FOR ISSUE IN THE UK AND EU. FINANCIAL PROMOTION/MARKETING MATERIAL.
FOR PROFESSIONAL CLIENTS AND QUALIFIED INVESTORS ONLY.
NOT TO BE REPRODUCED WITHOUT PRIOR WRITTEN APPROVAL.
**PLEASE REFER TO ALL RISK DISCLOSURES AT THE BACK OF THIS DOCUMENT.**

# THE FUTURE OF DB PENSION SCHEMES

APRIL 2024

BNY MELLON | INVESTMENT MANAGEMENT

# EXECUTIVE SUMMARY

A PANEL DISCUSSION HOSTED BY INSIGHT IN MARCH 2024 FOCUSED ON THE FUTURE OF UK DEFINED BENEFIT (DB) PENSION SCHEMES. THIS DOCUMENT OFFERS AN EDITED TRANSCRIPT OF THE DISCUSSION, WHICH COVERED THE ENVIRONMENT FOR DB SCHEMES TODAY, THE IMPLICATIONS OF THE CONSULTATION ON DB OPTIONS, AND A WIDE RANGE OF QUESTIONS ON THE PRACTICAL IMPLICATIONS FOR SCHEMES.

Sir Steve Webb
Partner, LCP

“If surplus extraction, pension run-on, new flexibilities, new underpins are of value and interest to you, they will not happen unless you tell the government.”

Paul Kitson
Actuary and UK Head of Pensions Consulting at EY

“We are definitely sensing a real move among CFOs from buy-out being the gold standard to…some recognising that the game has changed, and that in fact there may be another way.”

Simon Daniel
Partner in the Pension Practice at Eversheds Sutherland

“Where I’ve seen some of the healthiest discussions take place…is when people decide to think about the assumption, that has perhaps come from their advisers over the years, that buy-out is what they are aiming for and they must do.”

# THE ENVIRONMENT FOR DB SCHEMES TODAY

**Sir Steve Webb:** The funding level of defined benefit pension schemes shows that something extraordinary is happening. Whatever measure of funding you use, they all tell a similar story: DB scheme funding has improved dramatically.

Given this improvement you would assume that the government and pension schemes would be thinking very differently today relative to 10 years ago. But there is a risk of muscle memory, where the way of thinking through these issues is ingrained, and it takes time for things to change. The challenge for this panel is to consider what this new thinking might be, and what might be the pros and cons.

The fresh government thinking has been very recent (see box-out). It may be tempting to think that there is likely to be a new government within 12 months: but I would observe that new governments have typically spent years before coming to power campaigning to win an election, rather than drafting and thinking through the finer points of legislation on issues like the Pension Protection Fund (PPF) acting as a public sector consolidator. If that work has been done for them by the outgoing government, is at an advanced stage, is not particularly ideological, and might support their wider agenda (such as supporting productive finance), then you can expect to see continuity.

I would therefore argue very strongly that the current proposals and agenda matter, even if the government changes within the next year.

## THE MANSION HOUSE AGENDA FOR DB – KEY MILESTONES

- July 2023 Mansion House speech
  - Response to 2018 consultation on superfunds
  - Call for evidence on options for defined benefit schemes
    - Barriers to accessing DB surpluses
    - Potential for an enhanced PPF underpin to encourage productive investment
    - Potential creation of a public sector consolidator for 'unloved' DB schemes
- November 2023 Autumn Statement
  - Firmer commitment to PPF as public consolidator by end 2026
  - Announced further round of consultation
- February 2024
  - Publication of new consultation on:
    - scope of PPF as a public consolidator, and
    - DB surplus extraction (e.g., potential for statutory override) and 100% PPF underpin
- July 2024 Mansion House speech – decisions

Turning to the current consultation[1], the government is focusing on three big things. First of all, they are interested in the idea of enabling DB schemes to get money out more easily. The scheme rules now might say this can only happen when the scheme is wound up, and then it can only be extracted in a certain way; the proposal is to override these rules.

The second thing is that every time money leaves a scheme, that weakens the members' pension security, so the threshold at which surplus sharing is allowed is important.
Options include:

- 105% funded on a low-dependency basis;
- 100% funded, plus a factor reflecting a degree of investment risk;
- integrating the covenant (e.g., a minimum covenant strength); and
- full funding on a buy-out basis.

