

# The future security of defined benefit pensions

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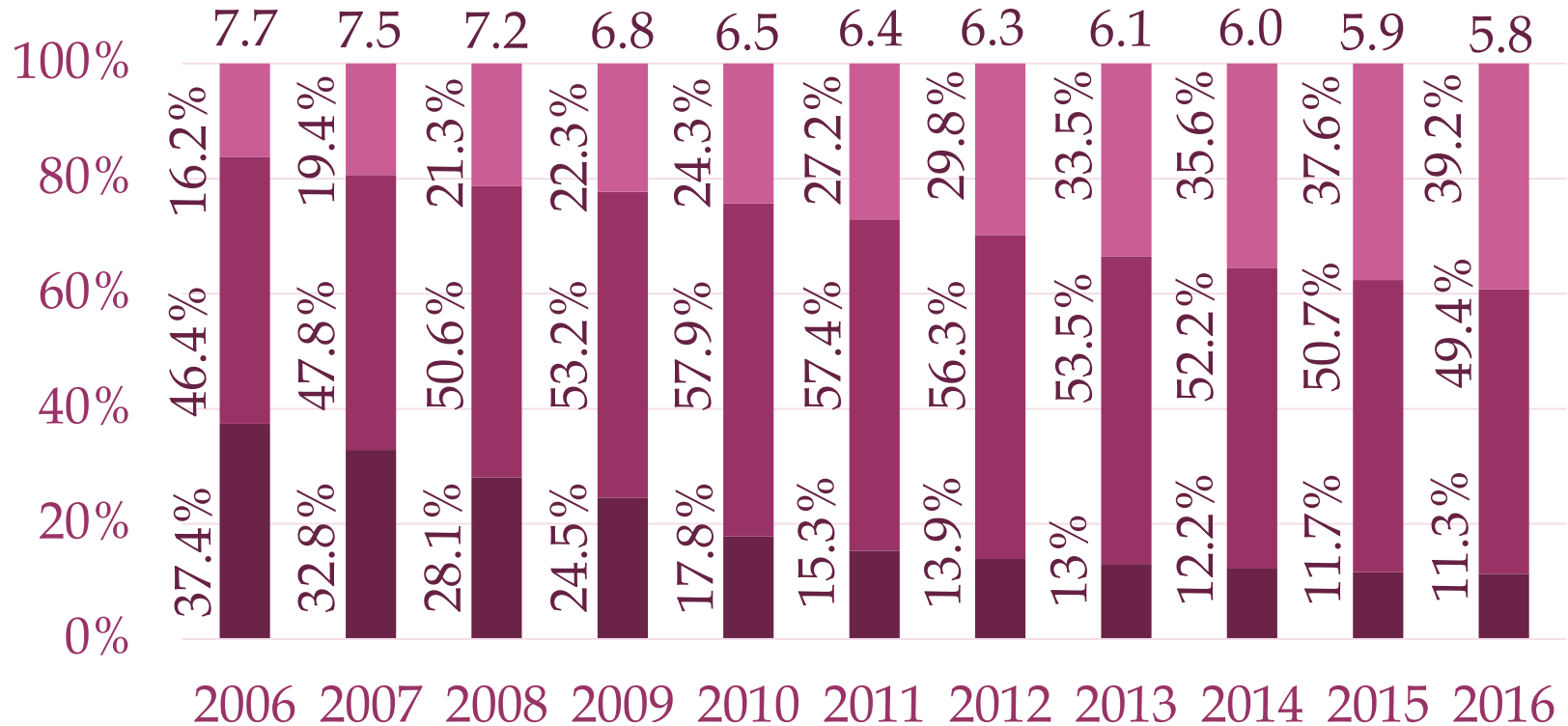
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# The future security of DB pensions

