, adopted the cold-storage principle, but they had also adopted something which might be considered for other schemes, namely, a 5-year 'thinking' period. By that he meant that there was automatic cold storage, but at the end of 5 years, if a man was quite certain that he had left the Merchant Navy, then he could get his own contributions back. It was interesting to observe how many, having left the Merchant Navy, possibly for domestic reasons and the desire to be at home, found within 5 years that the Merchant Navy was not such a bad life after all, and back they went to sea. In those cases, at any rate, their rights had been preserved.

He felt that there were social issues involved in the problem which were not nearly as simple as phrases like 'mobility of labour in the national interest' and 'deferred pay' might suggest. It was fascinating at times to gaze at the surgeon's kit, but it did not follow that in all cases an operation was desirable.

Mr L. J. Martin said that in a paper on the subject prepared for the Students' Society in 1956 by Mr D. Funnell and himself (*J.S.S.* **14**, 60), some thought had been given to some of the technicalities which arose in calculating the amount of a transfer value, and he would like to refer to a few of them.

In Section V of the Report, the authors set out two basic methods of assessment of transfer values, namely, a gross premium reserve for past and future service and a past service reserve based on accrued rights. As mentioned in the Report, the transfer value might be the whole or a portion of a member's actuarial interest, and Funnell and he felt that it could well include allowance for the member's net premium future service reserve.

The justification of that would be apparent on considering a hypothetical transfer between two identical 'average salary' schemes where the joint contribution payable was calculated on the valuation basis according to age at entry. If the original employer decided that he wished to place the transferring member in the same position in the new fund as he had been in the old fund, the transfer value must include, first, the past service reserve so that 'accrued rights' might count and, secondly, an amount sufficient to enable the member to contribute in the new fund at the contribution rate applicable to his age at entry to the original fund. That amount was the future service reserve expressed as the present value of the future difference in contributions.

The principle might obviously be extended to schemes where employee's and employer's contributions were expressed, solely for administrative convenience, as uniform percentages of salary regardless of age at entry, but in those cases the contribution to be taken into account must be the theoretical net contribution for the individual based on his age at entry and not the so-called 'joint' contribution which had no real meaning with reference to a single member.

However, whether or not in the event an employer would wish a transferring employee to be given the credit was a matter for his decision alone, and the actuary should indicate to the employer the alternative ways in which a pension might be considered to accrue and make his calculations in accordance with the employer's attitude. It should be noted that a net premium reserve would give consistent results as between one member and another.

A further point arose in connexion with the effect on transfer values of the rate and degree of funding, to which the authors referred in §68. Funnell and he felt that if an employer had decided in principle that he had an obligation to

a transferring member to preserve his accrued pension, the extent of the obligation should be unaffected by the degree or rate of funding, provided that the employer had either guaranteed the solvency of the fund or else intended to maintain the level of benefits.

From that it followed, first, that, since a guarantee of interest was really a means of varying the rate of funding, it should be ignored in the calculations; secondly, that the employer's obligation in an unfunded scheme should be the same as that in a fully funded scheme; and thirdly, that in a funded scheme any outstanding deficiency charges should be ignored, even though some part of those charges might refer to transferring members.

A technically difficult problem to which no reference had been made in the Report was the treatment of widows' and orphans' benefits. In general he felt that the assessment of the amount of a transfer value should take into account features appertaining to the individual rather than to the group of which he was a member. It followed that a transferring member's marital status should be taken into account, and that theoretically the reversionary method of calculation should be used. However, since it was almost certain that quinquennial valuations were made by the collective method, no reversionary factors would have been prepared and a great deal of work would be involved in calculating the transfer value. Since it was probable that the value of the widows' benefits would not be more than about a quarter of the total value, an approximation to the value on a reversionary method basis would be acceptable, and they had set out one such possible method of approximation in their paper to the Students' Society.