Alongside or instead of this, the proposal is to be able to buy extra insurance from the PPF to underpin pensions by 100%. Once you as a trustee know your members' benefits are 100% protected, you can be more relaxed about the investment strategy. The scheme can invest more for growth, and then stakeholders can focus on how to make best use of the surplus.

**If surplus extraction, pension run-on, new flexibilities, new underpins are of value and interest to you, they will not happen unless you tell the government.**

**SIR STEVE WEBB, LCP**

The final element of the consultation[1] is the proposal for the PPF to become a public sector consolidator, which would be an alternative to insurers. The PPF has since highlighted in its own blueprint that two of the government's objectives – to avoid upsetting the insurance market, and to maximise productive finance – are in tension. The PPF is seeking a maximalist approach, to be able to take over large and small schemes, and both well and less well funded schemes. This is a key point of debate. The current consultation suggests that the PPF would have no fundamental size limit. The scope of this could be huge.

A final introductory observation: the bane of government is when it consults, people don't respond, and it acts – then after it acts, people ask why they did so. My plea is that if surplus extraction, pension run-on, new flexibilities, new underpins are of value and interest to you, they will not happen unless you tell the government. There are a thousand things the government could be doing, and little time in which to do them. They will only do it if they think it will make a difference and there is demand to do it.

[1] Options for Defined Benefit schemes, 23 February 2024, DWP.

# THE CFO PERSPECTIVE

- Some CFOs are 'run-on curious', recognising the game has changed
- Understanding is growing that DB surpluses today are different to historical surpluses, which were based on a belief in equity returns when schemes were open
- There is acknowledgement of a DC crisis emerging, which will need more money from employees and sponsors to resolve

**Webb:** Paul, you talk to the nation's CFOs. Are there any CFOs out there who care about this?

**Paul Kitson:** Thank you. The short answer is yes, there are. I'm in a very fortunate position – we work with a number of trustees, but we also work with a number of corporates. We are definitely sensing a real move among CFOs from buy-out being the gold standard to what I'm describing as 'run-on curious', with some recognising that the game has changed, and that in fact there may be another way.

The first thing to say is that the position we're in today is fundamentally different to where we've been in the past. There's enough money in the system across the entire private sector DB world to buy out everything, and have about £100bn left over.

Of course, many schemes are in different positions. Some have too much, while some don't have enough and still have deficits. It's not that every scheme has a surplus today. But the fact that we start from a place that is fundamentally different from anywhere we've been means we can take different decisions.

In conversation with CFOs, many might say they want to focus on their business, and to be done with their pension scheme. When you ask why, a lot of what's behind that attitude is the uncertainty. Many remember, particularly the CFOs that have been in office for a long time, when we had contribution holidays; everything was going great. Then deficits meant companies paid contributions for many years, and now they are back in surplus – they don't want to run on in a world of up, down, up, down.

But CFOs are starting to understand that those surpluses of old were built off a belief in equity returns when schemes were open. It was a very different narrative to how we're seeing the potential for surplus to continue to manifest in a well-managed investment portfolio.

The second thing that is on CFOs' minds is the recognition that we have a crisis with DC emerging. Steve, you used to call it the slow-motion car crash; I've called it the crisis hiding in plain sight.

We are definitely sensing a real move among CFOs from buy-out being the gold standard to…some recognising that the game has changed, and that in fact there may be another way.

PAUL KITSON, EY

I don't think it's hiding in plain sight anymore. There's recognition from CFOs that those that only have DC are coming up to retirement in the next five, six, seven years with fundamentally less money than they're going to need, and they're going to be unable to retire. People are doing a lot to improve that position, but ultimately it is going to need more money from employees and the sponsor.

So CFOs are increasingly understanding that their pension costs are going to go up. We are not putting enough money into DC today, and that is going to start coming out on their watch as a CFO. They ask why we are in this situation, and they look at how much they have been paying into their DB scheme over the last 10 years – and this prompts the realisation that we've overshot the mark and potentially there is another way. The DB surplus is there today, and it can be generated in the future, to fund better pensions for current employees so they can actually retire when needed and with a good outcome for life. Anyone who looks at the PLSA retirement income requirements will see those numbers are quite scary in terms of what people have in their DC pension pots today.

So that is on some CFOs' minds. It's trickling through and even I notice it as I go and see a CFO one month, who is focusing on buy-out, to a different attitude the next month where they note their banks are talking to them about working on run-on.