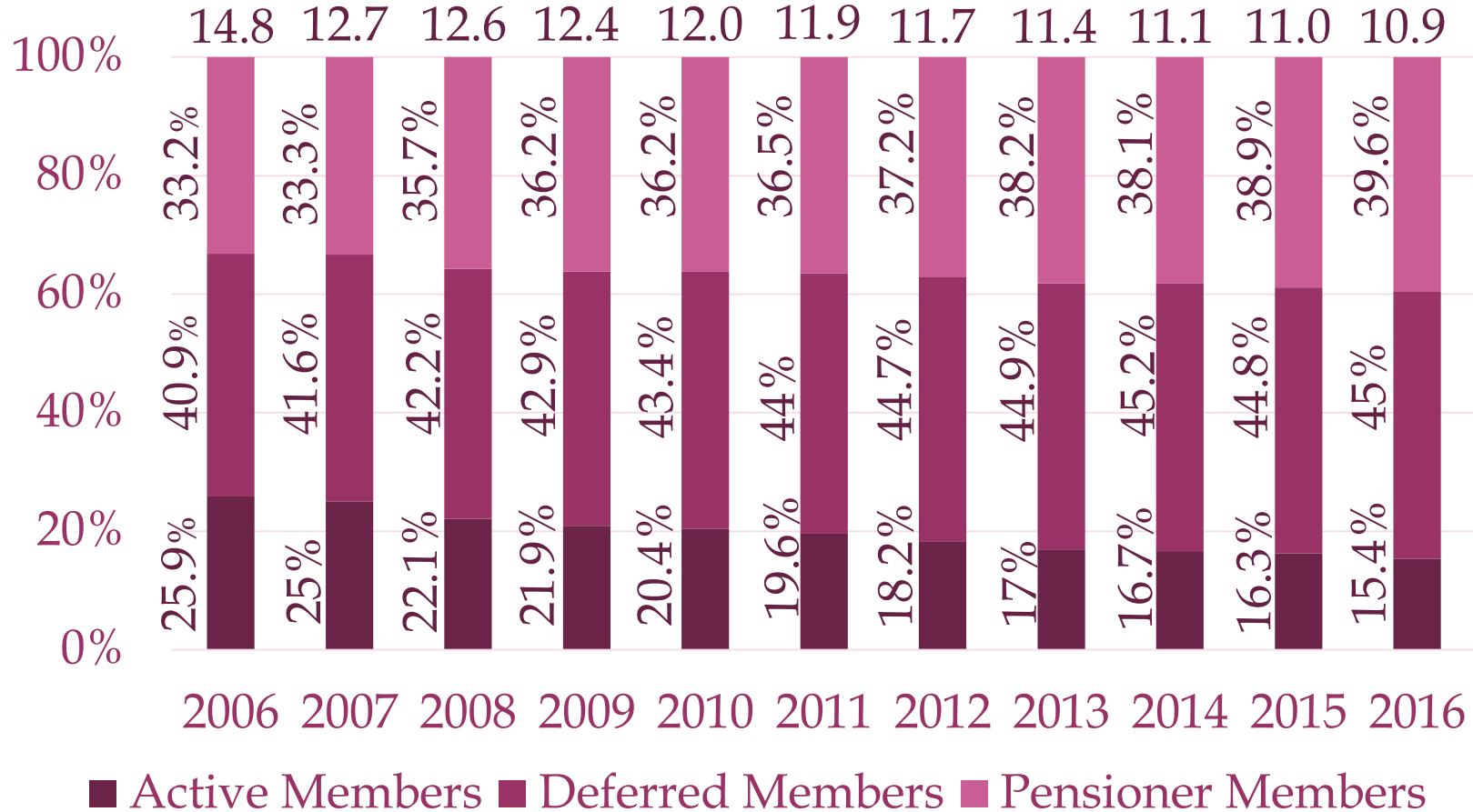
- Where are we on DB?
- What are the options for the future?
- How do these affect security?
- Do people want security?