In conclusion, he wished to mention two small points. The first was that the actual amount of a transfer value was of great importance to the individual, and that as far as possible the best assessment should be made of his individual rights in the fund—i.e. he should not necessarily be treated as one of a valuation group. The second was that it appeared that the effect of 'reciprocal arrangements' might be misunderstood. It was sometimes thought that the cost of transfer values paid out was balanced by transfer values received. That was obviously not so, since additional pension benefits were granted for transfer values received and the saving in cost to an employer was, therefore, confined to the cost of any additional past service for which he would otherwise have felt compelled to provide.

Mr **F. A. A. Menzler** said that, before he commented on the wider aspects, there were one or two points in the Report which required 'annotation', especially in connexion with the Civil Service, which he regarded as the pioneer in all staff matters.

Preservation had a long history. There was a statement in § 17 that the so-called 'Public Office' Rules dated from 1911, and that was formally accurate, but the statutory power to make such rules had originated in the Superannuation Act of 1892. That served to justify his statement that the Civil Service was a pioneer in that form of activity. He wished that time permitted him to say something about his personal experience of when a public office was not a public office for purposes of the Rules.

In § 21 of the Report it was stated that civil servants at ages over 50 had what was styled a 'virtually absolute' right to a cold-storage pension. Incidentally, a civil servant who retired from the service at age 50 had no absolute right to a pension at all; it was all 'at pleasure'. Anyone who disbelieved that should

look at the unrepealed S. 30 of the Superannuation Act of 1934. The civil servant over 50 could, however, walk out with his cold-storage pension and go into private employment wherever he liked without hindrance. Of course, the power to grant a deferred pension if a person was leaving the Civil Service at an age over 50 was intended to work both ways. It also enabled the State to get rid, almost painlessly, of officials, especially senior men, who might be showing signs perhaps of premature senescence.

In §25 there was a reference to the Royal Commission on the Civil Service, which concluded, as the Report said, that 'the balance of present advantage lies with making no change in the existing arrangements'. It should not be deduced that the Commissioners had found the idea of preservation in itself repugnant. How could they in view of the elaborate system for the preservation of the pension rights of those who moved from one form of public employment to another, including even the nationalized industries?

He could not with propriety reveal the secrets of the private discussions within the Commission, but it could be deduced, he thought, from the Report that there had been a number of different points of view regarding the practical application of preservation for civil servants going to private employment. Fundamentally, the Commissioners had thought that the Civil Service was a career service, and that transfer from the Civil Service to private employment should be exceptional; but they had gone on to remark that if the practice of preservation continued to spread among outside employers, the application of the principle of fair comparison with outside employment—which was the basis of their recommendations with regard to pay—would require the Government to take into account the relative disadvantage, as compared with outside employment, which the civil servant might suffer by reason of the non-transferability of the Civil Service benefits as regards transfers to private employment.

In §31 it was stated that only 15% of the privately administered funds had power to pay transfer values. He suggested that, if figures were extracted for funds established since the war, the proportion might be considerably higher.

On the question of merits, the Working Party were properly silent. There were visitors present from the Civil Service who would, he was sure, have noted the Working Party's professional detachment in that respect; they must often have written similarly detached briefs for the guidance of their Ministers. It was said by defenders of the existing rigidities that it was all a matter for the individual and his prospective employer, but, as had been pointed out by the Watkinson and Phillips Committees, there was a third party to the transaction, namely the State, which was concerned with the general economic welfare, apart from the interests of the particular elements in it.

The Report had an Appendix which contained some good material, some of which should be rescued and put in the main body of the Report, and on which he wished to make a few comments. The National Advisory Committee on the Employment of Older Men and Women had really started the discussion on the public plane. It had stated that the lack of facilities for transfer of pension rights might limit the movement of older persons to more suitable employment. Naturally, the Phillips Committee had followed that up and pointed out that the issue had wider implications, and that mobility of labour was obviously desirable if the economy was to remain flexible and progressive. The Phillips Committee had gone on to say that the national interest in its widest sense required industry to respond rapidly to changes in demand and technological advances, and that

the adjustment of manpower which would be entailed ought not to be impeded by any artificial restrictions arising out of pension rights.