CFOs are also starting to be cognisant that the only place now to really access third-party capital is that which the insurers put up when they take on the running of those schemes. I think over the coming months and years we will see an emergence of new technologies and ideas that bring third-party capital into pension funds to support run on. I think the 'connected covenant' model is one to watch. Buy-out doesn't have to be the only way to get third-party capital behind pension funds in a risk-managed way that CFOs may be more comfortable with.

Ultimately, if they're satisfied with the level of risk that's being run, they're happy with a pension scheme alongside their business. Time will tell whether the actual result is run-on or buyout or something different. But there is definite increasing cognisance from CFOs that different things are emerging and pension run-on is something they should be thinking about.

**Webb:** And are you noticing any sectoral differences? I tend to find financial services organisations are a bit keener to run on. And is there an M&A aspect to all of this? Back in the day, the DB scheme was almost the poison pill and something to get rid of. Is a DB scheme an asset now? Have we gone that far?

**Kitson:** Every situation is very particular, but there definitely are some sectoral challenges. Financial services companies think more about it, and those thinking more about financial wellness for their current employees are talking a bit more about those sorts of things.

# THE LEGAL PERSPECTIVE

- Buy-out has been assumed to be the automatic route or default option for pension schemes
- This assumption is being challenged in trustee meetings and by current consultations
- Trustees can consider a range of questions when considering their potential endgame

**Webb:** Simon, presumably there are plenty of trustees thinking, I only had one job – and I'm about to do it. They want to finish that job. Is it as simple as that?

**Simon Daniel**: It's important to recognise the way in which pensions legislation has always operated, from the days of the preservation regulations in the early nineties. This is to envisage that schemes would run on and pay pensions as they fell due and eventually get to a point where there were no liabilities left to discharge, and they would wind up. Under pensions legislation, buying out is an alternative way of securing benefits. Over the course of my career as a pensions lawyer, buy-out has been assumed to be the automatic route or the default option – as soon as a scheme is in a position to buy out, either because of its own funding status or because the sponsor can write a cheque, then that is what ought to be done. The prevailing thinking has been that not doing this exposes the trustees to regret risk and perhaps legal risk.

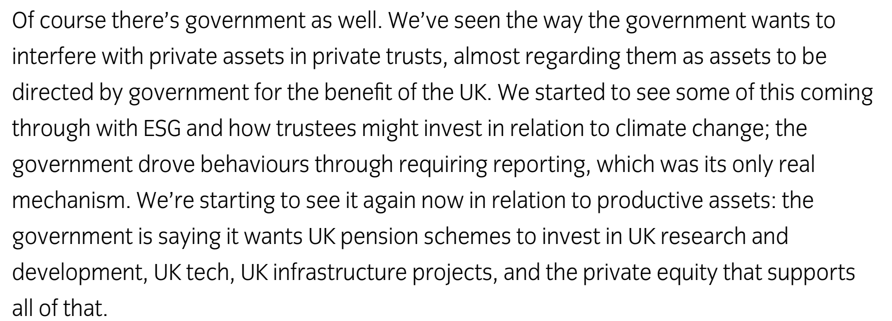
Where I've seen some of the healthiest discussions take place, particularly over the last 12 to 18 months around trustee board meeting tables, is when people decide to think about the assumption, that has perhaps come from their advisers over the years, that buy-out is what they are aiming for and they must do – that if they don't, they're in some way exposed; and what are the relative disadvantages?

Questions might include:

- What are the relative disadvantages of transacting with an insurer?
- What are the potential exposures if we do run on and the funding position deteriorates?
- What are the protections that might be available?
- How strong is our sponsor covenant?
- What does the new funding regime look like for us in terms of the low-dependency investment allocation?
- What might we start doing with surplus above a low-dependency allocation, that could bring more benefits to members and the sponsor?

The consultations that are ongoing currently really reinforce that message of it being worthwhile – I would say necessary – to step back and think about what we are doing here: what's our long-term funding target and strategy, and let's challenge some of those assumptions.

Trustees are ideally placed to do all of this given the number of vested interests. Sponsors may want a particular outcome, which is completely understandable given they've funded the benefits over the course of a scheme's life, and they will be on the hook if schemes run on. Then there are more remote connections like advisers who may have their own products or in-house thinking to bring to the table, which may not be 100% impartial or independent. I appreciate that's a fairly controversial statement. I do see this sometimes sitting back and observing discussions though.