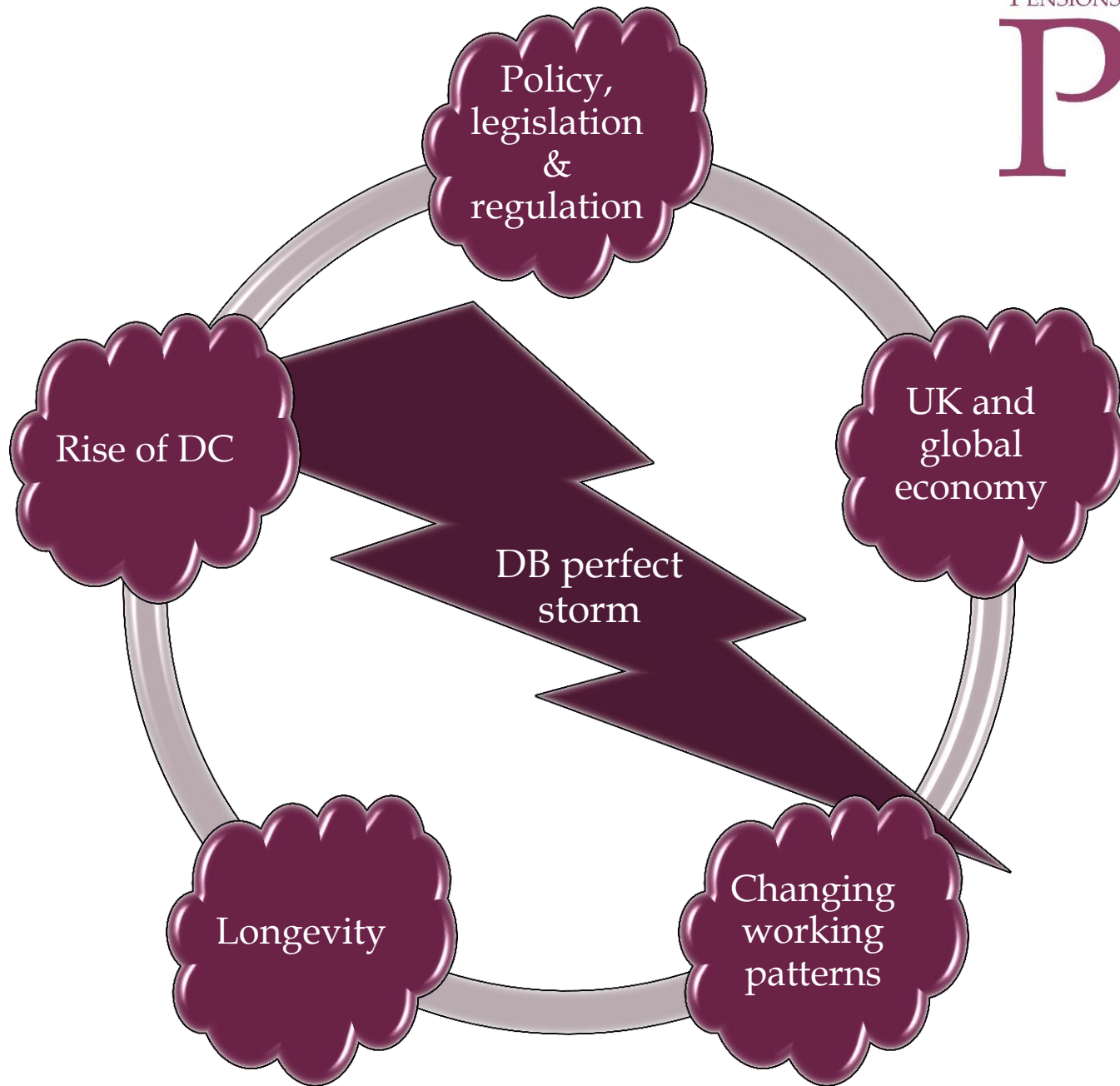
# The number of DB schemes, particularly open schemes, has declined



- Closed to new members and accruals
- Closed to new members/open to future accruals
- Open