He suggested that the ultimate test was the public interest and not the feelings of employers or of employed persons. In that connexion the Phillips Committee said (in §252) that they had given much consideration to the suggestion that it should be made a condition of approval by the Commissioners of Inland Revenue that schemes should include appropriate provisions to preserve accrued pension rights. It seemed to him that it was not unreasonable to suggest that the State was justified in attaching conditions to income tax relief, if it was thought that the national interest would thereby be served, and that, he thought, was the crux of the matter.

It was sometimes argued that it was a matter for the individual and his future employer. He would only say that the employer and the employee were not always free agents to do as they would wish. The larger firms were copying the Civil Service hierarchical methods of grading and classification of duties, and employees had to be treated more or less alike. An employer could not give one man 25 years' full back rights when he had perhaps started his scheme only 5 years previously and had given existing staff only half back rights. It might cause so much friction as to prevent a man being brought in, although it might well be in the public interest to bring him in because he could make a bigger contribution on the technological side by going to the new employer.

Whatever might be said about the merits of preservation, he thought it was as inevitable as inflation. It was already happening on a large scale and was spreading rapidly. It was thought to be good for scientists and university staffs to go from job to job, private or university, taking their policies with them. It was supposed to be good for teachers, who could also alternate between teaching and other employment without impairing their accruing pension rights. It was also taking place within public employment of every type and among a growing number of the more enlightened private employers. There was the threat of a possible statutory obligation, which had already been commented on. It was to be hoped that, without waiting for compulsion by statute, existing schemes would follow the advice of the Phillips Committee that employers should give careful consideration to the desirability of making provision on those lines, whether by way of amending existing schemes or when new schemes were contemplated.

Mr J. A. Mulligan thought they were in principle agreed that it was good for the economy of the country that employees should be able to transfer from employer to employer; but, when a man moved unexpectedly and left a critical vacancy which had to be filled, would it be right to advise the employer that he should chase after the man in order to pay him an expensive benefit and then rely on the former employer of his successor to preserve the latter's pension rights? The company was probably prepared to pay some money to preserve pension rights; but it was surprising how easy it was to help the national interest when the national interest coincided with the individual's interests, which in those circumstances were to help the man joining the employment and not the man leaving. He therefore endorsed Mr Abbott's suggestion that it was the employer to whom a man transferred who should bear the burden of preserving his pension rights.

Mr N. C. Turner, in closing the discussion, observed that it had already been remarked that the Report had appeared at an opportune moment in view of the

widespread interest in the subject. The discussion had shown the need for a wide measure of agreement within the profession as to the principles to be followed by actuaries in dealing with preservation arrangements. If preservation was to be imposed by any form of compulsion, then he thought it was even more important that actuaries directly concerned should work on entirely consistent principles, and that the determination of either cold-storage benefits or transfer values should not be allowed to be dependent on the possibly partisan views of trustees or employers.

The Report had properly segregated its consideration of the actuarial and the other aspects of the problem. While the discussion had been directed to both those aspects, he thought it was fair to say that they had not been as clearly segregated in the discussion as they had been in the Report. It also appeared to him that the discussion had given rather too much time to the non-actuarial aspects of preservation and perhaps insufficient time to a discussion of the purely actuarial aspects. It could be argued that the actuarial aspects were a comparatively small part of a large problem, but none the less the discussion in Staple Inn should, he felt, primarily be directed to the actuarial aspects. Having said that, he would confess that that criticism would probably be applicable to himself by the time he had finished, because he proposed to say very little about the actuarial aspects, leaving them to the authors of the Report in their reply.

