PENSIONS AND
LIFETIME SAVINGS
ASSOCIATION

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DB
TASKFORCE
OPPORTUNITIES FOR CHANGE

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The Pensions and Lifetime Savings Association is the national association with a ninety year history of helping pension professionals run better pension schemes. With the support of over 1,300 pension schemes with over 20 million members and £1tn in assets, and over 400 supporting businesses. They make us the leading voice for pensions and lifetime savings in Westminster, Whitehall and Brussels.

Our purpose is simple: to help everyone achieve a better income in retirement.

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CHAIR'S FOREWORD

FIFTY YEARS AGO, MORE THAN 12 MILLION WORKERS WERE BUILDING UP A FINAL SALARY PENSION[1]. PENSION SCHEMES OPERATED ON A BEST ENDEAVOURS BASIS IN AN ENVIRONMENT WHERE HIGH INTEREST RATES AND GOOD STOCK MARKET RETURNS WERE THE NORM. LIFE EXPECTANCY FOR A 65-YEAR-OLD MAN WAS 12 YEARS. IT WAS STRAIGHTFORWARD FOR FIRMS TO PROVIDE FOR THEIR EMPLOYEES' RETIREMENT.

Today, the system in which defined benefit (DB) schemes operate is very different. Economic, cultural and demographic shifts over recent decades pose significant challenges to the ability of schemes to meet their funding commitments to what are, largely, former employees. The average 65-year-old now lives for another 18 years – an increase of 50% in 50 years. Regulation has, in pursuit of members' interests, hardened the benefit promise. Combine this with persistently low interest rates and lower investment returns, and the result is a situation where the aggregate DB deficit has been over £400 billion[2] for the last ten years.

Employers are a key part of the solution to this gap, and the system depends on the strength of their covenants to eliminate scheme deficits over many years. But not all employers will be strong enough. Covenant risk is the great unknown in our current regulatory framework and the scale of that risk is material. Many existing DB schemes were established in traditional industries like manufacturing and bricks-and-mortar retailing. Trends such as globalisation, increasing digitalisation and the risks arising from Brexit and wider political uncertainty are impacting, and will continue to impact, all UK employers. Many firms will adapt successfully but not all will be able to do so.

As a result, millions of people's retirement incomes are now at risk with approximately 3 million people in DB schemes having only a 50% chance of seeing their benefits paid in full[2], despite the fact that employers are paying out billions each year in deficit recovery contributions (DRCs). Indeed, for some employers the cost and uncertainty of these DRCs will further jeopardise their future, diverting money away from crucial investment in developing their businesses and improving the productivity of their workforce.

This is why the PLSA set up its DB Taskforce nearly 18 months ago, working with people from across the DB sector – including employers, trustees, scheme advisers and others – to explore the many and varied challenges facing DB schemes, the impact of these issues on member benefits, and to propose a broad set of possible solutions.

It is clear to the Taskforce that reforms are essential to sustain confidence in the DB pension system. In this, our final report, we explore some potential new options for trustees and sponsors of the nation's 6,000 DB schemes. Each of these schemes is different and faces different challenges. We hope that the suggested options set out in this report will help stimulate further thinking on how to tackle those diverse challenges successfully.

I am grateful to all the members of the DB Taskforce for their insight, time and commitment, as well as to the PLSA for co-ordinating this piece of work. I would also like to thank the Department for Work and Pensions (DWP), the Pension Protection Fund (PPF), The Pensions Regulator (TPR) and many others in government, regulatory bodies and the pensions industry who have taken the time to engage with us throughout this process. I welcome the fact that much of the Taskforce's research has been reflected in recent policymaker reports.

Time is running out for a solution to the challenges DB schemes face, and it is more vital than ever that industry and policymakers work together to protect the millions of people whose retirement savings are at risk.