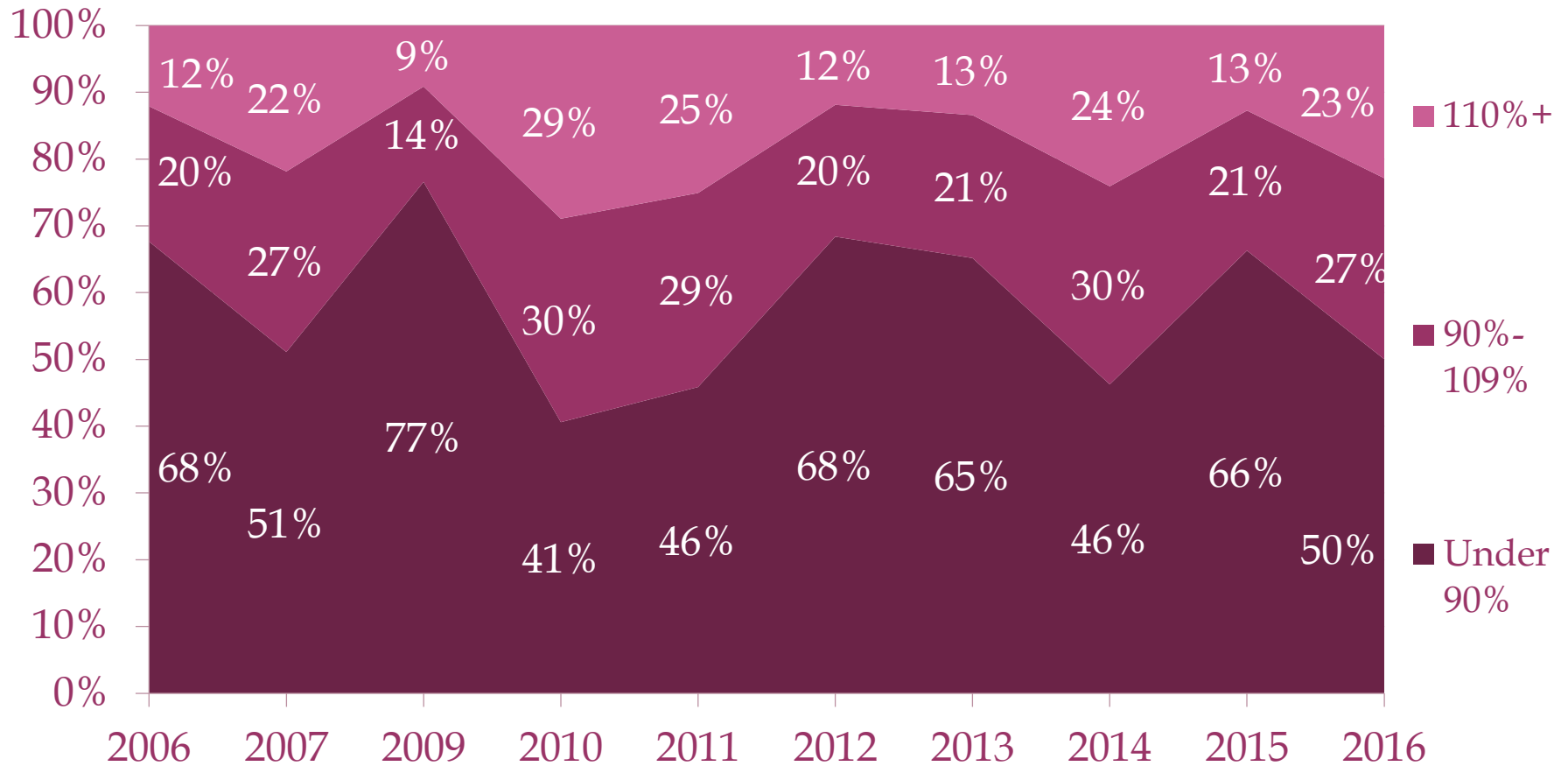
# The number of active members in DB schemes has declined relative to the number of deferred and pensioner members