He wished to make one or two comments on the method by which preservation could be achieved. He could not help feeling that the cold-storage method had little to recommend it, except perhaps in the special case of the employee who transferred to non-pensionable employment. No pensioner would be happy at receiving his ultimate pension in odd amounts from various sources. He did not think that any pension fund or life office would be happy at the thought of maintaining a number of comparatively small paid-up pensions in force for a number of years and then having to pay small amounts. Equally, he could not imagine an employer with a private fund being content to cover the mortality risk and the possibility of interest loss for the remainder of the working life of a man who had left his service many years before. He therefore favoured the preservation of pension rights through the payment of transfer values, although he was inclined to agree with what was, he thought, the method favoured by the authors, namely, the calculation of the transfer value from the cold-storage benefit.

When they turned to the other problems referred to in the original Council decision, they could allow themselves to range widely over many aspects with which professionally they were not concerned. They might, if they were not careful, find themselves as actuaries expressing opinions on non-actuarial subjects, and that route could lead them into dangerous places, particularly when the non-actuarial subject had a political flavour. What they could safely say was that the extensive growth of transfer arrangements in the public service could only have the effect of influencing the general climate of opinion. Also, the rapid growth in recent years in the proportion of the working population covered by private pension schemes of one sort or another must tend to bring nearer the day when employers regarded pension schemes not just as a means to retain employees, but as an essential item in their terms of employment without which they could not obtain the employees they needed. He hesitated to differ from their distinguished visitor, Sir Richard Snedden, but he felt that more and more would leading employers come to look on a pension as a benefit which

accrued throughout the working lifetime of an employee or as a form of deferred pay which should not be taken away from the employee because he chose to change his employment. More and more, in consequence, he thought, would employers be willing to allow withdrawing employees to retain the pension provision built up during their period of employment. It was only reasonable that there should be some minimum service qualification before the full vesting of the right, but it was his personal opinion that that should be kept as low as possible, and he would like to see full pension rights preserved after 5 years' membership.

It had been remarked that there were three interested parties in any pension arrangement: the employer, the employee, and the State. Whilst all too few employees, particularly at the young ages, regarded pension provision as having much value, any spread of preservation rights could only be of advantage to the individual. He agreed with what had already been indicated in the discussion, namely, that at the time of speaking the majority of employers would object to allowing a withdrawing employee to take his pension rights with him. Personally, he found that a rather strange attitude, because transfer out of one employment almost inevitably involved transfer into another. For every employer on the losing end there was almost inevitably one on the receiving end. The receipt of a transfer value could only be of advantage to an employer in relation to the ultimate pension provision to be made for a particular employee. It seemed to him that the only real objection should come from those employers, if there were any such, who, from the nature of their work, might expect to be usually on the losing end.

The third interested party was the State. What was good for the State could scarcely be bad for more than a minority of the persons or institutions comprising the State. The State must be concerned with mobility of labour in the sense of wishing to encourage movement from decaying to progressive industry and from time to time from one industry to another where the change could bring about an increase in national productivity or an increase in production in particular sections of the economy, such as exports, which might be desirable for special reasons at a particular time. From the point of view of the State, then, a degree of mobility was highly desirable, and that mobility should not be prevented by loss of pension rights. It could not, of course, be in the interests of either employer or State to encourage in any way the casual type of transfer—the movement of the employee who merely wanted a change. The loss of skill and experience brought about by such moves could only have an adverse effect on the productivity of both individual firms and the State.

He suggested that it should not be supposed that the preservation arrangements would in any way actively encourage the transfer of labour. They did not, in fact, do more than remove certain discouragements. It was not, therefore, to be presumed that the widespread introduction of the principles of preservation would have any considerable effect on the volume of pension scheme withdrawals. Obviously, if the whole of the working force of the country were covered by pension arrangements in virtually identical form, there would be few objections to preservation arrangements and comparatively few practical difficulties. The difficulties were enormously increased by the wide differences between individual schemes and by the fact that in many employments there were no schemes in existence.