ASHOK GUPTA

1 Occupational Pension Schemes survey, ONS.
2 DB Taskforce *Interim Report,* TPR data, and PPF Purple Book.

EXECUTIVE SUMMARY

AS OUR SOCIETY HAS CHANGED, SO TOO HAS THE BASIS ON WHICH DB PENSIONS WERE DESIGNED, ESTABLISHED AND PROMISED. A NEW ECONOMIC AND REGULATORY REALITY HAS BROUGHT CHALLENGES TO A SYSTEM ON WHICH MILLIONS OF PEOPLE RELY FOR THEIR SECURITY AND COMFORT IN OLD AGE. THERE IS A GROWING CONSENSUS AMONG POLICYMAKERS, REGULATORS, INDUSTRY AND OTHERS THAT THE INTERRELATED PROBLEMS WITH FUNDING, GOVERNANCE, EFFICIENCY, COVENANT AND SCALE CAN NO LONGER BE IGNORED.

While most schemes and employers will successfully adapt to these changes, many others face a harsher reality. In our final report we have focused on the key issues of underfunding, covenant risk and lack of scale. Addressing these underlying issues would also have an impact on efficiency and governance.

UNDERFUNDING

Much of the UK's DB system is underfunded. Of the UK's 6,000 schemes, with 11 million members, just over 4,000 are in deficit[3]. These deficits are getting worse and have been at a level of over £400 billion on a buy-out basis over the last 10 years[4]. In an environment where it is becoming increasingly hard to get the necessary returns on investment, and where employer contributions often seem to be making little impact[5], this does not seem to be a problem that will resolve itself without help.

COVENANT RISK

Employer covenants are the solution to underfunding, and it is likely that most schemes in deficit should eventually reach a sustainable funding position by drawing on the financial strength of their sponsoring employer. But some will not. Employer covenants are under pressure, often severe pressure. The kinds of sectors which were thriving when DB schemes were established and where current DB liabilities are disproportionately concentrated, such as manufacturing[6], have often struggled to deal with the new world order. Even for those employers currently maintaining deficit recovery payments, it is impossible to be certain that future developments – social, technological and economic – will not be detrimental to their ability to do business.

SCALE

These problems are exacerbated by the fact that most schemes in the UK lack the scale needed to fix the situation themselves. The majority of the UK's schemes are small: two-thirds have fewer than 1,000 members, while the average scheme has just over 1,800 members and £200 million of assets.

Whilst scale by itself is not a determinant of success, the greater the amount of assets under management, usually, the better able trustees are to both access sophisticated investment skills and negotiate lower fees along a highly intermediated investment chain. Access to resource and expertise is also a critical factor in good scheme governance.

With some schemes facing one or more challenges, there is no one-size-fits-all solution. Scheme trustees will need to assess their situation in terms of these challenges and make a considered decision. In our report we have sought to investigate a range of potential options that could help different schemes improve their performance and improve the probability of members seeing their benefits paid in full. Our recommendations include a template for a new Chair's statement for DB scheme trustees, to create an impetus for good governance, cost transparency and a culture of considering consolidation. We also set out the potential efficiencies and improvements in communication that benefit simplification could provide.

In addition, we explore what action trustees might take for underfunded schemes with secure covenants, i.e. those covenants classified by the

3 PPF 7800 index update.
4 The Purple Book – DB Pensions Universe risk profile 2016.
5 As identified in earlier DB Taskforce reports, and reiterated recently in LCP's report, Accounting for Pensions 2017, which highlighted the £625bn level of liabilities on an IAS19 basis.
6 In the calculation of the PPF Levy, the manufacturing sector is reported to have the highest insolvency probability of any industry, Purple Book, 2015.

regulator as 'strong' or 'tending to strong'. In these cases, the consolidation of assets, services and governance can often result in better value for money and improved governance, while the employer covenant remains intact.

We believe it is those underfunded schemes whose trustees believe their employer's covenant to be under pressure – those in the 'weak' and 'tending to weak' groups – which most urgently need help. When facing the dual problem of both underfunding and a covenant at risk, trustees need to reconsider the value of their employer covenant. We suggest that if an alternative was available, exchanging the covenant for a more secure arrangement could be an appropriate alternative option for these struggling schemes.

This report presents an outline as to how to potentially turn the covenant – essentially an unknown and intangible arrangement – into a cash payment, as well as into stronger and more secure scheme backing from a larger sponsor. We think that doing so could require the provision of consolidation vehicles, 'Superfunds' which would consolidate the assets and liabilities of entering schemes.

