Institute and Faculty of Actuaries

DB Taskforce
Call for Evidence

IFoA response to the Pensions and Lifetime Saving Association

18 July 2016

About the Institute and Faculty of Actuaries

The Institute and Faculty of Actuaries is the chartered professional body for actuaries in the United Kingdom. A rigorous examination system is supported by a programme of continuous professional development and a professional code of conduct supports high standards, reflecting the significant role of the Profession in society.

Actuaries' training is founded on mathematical and statistical techniques used in insurance, pension fund management and investment and then builds the management skills associated with the application of these techniques. The training includes the derivation and application of 'mortality tables' used to assess probabilities of death or survival. It also includes the financial mathematics of interest and risk associated with different investment vehicles – from simple deposits through to complex stock market derivatives.

Actuaries provide commercial, financial and prudential advice on the management of a business' assets and liabilities, especially where long term management and planning are critical to the success of any business venture. A majority of actuaries work for insurance companies or pension funds – either as their direct employees or in firms which undertake work on a consultancy basis – but they also advise individuals and offer comment on social and public interest issues. Members of the profession have a statutory role in the supervision of pension funds and life insurance companies as well as a statutory role to provide actuarial opinions for managing agents at Lloyd's.

Institute and Faculty of Actuaries

Ashok Gupta
Chair, DB Taskforce
Pensions and Lifetime Savings Association
Cheapside House
138 Cheapside
EC2V 6AE

18 July 2016

Dear Ashok,

IFoA response to PLSA DB Taskforce Call for Evidence

1. The Institute and Faculty of Actuaries (IFoA) supports the Pension and Lifetime Savings Association's decision to establish a DB Taskforce. Tackling the pressures on DB schemes you raise in this Call for Evidence will be vital in ensuring the sustainability of DB pension provision. IFoA members have an active role in DB schemes and we draw on their expertise in our response.

General Comments

2. As a professional body with a Royal Charter, our response is focused on public interest concerns. We would hope that our public interest role offers the Taskforce an independent view of any solutions that you propose. It is worth noting from the outset that there are conflicts between different classes of scheme members, employers, pension schemes and shareholders in defining what is in the public interest and that balancing these conflicts will be crucial. For example, the perspective of the current workforce will differ from those currently receiving a pension. Providing security for former employees' benefits is important, as too is the ability to recruit and retain employees and security for the current workforce. It is challenging to assess which group should have greater priority, pension scheme beneficiaries, or current, and future, employees where employer covenant is at risk. We suggest that any solutions recommended by the Taskforce should avoid putting trustees in a position where they would have to favour one class of members at the expense of another class of members.

3. You recognise this challenge on page nine of your paper and within this section of your paper you include an expectation that the Taskforce will recommend solutions. Even at this stage, we urge you to highlight that those solutions could lead to a shifting of the balance of stakeholders' competing interests. We consider that the underlying issue in meeting these conflicting interests is not pension scheme legislation and regulation, but rather economics and finance, as it is about the allocation of scarce employer resources in meeting differing objectives.

Pensions Landscape

4. It is possible to identify the regulatory changes in pensions over the last 30 years that are contributing to today's landscape. However, we suggest there would be little benefit in attempting to roll back legislation to a supposed golden age of DB. Each change was made to meet a specific objective and so it could be unhelpful if we were to remove those changes.

5. We suggest that the most important change in the DB landscape was regarding the nature of the pension promise. While employers recognised the desire to provide the pension benefit, when it became a contractual right this changed the nature of pensions. The consequences of this change became evident in the challenges in altering benefits and with the introduction of s75 debt. Whilst we would not propose reversing this, we can learn from it. Schemes should look very closely at the consequences of changes to legislation when they are first proposed, to avoid pain further down the line.

6. The end result of the many changes in legislation, improvements in life expectancy[1] and the reduction in rates of return is that very few, if any, employers, are willing to take on the numerous risks inherent in a DB scheme. This means that individuals will have to take on those risks, and many, if not most, do not currently have the information or skills to manage those risks effectively.

7. Even if the regulatory environment were more employer friendly, it is unlikely that employers could ignore the last three decades and take a chance on governments remaining employer friendly in a DB environment.

Regulation

8. The Pensions Regulator (tPR) has encouraged trustees to reduce risk. Whilst we understand the motives for this, and we would not wish to criticise this reasonable position, we would highlight that one implication is as employers have struggled to meet increasing contributions, the risk reduction measures highlight the difficulties in achieving full funding. We would welcome any candid discussions about how trustees can address funding shortfalls, given falling returns and the lack of further employer contributions.

9. Such discussions would mean challenging questions for trustees in terms of investment approaches. We question whether trustees are qualified to address those questions, particularly, for very small schemes. We would support measures that provided trustees with the ability to understand the detail of these challenges much better.

10. We recommend that the Taskforce consider providing key organisations with an opportunity to meet with tPR to identify and address the main challenges affecting DB schemes. This could give trustees assurance that 'pensions experts' understand the challenging, if not impossible roles they have to fulfil. If the Taskforce were to take this recommendation forward, the IFoA would welcome the opportunity to support this.

Should you wish to discuss any of the points raised in further detail please contact Philip Doggart, Technical Policy Manager (Philip.Doggart@actuaries.org.uk / 0131 240 1319) in the first instance.

Yours sincerely,

Charles Cowling
Member of Policy and Public Affairs Committee, Institute and Faculty of Actuaries

[1] It would be more useful to refer solely to post retirement increases in longevity rather than from birth increases