Institute and Faculty of Actuaries

Noting report

Subject	Emerging pension funds
Regulation Board meeting	17 November 2020
Author	IFoA Executive
International Issues Considered	Yes – UK specific matter

A: Objective

1. To note an update on changes to the UK pensions landscape, including DB superfunds and Collective Defined Contribution (CDC) funds.

B: DB consolidation / superfunds

2. DB superfunds offer a way for employers to consolidate existing DB schemes, by replacing the sponsoring employer with a capital-backed vehicle, creating a large retirement savings fund which includes different company schemes. This means participating employers are no longer liable for member benefits.

3. Participating in a DB superfund will be a new option for schemes that have no clear way of securing members' benefits via an insurance company buyout. Crucially the capital requirements for DB superfunds will, for now at least, be less stringent than those required under Solvency II, and thus a potentially cheaper option than a traditional buyout. This may of course change after the UK leaves the EU.

4. It is expect that several billions of pension assets will transfer to superfunds during 2021 and 2022, initially relating to pension schemes whose employers are in distress or already insolvent. In these cases, the capital buffer offered by the superfunds is expected to offer a clear improvement to the likelihood of members receiving their benefits in full, and thus not falling into the PPF. PwC research suggests up to one million pension scheme members and £170bn of assets could take this route over the next decade.

5. TPR launched its interim regime for superfunds in June, ahead of proposed government legislation. The regulator last month published new guidance for trustees and employers. The guidance outlines a series of 'gateway principles' for trustees and sponsoring employers considering a transfer to a superfund.

6. **IFoA position:** Coming to a consensus 'IFoA line' on this issue has proved complicated, because of the differing viewpoints of actuaries working for pension schemes and those working for life insurers. A cross-practice IFoA working party is exploring the topic in more detail and expecting to agree a consensus position ahead of further consultation on the future legislation.

C: CDC Schemes

7. The UK Government is currently legislating for the introduction of collective money purchase, or collective defined contribution (CDC) schemes to become part of the pensions landscape.

8. DB and DC models place all the risks and associated costs – economic, financial, and longevity – with either the sponsoring employer (DB) or the individual member (DC). The Government believes creating a third option in the form of CDC schemes – where risks would be entirely with the members but shared between them collectively – could be beneficial to both sponsoring businesses and individuals.

9. Willis Towers Watson estimates that CDC pensions would be expected to average 70% higher than either individual DC insured annuities, or 40% higher than pensions provided on average in DB schemes. A 2013 study by AON also estimated that CDC schemes would have delivered a steady 28 per cent of salary over the past 50 years, whereas DC schemes varied between 17 per cent and 61 per cent.

10. As well as the expected public interest benefits of CDC schemes, they could also be an important growth area for actuarial work, particularly as DB schemes continue to close and more closed schemes begin to wind up.

11. However, at present Royal Mail is the only employer currently committed to introducing a CDC scheme. Royal Mail's scheme design is being seen as the blueprint for future CDC schemes, but there are a number of different ways the scheme could be designed that are currently being explored. It is unclear what employer appetite will look like once CDC schemes have been legislated for, particularly in the immediate-term economic situation.

12. **IFoA position**: The IFoA has been broadly supportive of the introduction of CDC schemes. In our responses to Government consultations and inquiries, we have said that CDC schemes could be a valuable addition to the UK pension landscape. We stressed however that CDC schemes should be considered as a way of 'levelling up' the offering for those in DC arrangements, not as a way of employers with open DB schemes reducing their contributions.

13. The IFoA is working closely with DWP and TPR as they develop the regulations that will sit behind CDC schemes, both in terms of how schemes operate and more specifically how actuarial work will be defined and regulated as they develop.

D: Recommendation

14. The Regulation Board is asked to note this update.