Here we present some further thinking about what a Superfund might look like; we believe that this might be a useful additional option for some schemes to consider when thinking of possible ways forward.

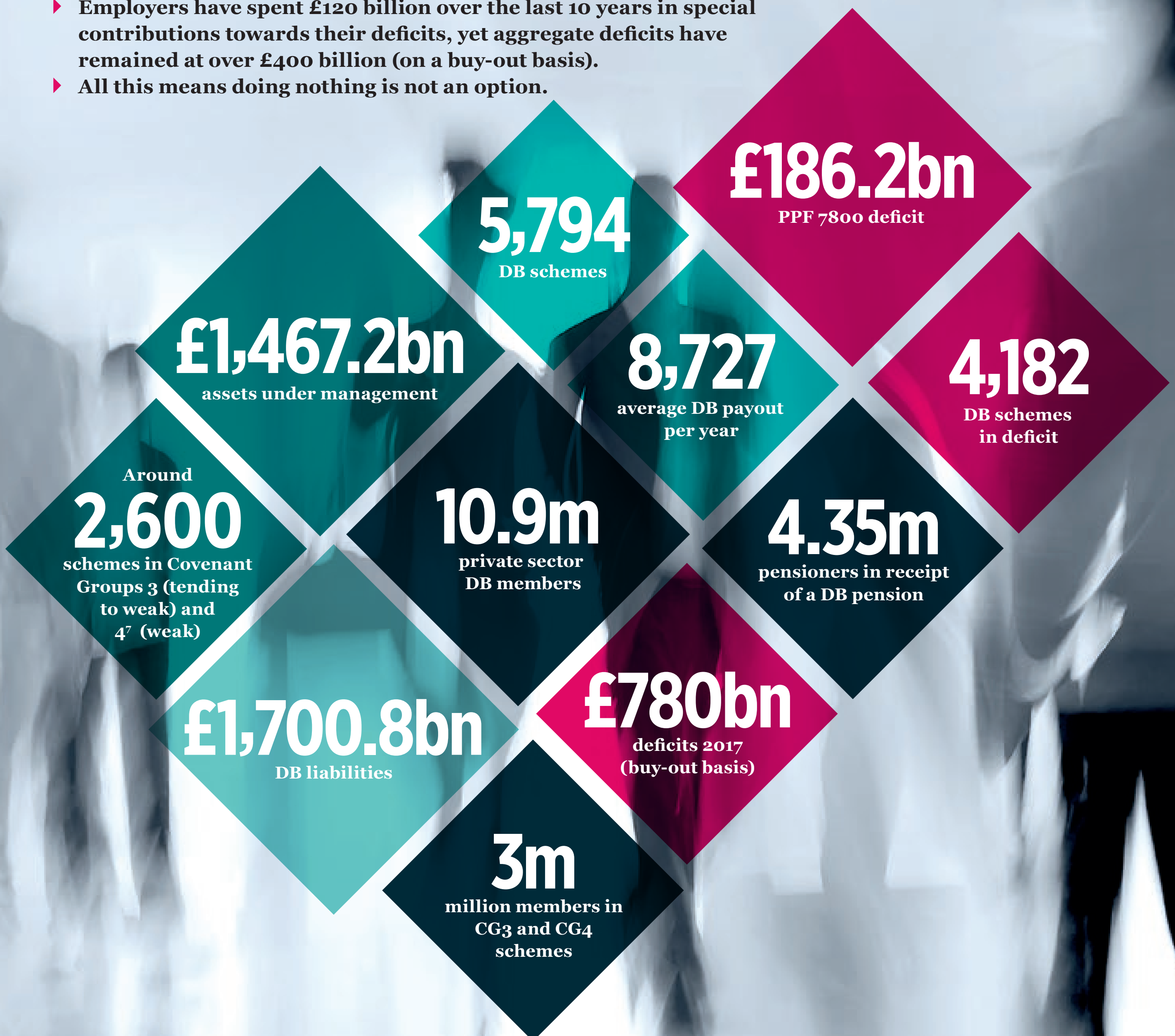
Transferring to a Superfund could allow employers to concentrate on securing the future of their business, provide trustees with another way of securing member benefits, and ensure members gain from the greater likelihood of their benefits being paid in full. Our modelling and analysis provisionally indicates that Superfunds:

- Could pay members the full value of their benefits in more than 90% of scenarios, which has the potential to improve outcomes for more than 3 million members;
- Could cost employers significantly less than buy-out, with 39% of employers surveyed already keen to consider Superfund entry; and
- Could free up employer resources for investment in their businesses. Of those who knew what they would invest in, 49% of employers said they would invest the money freed up directly in their employees, for instance through contributions to the DC pension scheme or wage growth; while 28% would invest in business growth, e.g. new equipment or company infrastructure.