# Funding ratios (s179) improve in 2016, although half of schemes still below 90%

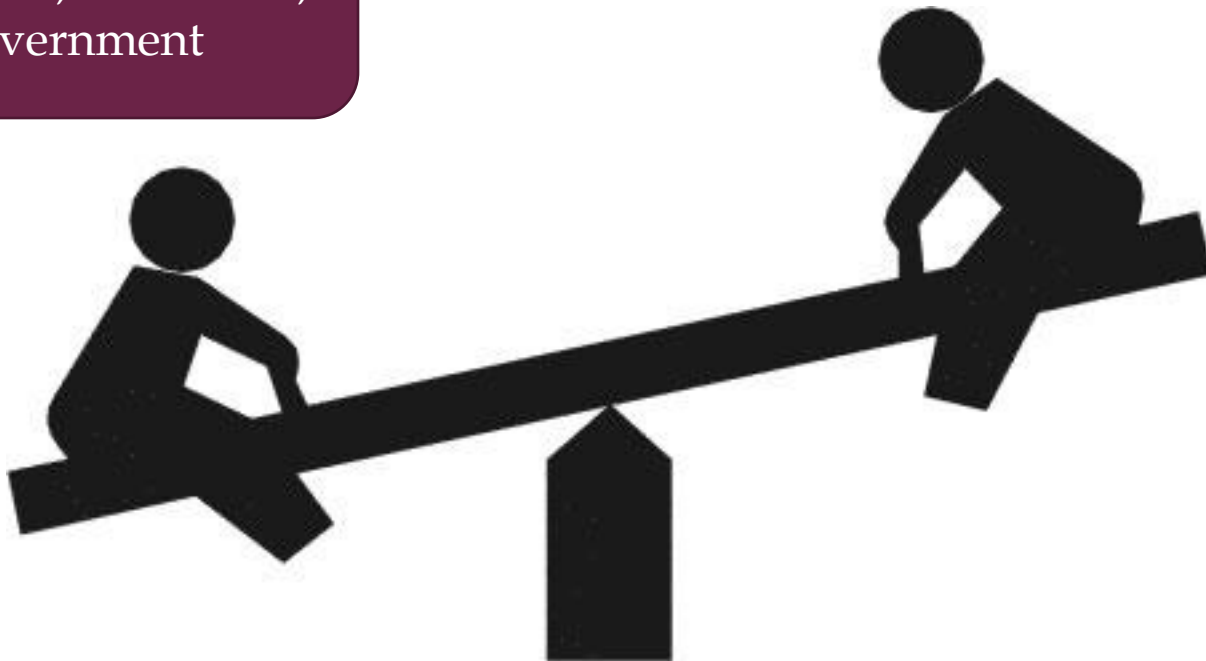
Data from TPR returns (no data for 2008)



# Balancing the needs of different stakeholders

Shareholders, current employees, customers, Government

Active, deferred and pensioner members



# Options for the future

- Does anything need to change?
  - *“The available evidence does not appear to support the view that these pensions are generally ‘unaffordable’ for employers. While DB pensions are more expensive than they were when they were originally set up, many employers could clear their pension deficit if required. There is also little evidence that scheme funding deficits are driving companies to insolvency, and it seems clear that the majority of employers should be able to continue to fund their schemes and manage the risk their schemes are running.”*
- But some schemes are definitely at risk
  - Worth remembering that the lower bound is no longer 0 – the PPF provides a minimum level of benefits



# Options for the future

- Assets could grow more....
  - “Better” investment over a longer time period
  - This could be linked to valuation (or at least interpretation of valuation)
- Or liabilities could be reduced
  - Changes to benefits (such as pension ages, salary definitions)
  - Changes to indexation - RPI to CPI
  - Even conditional indexation
- Consolidation is a more radical option
  - This could be of administration
  - or assets
  - or even liabilities as well, into a Supertrust (PLSA)

# What would this mean for security?

- Views on appropriate investment – and risks – are divided
- Reductions in liabilities would reduce the value of benefits, but make them more likely to be paid
- Economies of scale and efficiencies could reduce the cost of providing pensions and increase security
- The challenge is to increase the benefits from vulnerable schemes without reducing benefits from more secure schemes

# How much do people value security?

- It is now possible to transfer “secure” benefits from a DB scheme to a more “risky” DC scheme
  - Advice is required for transfers worth more than £30,000
- Why would people give up a secure income stream with investment, inflation and longevity protection?
  - Preferences for flexibility
  - If they have other secure income
  - Fears over security
  - Money illusion – blinded by a large lump sum
- While some transfers make financial sense, others may not
  - But is “financial” the only measure we should consider?

# The future security of DB pensions

- DB has been declining – but might not be in as bad shape as feared
- The challenge is in improving the security of vulnerable schemes without reducing benefits in more secure schemes
- But the shape of retirement is changing, and individuals appear to be placing more value on flexibility
- Should they?