Of course there's government as well. We've seen the way the government wants to interfere with private assets in private trusts, almost regarding them as assets to be directed by government for the benefit of the UK. We started to see some of this coming through with ESG and how trustees might invest in relation to climate change; the government drove behaviours through requiring reporting, which was its only real mechanism. We're starting to see it again now in relation to productive assets: the government is saying it wants UK pension schemes to invest in UK research and development, UK tech, UK infrastructure projects, and the private equity that supports all of that.

Trustees are there to say that's just noise for us. We focus on our scheme, our obligations and our sponsor, and we insulate ourselves somewhat from all of that and take the right view. That's how I would see it currently in place and working as trustees and sponsors deal with some of these things.

**Where I've seen some of the healthiest discussions take place…is when people decide to think about the assumption, that has perhaps come from their advisers over the years, that buy-out is what they are aiming for and they must do.**

SIMON DANIEL, EVERSHEDS SUTHERLAND

# QUESTIONS AND ANSWERS

## FIDUCIARY DUTY AND THE PROPOSED 100% PPF UNDERPIN

**Webb:** If the government goes ahead with the option of 100% PPF protection, if a trustee assumes that is in place, to what extent is their fiduciary duty to run on in order to pursue surplus growth for the benefit of their members?

**Daniel:** I think that somewhat interferes with the way in which fiduciary duty has traditionally been understood and also interpreted in light of the existence of the PPF. A case was decided in the High Court a few years ago that deployed the principle that trustees ought not to game the PPF – trustees need to run their scheme and make decisions about their scheme without taking risks which they wouldn't take if the PPF weren't there.

The question is about the same thing, manifesting itself through the 100% PPF cover option. The difference is that with the 100% underpin schemes would pay a super levy, and we can have a discussion about the level of that and whether that really works; but there would actually be a payment of an enhanced levy in exchange for having that protection.

Explicitly, the government is saying that's to enable schemes to run on, but we're also to start releasing surplus. I think that fundamentally changes the way in which fiduciary duty has always operated: you're then taking on an assumed responsibility to achieve that strategy of investing for more surplus to potentially benefit the sponsor and members, because the levy's been paid.

It really is quite fundamental for our UK pension system, and I'm not sure that's really been considered yet by the government.

**Webb:** I would encourage all respondents to the consultation to submit a one-page summary of their views.

It really is quite fundamental for our UK pension system, and I'm not sure that's really been considered yet by the government.

SIMON DANIEL, EVERSHEDS SUTHERLAND

## SPONSOR DEMAND FOR RUN-ON AND ATTITUDES TO RISK

**Webb:** Why should a sponsor want to run on and retain the risk of a DB scheme? How does investing in more UK equities lead to greater security for member benefits? Why should trustees increase risk in the hope of generating UK growth? How does that sit with fiduciary duty?

**Kitson:** It's important to understand what run on is. Part of the challenge is we're all still thinking through it, but I don't think it is about equities. I think there's a misconception that run-on is about re risking. I think of it as about 'right risking'.

On a buy-out, what is your insurer doing? Your insurer isn't investing at gilts plus 50bp or gilts flat. They're looking at the cashflows of the benefits promised, and they're building a low-risk investment portfolio around it and generating a surplus from that. It's that same mindset for run-on.

Of course that raises a question: do insurers have access to assets that pension schemes don't? But that can be dealt with via consolidation in other ways: asset managers for example. But I think run-on is that sort of strategy.

It's not suddenly going back to a "let's invest in equities and take more risk" attitude – that requires a different mindset. It's not about VAR anymore; it's more about investing in things like high quality credit, it's more about reinvestment risk, it's more about default risk. We need a different risk mindset to make sure we're properly thinking about these.

> I think there's a misconception that run-on is about re-risking. I think of it as about 'right risking'.
>
> PAUL KITSON, EY

Again, similar to an insurer would in the buyout model, and dare I say, there's a change in the way we think about the discount rates. I think this obsession we've had in the UK of 'gilts plus' being the measure that we mark all of the liabilities by doesn't work in this run-on world. Like an insurer, we need to think about how we set the discount rate properly holistically, properly dynamically, recognising the risks that are actually there, like default and credit downgrade risks, but not the risks that aren't, like temporary mark-to-market risks.