The government and regulatory bodies have already taken several welcome steps to analyse and unravel the problems facing UK DB schemes. This report – and the work of the Taskforce more generally – is intended to refocus the DB debate on member outcomes and stimulate new thinking. **We welcome discussion and challenge from both industry and policymakers; this is a necessary part of designing and delivering practical long-term solutions to protect the hard-earned retirement savings of millions of people**.

UNDER PRESSURE – DB TODAY

- DB matters to millions of people who rely on DB benefits to support them in retirement.
- DB also matters to the UK economy – £1.5 trillion is invested in DB schemes, supporting all parts of the economy.
- The current system is fragmented, with schemes attempting to de-risk and requiring ever-increasing amounts of capital from corporate sponsors.
- Not only are DB scheme problems being made worse by the current economic climate, they are also contributing to economic weakness.
- Employer covenants are under pressure – the ability of FTSE 350 companies to fulfil their DB pension obligations has sunk to its lowest level since the recession.
- There are risks and costs in the system that place strain on scheme sponsors and the economy – but they also have an impact on scheme members and future generations of pensioners.
- Employers have spent £120 billion over the last 10 years in special contributions towards their deficits, yet aggregate deficits have remained at over £400 billion (on a buy-out basis).
- All this means doing nothing is not an option.



7 A PLSA estimation using TPR data on Tranches 8,9 and 10 – a close approximation of the DB universe.

THE DB TASKFORCE INTERIM REPORT IDENTIFIED FOUR AREAS THAT POLICYMAKERS SHOULD GIVE IMMEDIATE FOCUS TO ADDRESS THE CHALLENGES FACED BY DB SCHEMES TODAY, AND UNDERTOOK TO DEVELOP RECOMMENDATIONS TO TACKLE EACH OF THEM.

THE SYSTEM IS TOO FRAGMENTED

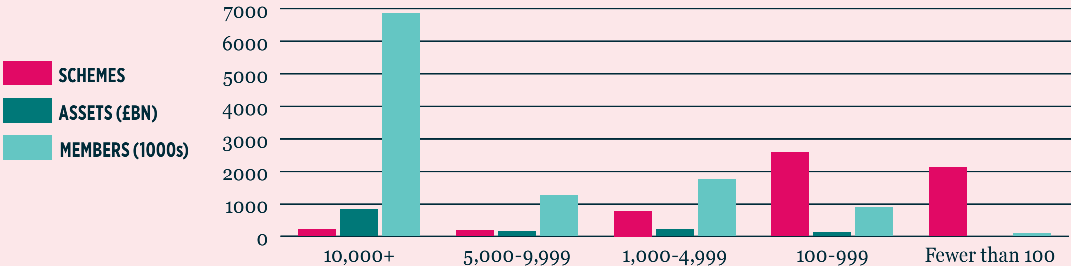
THE SYSTEM IS TOO FRAGMENTED

The Taskforce highlighted that there are too many small, sub-scale schemes. In an environment that is far more complex than the one in which those schemes were first created, the cost of provision more expensive, and economic conditions less benign, the proliferation of small schemes creates problems for sponsors, trustees and regulators.

Smaller schemes are generally characterised by poorer governance standards than their larger counterparts. They also struggle to leverage economies of scale and attract the quality of skills needed to operate and invest efficiently. They can also find it harder to navigate the highly intermediated nature of the UK pensions system. All this results in significant value leakage.

We recommended that work is undertaken to investigate the potential for scheme consolidation.