They might perhaps ask themselves what effect those difficulties had on practical arrangements for preservation and on the desirability or otherwise of arrangements being made compulsory. He suggested that compulsion on the individual was probably undesirable in itself. For the man who was transferring to non-pensionable employment, any compulsion was virtually impossible, at least in the absence of some special State-made arrangement, which probably no one would like, or in the absence of special provisions enabling a transfer value to be applied as a single premium for a deferred annuity of a type comparable to those available for the self-employed. On the other hand, it was, he thought, quite feasible to consider the desirability of compulsion as applied to the employer with a pension fund or a life office scheme. It was his opinion that all that preservation should seek to do was to provide the transferring employee with the opportunity to maintain his accrued pension rights, and that would involve compulsion on the old scheme to allow cold-storage benefits or to pay a transfer value at the request of the employee. It was made clear in the Report that there were certain taxation difficulties which would need to be removed, but subject to that essential preliminary, it was his personal opinion that there should be no objection to compulsory preservation of pension rights (subject to a minimum service requirement) being made a condition of Inland Revenue approval.

The President (Mr C. F. Wood), in proposing a vote of thanks to the Working Party, said that the Institute and the Faculty were indeed fortunate in knowing that when a task had to be undertaken requiring knowledge and skill, patience and hard work, there were members who would come forward to give ungrudgingly of their time and their services for the benefit of the profession. Three such men were the members of the Working Party whose Report had been discussed, a Report which had not only benefited the profession but, he ventured to suggest, would be of great value to Government officials, to employers and to all who were concerned with that important aspect of pension schemes. With the names of the members of the Working Party should be included that of Mr H. W. McLellan, who had attended all the meetings of the Working Party as an alternate for Mr Bromfield.

Those four men had already served the Institute and the Faculty in various capacities, and the work involved in the preparation of the Report had further placed the Institute and the Faculty in their debt. He hoped that the discussions which had taken place in Edinburgh the previous week and in London that evening had been regarded by them as a measure of the appreciation which was felt for the work which had been undertaken.

Mr F. H. Spratling, in acknowledging the vote of thanks on behalf of his colleagues and himself, said that the stimulating discussions at the Faculty and at the Institute were a reward which they valued for the effort which they had put into the production of the Report.

The title of the Report was a very short one of four words. The first word was 'preservation', and the Working Party had explained why it had been preferred to 'transferability'. The second and third words—'of pension'—seemed quite uncontroversial. The fourth word, 'rights', led into deep questions of philosophy, more contentious than the actuarial problems of preserving what might or, it seemed, might not exist. But however it might be described, he thought there was no doubt of the practical importance of the subject of the Report.

The phrase 'substantial' had been picked on. He did not know what the Phillips Committee meant by that phrase, but it had seemed to be good enough for the Working Party. The principles were the same whether it meant 5, 10, 15 or 20 years. But as Mr Bromfield had said in introducing the Report, there was a great difference in the weight of the practical problems attaching to different definitions of that phrase.

He was grateful to Mr Clemow for filling in a gap which Mr Pingstone had criticized, namely, that there was no reference in the Report to foreign practice. Rightly or wrongly, the Working Party had interpreted their terms of reference in the way they had described in § 11. Mr Pingstone had also criticized the Working Party for not referring to certain other contributions to the knowledge on the subject, and he would like to assure Mr Pingstone that, even though it was not mentioned in the Report, the Working Party had made it their business to study the literature on the subject so far as it had been available to them. He was grateful to Mr Pingstone and to Mr Edey for their references to the income tax position. The Working Party had had a difficulty which he was quite sure that many members present had experienced themselves; they had found difficulty in establishing just what current Inland Revenue practice was, let alone what it had been 20 years earlier.

He liked Miss Merriman's development of the idea in § 100, and he looked forward to seeing her contribution in print, so that it could be considered in more detail.

To Mr Menzler he would say that he was grateful for the additional information on the 'Public Office' Rules referred to in § 17 and for the further references to the matters discussed by the Phillips Committee and the Royal Commission on the Civil Service.