To the point of the question – why would the CFO do this; how would they get comfortable that they are not going to be funding volatility – it needs to be stable in the run-on process. That's the only way we can safely distribute surplus. If it isn't stable, it doesn't work.

## CLARITY ON FIDUCIARY DUTY

**Webb:** On fiduciary duty, what is the scope for it to change from just paying pensions to building surplus? Can the government do this?

**Daniel:** In terms of legal principle, the government can do anything if it passes an Act of Parliament. We can all say what we think fiduciary duty ought to require, but that's a common law concept which comes from the law of equity. The government could legislate and declare what fiduciary duty means, and then trustees would at least have clarity as to how it is to be interpreted.

I think fiduciary duty has held up pretty well in how it's been applied to issues of sustainability and climate change; there have been some variances in how it's been interpreted, but I think most people coalesce around a similar view these days.

I think it's possible that people could get to the right interpretation of what fiduciary duty would mean in that world without legislation, but I think it would be helpful if the world was going to change in a very fundamental way for the government to tell trustees, if you pay a super levy from your scheme in order to gain a 100% underpin, then your fiduciary duties are altered – because you are then explicitly taking on an objective to fund for surplus and then distribute it. That is a very different thing.

## HOW EQUITY ANALYSTS VIEW DB SCHEMES AND THEIR IMPACT ON COMPANY BALANCE SHEETS

**Webb:** Do equity analysts care about what's going on with a company's DB scheme?

**Kitson:** A number of CFOs tell me, and this seems mind boggling in the current world, given our understanding about pensions, their analysts look at the surplus in their UK DB fund and deduct it from their German unfunded liabilities. So a buy-out would actually destroy value in the way that analysts think about it. Despite there being no mechanism today for getting the surplus in the UK plan (that's there on an accounting basis) into the German plan, they are effectively getting credit for that in the analysts' model. There are multiple cases like that.

It seems that running on would support the way analysts are currently looking at business in a positive way. It seems that, at the moment, they see run on as a benefit in a number of cases.

**Webb:** We've had a few annual reports where the accounts have shown an unexpected boost from the DB scheme, and the share price has gone up. So people are starting to see the connection, and these are quite big numbers sometimes, relative to the size of the sponsor company.

**Kitson:** Yes, and there's a quirk of accounting that if you have a certain set of trustee rules and you are paying deficit contributions, those are added to the balance sheet as a debt. So even if you have a surplus on any measure, you present-value those contributions; so as soon as you turn those contributions off, that disappears. So there are some interesting accounting implications for some of the changes that are coming.

## THE LIKELY FUTURE FOR DB SCHEMES

**Webb:** There are questions which focus on our central expectation for the future of DB schemes. Will a meaningful proportion of schemes realistically run on, or are they all going to insure or consolidate?

Part of my answer to that would be that it depends on when you are talking about. I don't think we are necessarily talking about running on until the last pension is paid; but I think we are talking about, let's say, a 10-year horizon – certainly, running on into the medium term. It is striking that on looking at The Pensions Regulator (TPR) surveys of the largest schemes, you might expect them all to have a journey plan towards buy-out, but that's not the case.

Insight's recent piece, Time is your friend[2], is very clear. We are in a time of real flux. The opportunity set in front of trustees and corporates is changing for market reasons, but could also change for legislative and regulatory reasons. So is there a rush to make a final and irreversible decision?

Then there is the mere fact that as a scheme matures and more people become pensioners, you're potentially going to get better prices anyway. So you can see the argument for taking your time thinking about this, and then potentially taking advantage of a new regime.

We are in a time of real flux. The opportunity set in front of trustees and corporates is changing for market reasons, but could also change for legislative and regulatory reasons. So is there a rush to make a final and irreversible decision?

SIR STEVE WEBB, LCP

[2] Time is your friend: the case for delaying bulk purchase annuity transactions, 13 March 2024, Insight.

## PRACTICAL STEPS FOR EXPLOITING A SURPLUS

**Webb:** If I wanted to exploit my surplus starting tomorrow, what are the practical steps I need to take?

**Daniel:** I would say that the new funding and investment regime creates a reasonably helpful framework for this, subject to one caveat: it's interfered with by the government in the new consultation on DB options in a slightly unhelpful way.