NUMBER OF MEMBERS, SCHEMES AND ASSETS UNDER MANAGEMENT BY SIZE OF SCHEME



SCHEME RESOLUTION IS INFLEXIBLE

SCHEME RESOLUTION IS INFLEXIBLE

The Taskforce highlighted that the current system only allows binary outcomes of complete 'success' or complete 'failure' whereby a scheme can either be:

- Supported by a solvent employer and funded (or funding to provide full benefits); or
- Unsupported by a solvent employer, and transferred to the PPF with members receiving compensation which in aggregate replaces around 80% of the value of their scheme benefits.

We recommended that greater regulatory flexibility may help to achieve earlier scheme resolution and could mean that funding issues could be addressed before failure (of the scheme or sponsor) became inevitable, with better outcomes for scheme members.

APPROACH TO BENEFIT CHANGE IS TOO RIGID

What started for many employers as a benefit offered on a 'best endeavours' basis has now become a hard-wired promise.

This, combined with improving longevity, has added significantly to the cost of providing pensions. As a consequence, sponsors in the UK do not have the 'pressure valves' available to sponsors of DB schemes in other developed economies. Greater benefit flexibility – such as that available to the PPF itself – may help to avoid or address problems.

We identified that work should be undertaken to investigate how a more flexible approach to benefit design/change could be implemented to help sustain schemes.

RISK BEARING IS SUB-OPTIMAL

Taskforce analysis showed that the continued trend towards de-risking investment strategies is placing greater emphasis on making good deficits through contributions, with, consequently, a greater reliance on the sponsor's solvency. This effectively exchanges investment risk for solvency risk – on aggregate moving risk around the system rather than removing it.

We recommended that work should be undertaken to build a greater focus on risk to member benefits.

DB ISSUES: AN OVERVIEW

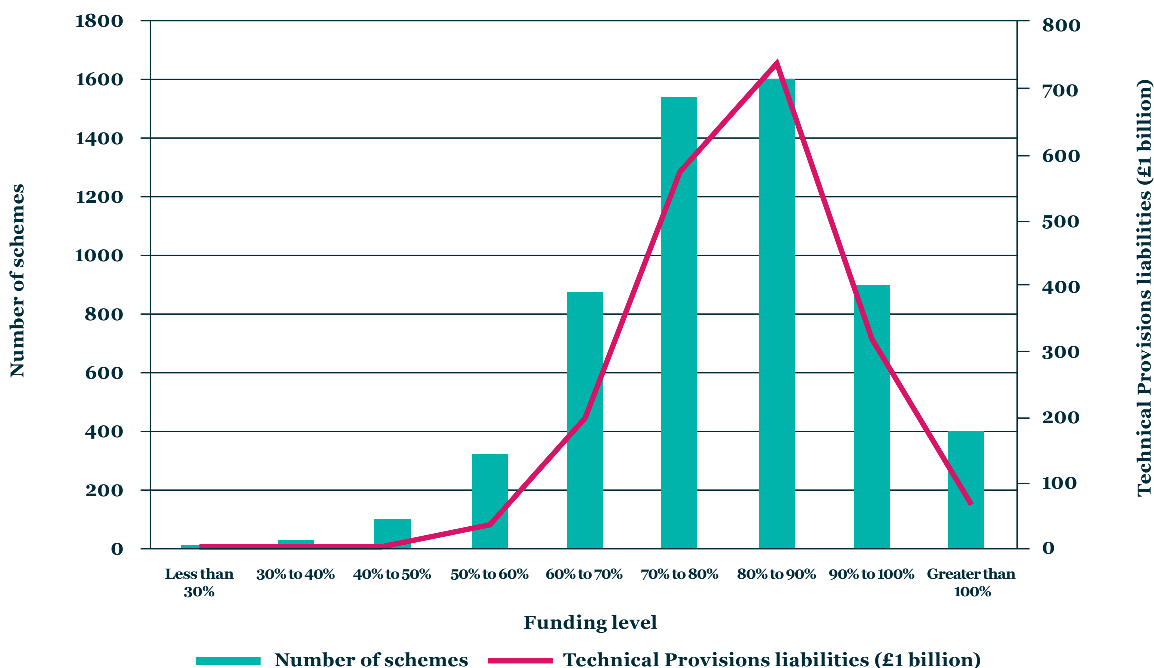
THE DB TASKFORCE'S FIRST TWO REPORTS ANALYSED THE NATURE AND EXTENT OF THE CHALLENGES FACING DB SCHEMES, THEIR MEMBERS AND SPONSORING EMPLOYERS. THESE ISSUES ARE STILL PREVALENT TODAY.