He wished to conclude by expressing his personal thanks to his colleagues and to Mr McLellan. It had been a privilege for all of them to be joined together in a joint Faculty and Institute enterprise of that nature.

The **members of the Working Party** have sent the following written reply to the discussion:

In most pension schemes except the vocational schemes referred to in §§ 13 and 14 of the Report and those of the public service schemes which are covered by the arrangements described in §§ 15–19, preservation arrangements would unquestionably be an additional benefit which would have to be paid for. The discussion in Section IV of the Report proceeds on the footing that the cost in respect of outgoing employees would fall on the scheme associated with the employment they are leaving and shows that in most cases it would be borne ultimately in whole or in part by the old employer. Mr Abbott and Mr Mulligan suggested that the cost should be borne by the new employer. In cases where preservation arrangements do not apply in respect of the old employment that has for long been done on a limited scale in the public services, and in some private employments by means of such devices as 'added years'. Arrangements of this kind are usually confined to persons with exceptional qualifications or experience, or both, whose services an employer strongly desires to acquire. In our view, it is essentially a principle of limited application; it would not provide a satisfactory means of dealing with the problem of preservation of pension rights on a large scale.

It must, however, be recognized, as Mr Menzler indicated, that the large employer has a special problem when he needs to enlarge and strengthen his

staff by importation of specially qualified people in mid-career who have gained their experience elsewhere. He must treat people in his employment carrying comparable responsibilities more or less alike. This applies with particular force in the public services, where there are special constraints on the salary levels for particular posts, and may well be an important reason why there are such comprehensive arrangements for preservation of pension rights in the public services.

Miss Merriman's suggestion, that certificates of cold-storage interests should be capable of assignment to the trustees or managers of other approved pension schemes, is interesting and might contribute to a solution of the administrative problems that would arise if arrangements for preservation of pension rights became more widespread. In so many schemes there are rules prohibiting the assignment of benefits that documents of this kind might require some special legal sanction either by statute or by suitable amendment of the rules of individual schemes. Such a method could readily be associated with the establishment of a clearing house of the kind visualized by Mr Melton. Detailed problems would arise for solution in the amalgamation of a number of separate cold-storage pensions payable to a single individual, for it is most unlikely that the same conditions concerning, for example, frequency of payment, length of guarantee period, whether there is to be a proportionate payment to date of death or not, tax position, and so on, would apply to the separate parts of the combined pension; but there should be no insuperable difficulty.

Mr Clemow expressed a wish that some provision for preservation of pension rights should be made an added condition of approval of private schemes for tax purposes. Mr Menzler said that to him it did not seem unreasonable to suggest that the State was right to attach conditions to concessions or income tax relief if it were thought that the national interest would thereby be served. While we would not dissent from the view expressed by Mr Menzler, we think we should emphasize that in the case of approved pension schemes the relief takes the form of a postponement rather than a remission of tax. So far as the employee is concerned, the 'build-up' is exempt but the pension benefits are taxable. So far as the employer is concerned, his contributions are allowed as an expense, but the pension payments are made out of the fund and so are not allowed as a charge against his profits; if he had provided the same pensions without making provision in advance the pensions would have been paid directly out of profits and would have been allowed as an expense. Thus, in both cases the Inland Revenue receives the tax eventually, although not necessarily of precisely the same amount.

In the discussion several speakers suggested that the strength of the case for preservation of pension rights depended on whether or not pensions provided at the employer's cost (or the relevant part of jointly financed pensions) were to be regarded as deferred pay. A different test, even if it does not always provide a definite answer, is whether the salaries and wages paid to the members would be correspondingly higher if there were no pension scheme. If the answer is in the affirmative, theoretically preservation should apply, and *vice versa*. Sir Richard Snedden thought, however, that the deferred pay argument begs the question and it is, perhaps, unlikely that the issue will be settled by reference to propositions which may not be capable of precise application to individual cases.