If you are a significantly mature scheme, the regime will say your low-dependency investment allocation does not need to address the surplus of funding that you might have above your low-dependency funding basis. In other words, if you're 100% funded on your low-dependency funding basis, then the requirements around low-dependency investment just apply to that 100%, which means that part of your scheme's assets needs to be highly resilient to short-term adverse changes in market movements. But the excess can be invested in a different way, which potentially would seek to achieve higher returns, or potentially would get invested in a less liquid set of asset opportunities.

The government says that if you have a surplus, we would like you to start thinking about whether you can distribute that to members and employers; we may give you a statutory override in case you have scheme rules which don't allow you to do that, because you didn't pass what was called a section 251 resolution, which preserves your ability to distribute surplus from an ongoing scheme.

However, coming back to the caveat, the government also says it would like schemes who are doing this to invest in productive assets which are typically less liquid.

So on the one hand we're creating a funding regime which allows surplus to be released in this way periodically, perhaps at each valuation or even on an annual basis; but then the government says what we really want you to do is put them in productive assets. To me, that's inconsistent, and trustees have the freedom to ignore that.

**Kitson:** There are two different avenues here. In terms of practically what can you do now with a surplus, the obvious thing is to fund DC contributions. Even if the DC scheme is outside of the DB scheme, in a master trust for example, there are ways of getting the surplus there to fund DC contributions.

Most of the discussions we are having about surplus usage now is around use for DC; it's a bit early to be thinking about where else you might do it in terms of member benefit improvements or return to sponsors. Other things people are doing include removing the cost of service provision back to the scheme, rather than the employer paying.

But I suppose the other thing is that there's an obvious off ramp now to buy out. Some of the conversations we're having are less about do we buy out or run on, and more about whether to keep going and see what those avenues are in the future. That's the point that's already been made that, all else being equal, buy-out is going to get better. There's still such a pricing differential for deferred versus pensioner members, and by duration. The shorter the duration gets, and the more people move from deferred to pension status, the better the buy-out pricing gets.

Of course, buy-out pricing can move – it depends how you are investing. But there is a sense that all else being equal, there's a benefit from driving down that road.

## MOTIVATIONS FOR TRUSTEES

**Webb:** What makes anyone think that trustees risk liability by running on when they could have executed an insurance transaction?

**Daniel:** There is obviously a strong reason why you would seriously consider going to buy-out if you can afford to and the sponsor wants you to. That's what most schemes do.

What you do forgo if you buy out is the ability subsequently to award discretionary pension increases, and to give those more idiosyncratic benefits, which insurers say they can't give.

SIMON DANIEL, EVERSHEDS SUTHERLAND

But I've seen a lot of schemes in the last 12 months being surprised to find themselves fully funded on a buy-out basis. It's almost accidental. The markets have meant they suddenly found themselves in that position, and they're scrambling because they're thinking they need to suddenly transact because their funding position might fall back and the opportunity is lost.

I think for those situations, you're rushing around trying to do the benefit specification, to clean the data, to approach the market to say we have good governance and we're ready to transact. To me that feels panicked. It can work, with the right support and decision-making frameworks, but I think it is best avoided.

Once you are there and ready to go, you have to be prepared for compromises that have to be made. I've done dozens of transactions in the course of my 20 years in pensions and in every single one of those there has been at least one compromise which has required the trustees to consider whether they are happy to proceed. Normally they decide that in the round, everyone benefits, so they're comfortable to proceed.

But there is always a compromise to be made: whether it's just codifying discretions in the way the insurer wishes to, or giving up some of the more idiosyncratic benefits that the scheme provides for, or the way in which certain contractual terms work where you're transacting at a particular point in time and actually the market would be more favourable to you later on.

Going back 10 years or so, schemes used to get collateral from insurers for big buy-ins. That doesn't happen these days. So there is a degree of credit exposure to insurers in buy-in. Some may feel agnostic about that and have good reason for it. But there are things there which may make you think again. People also have a reluctance to effectively give insurers profits from their scheme, which sponsors may have a view on. So I think all of that needs to be considered.

What you do forgo if you buy out is the ability subsequently to award discretionary pension increases, and to give those more idiosyncratic benefits, which insurers say they can't give.

## OTHER APPROACHES TO PENSIONS

**Webb:** If DB is too volatile and personal DC doesn't lead to good outcomes, what about collective DC?

**Daniel:** It has merits. I think it's been inevitable and obvious to all of us that DC is a slow-motion car crash for one or two generations. It's going to be hard when they get to the point of needing to take benefits.