THE SCALE OF UNDERFUNDING

DB schemes provide, now or in the future, pensions to 11 million people[8] who will rely on these payments to support them in retirement, and have assets under management of £1.5 trillion in the UK[9]. Yet despite the collective size and importance of these funds, DB pension schemes are under pressure as liabilities have grown faster than assets over the last 10 years. At the end of August 2017, the deficit of DB pension schemes stood at £460 billion[10]. Of the 6,000 schemes in the UK, just over 4,000 are in deficit. Seventy-two percent of the 5,794 schemes which are eligible for PPF protection are in deficit.

The aggregate figures conceal the diverse nature of DB schemes and their sponsors. TPR data shows that there is a wide distribution of funding levels across schemes.

FIGURE 1: SCHEMES BY TECHNICAL PROVISIONS FUNDING LEVEL (OCTOBER 2016)



SOURCE: DWP GREEN PAPER – SECURITY AND SUSTAINABILITY IN DEFINED BENEFIT PENSION SCHEMES

Around 400 schemes are funded above 100% of Technical Provisions while approximately 450 are funded below 60%. On average, it is the relatively smaller (in terms of liability) schemes that are more likely to have funding levels of less than 60%[11]. Technical Provisions funding level is significantly below the level required for full buy-out, i.e. this measure potentially underestimates the funding challenge.

8 Purple book – DB pensions Universe Risk Profile, TPR and PPF, December 2016.
9 Annual Survey 2015 – 2016, Investment Association.
10 PwC Skyval Index August 2017.
11 Department for Work and Pensions Green Paper: Security and Sustainability in Defined Benefit Pension Schemes.

This underfunding requires trustees to work increasingly hard to a) protect their capital, and b) invest in assets which get a good rate of return. This is a difficult balance to achieve,[12] and has placed greater emphasis on either getting the right investment strategy to boost returns or on making deficits good through employer contributions – the latter approach requiring greater reliance on sponsor solvency.

Although it is possible that we could see a reversal of the economic and demographic trends driving underfunding, we cannot rely on this to secure the living standards of millions of pensioners. This is particularly so in a fragmented DB system characterised by a significant level of intermediation; without economies of scale, it is harder for trustees to achieve good value for money and access appropriate investment expertise[13]. Reform to regulation to increase the range of options facing concerned trustees is therefore the most reliable way to drive improvement and the elimination of deficits. The time for this reform is running out as schemes are rapidly maturing.