That's given rise to the expectation that it will come back to some degree towards something that looks a bit more like DB. Collective DC has worked in the Netherlands, and has some principles about sharing longevity and investment risk, which seem to be advantageous, but it's not really gathered much government support. We've done it for Royal Mail and there's legislation coming to make it available for a multi-employer situation. I think employers will be interested – it's just whether those structures are available and whether there is the appetite to do something more than what's currently being done.

**Webb:** How about reopening DB? Is that on the table?

**Kitson:** The pendulum is swinging with CFOs certainly thinking about the alternatives to buy-out. I think it's too early to say that will manifest itself in reopening DB. But the question is even bigger: we have to rethink retirement in the UK more generally, as well as about how we provide pensions and where the risk sits.

We've got a big challenge coming with long-term care costs. For example, one of the unfortunate side effects of us getting so good at extending life is people now living to ages far more commonly where issues like dementia are prevalent. The cost is huge. So we need to rethink this whole conundrum of what retirement is for people, and how we build a pension system that supports that.

DC is a slow-motion car crash for one or two generations…That's given rise to the expectation that it will come back to some degree towards something that looks a bit more like DB.

SIMON DANIEL, EVERSHEDS SUTHERLAND

## IMPLICATIONS FOR SPONSORS WITH MULTIPLE PENSION SCHEMES

**Webb:** For sponsors with multiple pension schemes of differing funding levels, does surplus extraction open the door to multiple mergers of pension schemes to share the surplus? For example, you have a scheme that could buy out and another in deficit – could you hold off buying out the former and cover both of them?

**Kitson:** We are definitely seeing a lot of activity from corporates with lots of plans in different places. There is a lot of discussion around ways of utilising surplus within our pension group more broadly.

## CONCLUDING THOUGHTS

**Webb:** For those still questioning whether any alternative to buy-out is realistic – is it possible to overcome the muscle memory driving them to that conclusion?

**Daniel:** The key point for me, looking at everything that's currently in flux and where things might be going, is for trustees to realise they are in a prime position to make the right decisions. They have the ability to take the advice they require and to block out some of the noise, with input from different people if they think they need a diversity of views to challenge some of the assumptions and vested interests that are out there.

I think trustees should feel this needs to be done in order to set the right strategy, notwithstanding fluctuating funding levels and policies, to do the right thing for members and sponsors given the framework they are operating in and what they ultimately want to achieve.

**Kitson:** This is a very luxurious problem we have here. Do you buy out now and give members full security, or find security another way? It's a great choice to have. There are so many competing ideas and innovations coming.

The other point is that even if we have 11 or 12 UK insurers/bulk purchase annuity writers in the not-too-distant future, we are not going to find all the schemes buying our any time soon anyway. It won't fundamentally change capacity.

So in one shape or form, run on in a temporary sense, is here to stay.

**Webb:** A concluding thought from me would be, having seen all of this from inside government, you really can't make decisions on feedback you don't get. The government is not going to create opportunities if you don't tell it that's what you want, even if you just answer one question or respond and say "I would value this option on my suite of options".

I hope everyone will engage with this consultation before the deadline on 19 April. Hopefully, we can then have time to explore all the options across a whole suite of new things pension schemes can do.

.

# PANEL PARTICIPANTS

### Sir Steve Webb
### Partner, LCP

Sir Steve Webb's first role was as a micro-economist with the Institute for Fiscal Studies for nine years, followed by two years teaching social policy at Bath University. He was unexpectedly elected to Parliament in 1997, and served for 18 years, the last five of which he was Pensions Minister.

During his time at the Department of Work and Pensions (DWP) Steve oversaw the successful implementation of automatic enrolment, helped design and legislate for the new state pension and played a key role in the 'pension freedoms' introduced in 2015. Since leaving politics he worked for four years for the mutual insurer Royal London commenting on all matters relating to pensions and in 2020 joined LCP as a partner, advising and commenting on a wide range of DB and defined contribution (DC) pensions issues and speaking at a variety of events.

### Paul Kitson
### Actuary and UK Head of Pensions Consulting at EY

Paul Kitson leads a multi-disciplinary pensions advisory team of actuaries, investment consultants, data scientists and governance experts. Paul has led several market leading de-risking transactions, including a £1.2bn synthetic buy-in for British Airways Pension schemes, later executing a longevity swap for another of British Airways Pension schemes, before novating this to a £3.5bn buy-in with L&G. Paul is a frequent speaking on pensions and retirement globally, having led plenary sessions at retirement conferences in US, Taiwan, Canada, South Africa, and throughout Europe and the UK. Last year, Paul was instrumental in the work by the City of London Corporation leading to the Mansion House DC Compact which is encouraging more investment by UK pension plans into unlisted equity and associated asset classes, delivering better outcomes for members and increased benefit for the UK economy. Paul is currently leading on a number of initiatives to support UK pension plans to safely run-on, leading to enhanced member benefits, maintaining benefit security and enabling surplus return to sponsors to support increased DC pension provision. Paul is a specialist in longevity risk and has acted as an Actuarial Expert Witness in several court cases and regulatory action.

### Simon Daniel
### Partner in the Pension Practice at Eversheds Sutherland

Simon Daniel helps pension scheme trustees, sponsors and providers achieve successful outcomes in asset investment and insurance risk settlement. Simon focuses on supporting pension scheme trustees, Local Government Pension Scheme (LGPS) funds and other institutional investors with the investment of their assets and helping trustees, sponsors and insurers successfully execute insurance risk settlement transactions.

In the risk settlement area, Simon has advised on longevity-hedging structures and bulk annuity transactions of all sizes and types. This includes a £3bn residual risk transaction, a collateralised pensioner buy-in for £1.8bn, a non-collateralised pensioner buy-in for £900m, and an £800m longevity pass-through arrangement. It also includes numerous full buy-outs for sub-£100m schemes (including a PPF+ buy-out for just £2.5m). Simon is a lead Partner for Pathway, Eversheds Sutherland's joint proposition for streamlined bulk annuity transactions with Aon which has been used in transactions for aggregate premiums exceeding £1bn.

Simon's focus on asset investment includes supporting trustees and LGPS funds with investment reviews of all types (from advice on investment-linked life policies and authorised pooled funds to legal and tax due diligence reports on unauthorised alternative investment funds structured as non-UK limited partnerships). It also involves reviewing discretionary investment management and fiduciary management agreements. A key feature of Simon's investment work is supporting schemes with their increasing investment governance obligations, including their policies, practices and disclosures in relation to environmental, social and governance (ESG) factors and stewardship.

## FIND OUT MORE


**Institutional Business Development**
businessdevelopment@insightinvestment.com

**European Business Development**
europe@insightinvestment.com

**Consultant Relationship Management**
consultantrelations@insightinvestment.com

**company/insight-investment**

**www.insightinvestment.com**



This document is a financial promotion/marketing communication and is not investment advice.

This document is not a contractually binding document and must not be used for the purpose of an offer or solicitation in any jurisdiction or in any circumstances in which such offer or solicitation is unlawful or otherwise not permitted. This document should not be duplicated, amended or forwarded to a third party without consent from Insight Investment.

Insight does not provide tax or legal advice to its clients and all investors are strongly urged to seek professional advice regarding any potential strategy or investment.

For a full list of applicable risks, investor rights, KIID/KID risk profile, financial and non-financial investment terms and before investing, where applicable, investors should refer to the Prospectus, other offering documents, and the KIID/KID which is available in English and an official language of the jurisdictions in which the fund(s) are registered for public sale. Do not base any final investment decision on this communication alone. Please go to www.insightinvestment.com

Unless otherwise stated, the source of information and any views and opinions are those of Insight Investment.

Telephone conversations may be recorded in accordance with applicable laws.

**For clients and prospects of Insight Investment Management (Global) Limited:** Issued by Insight Investment Management (Global) Limited. Registered office 160 Queen Victoria Street, London EC4V 4LA. Registered in England and Wales. Registered number 00827982. Authorised and regulated by the Financial Conduct Authority. FCA Firm reference number 119308.

**For clients and prospects of Insight Investment Management (Europe) Limited:** Issued by Insight Investment Management (Europe) Limited. Registered office Riverside Two, 43-49 Sir John Rogerson's Quay, Dublin, D02 KV60. Registered in Ireland. Registered number 581405. Insight Investment Management (Europe) Limited is regulated by the Central Bank of Ireland. CBI reference number C154503.

© 2024 Insight Investment. All rights reserved.


16026-04-23