DEPENDENCE ON A STRONG AND SUSTAINABLE EMPLOYER

FIGURE 2: TPR COVENANT GRADE SEGMENTATION

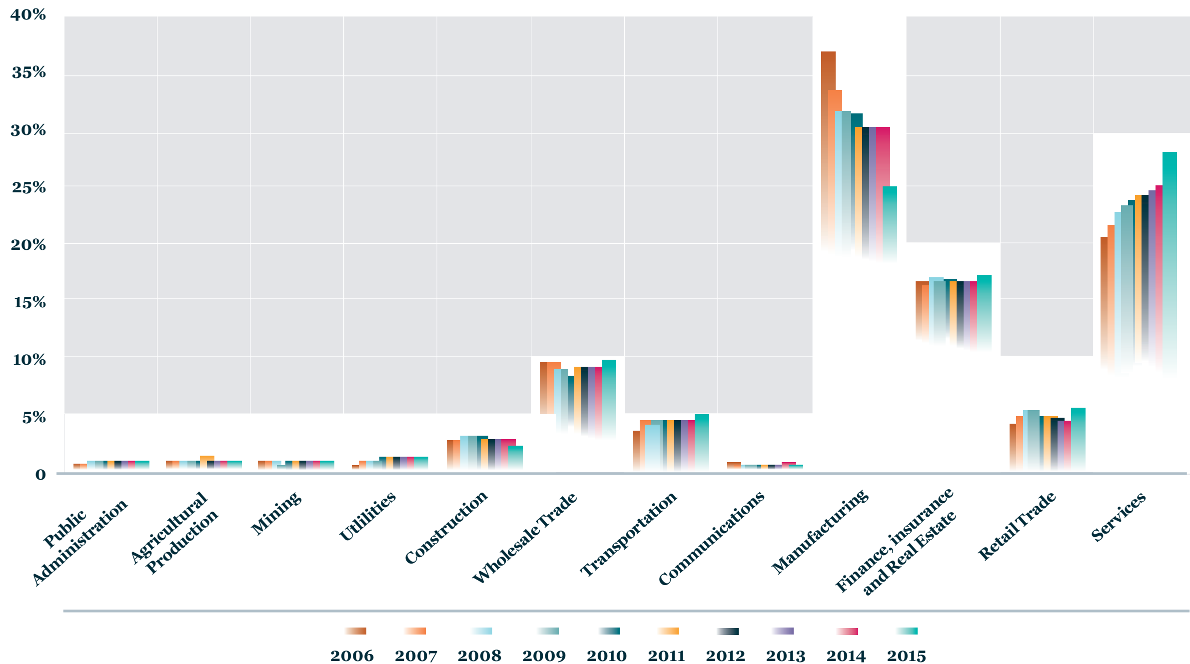
CG1	**Strong**	Very strong trading and asset position. Good growth prospects. Low risk of not being able to support scheme.
CG2	**Tending to strong**	Good trading and asset position. Reasonably positive market outlook. Medium-term risk of employer not being able to support scheme.
CG3	**Tending to weak**	Concerns over employer strength, signs of weak profitability. Potential risk of decline.
CG4	**Weak**	Weak employer, concerns over potential insolvency, scheme large relative to firm's asset and cash position.

The employer covenant plays a vital role in the functioning of DB schemes, effectively underwriting the risks to which a scheme is exposed – including underfunding but also longevity, investment and inflation. The existence of a strong and solvent employer is the key element in ensuring that members' benefits are protected. When a scheme is underfunded, its reliance on the employer's covenant – to ensure deficits are met and member benefits are secured – becomes even more important.

Most underfunded schemes will be able to rely on their sponsoring employers now and in the future. However, many DB schemes will face more fundamental challenges which threaten the strength of their employer covenant. Notably, the schemes run by employers in traditional industries, such as manufacturing or bricks-and-mortar retail, were established at a time when firms in these sectors were thriving. The changing landscape of UK industry means that this is no longer the case today, and DB schemes are now disproportionately concentrated in sectors which are no longer as robust as they once were.

12 The pursuit of this balance has been partly responsible for increased interest from trustees in investment approaches which promise to do both, such as liability-driven investment (LDI) or 'alternative de-risking'.
13 We note there are some services available from market providers that can assist with the related governance requirements.

FIGURE 3: PROPORTION OF SCHEMES BY INDUSTRY CLASSIFICATION



SOURCE: THE PURPLE BOOK 2015, PPF

As an example, the DB schemes of the UK manufacturing and financial services sectors account for just under 60% of DB liabilities but only 30% of GDP[14]. Both these industries have faced their own challenges recently, from globalisation and greater competition in manufacturing from China, India and elsewhere, to the 2007/8 financial crash and its devastating impact on financial institutions. Further challenges to existing business models owing to developments as diverse as digitisation, Brexit and robotics suggest that it is impossible to predict which firms will successfully adapt to these structural headwinds. The high-profile cases of the challenges faced by BHS, Woolworths and the British Steel Pension Scheme show that even household names are not immune. In June 2017, PwC reported that the ability of FTSE 350 companies to fulfil their DB pension obligations had sunk to its lowest level since the recession[15].

Our analysis[16] also shows that over the next 30 years, schemes in the weakest solvency group (CG4) have only a 32% probability of reaching full solvency funding (i.e. paying future pensions in full to members), with those schemes in the CG3 category having a 52% chance of hitting this target. Punter Southall's recent *Risk of Ruin*[17] report estimated that around a third of schemes in the UK "will fail to deliver their benefits in full".

14 J.P.Morgan Asset Management research, 2015: To arrive at this conclusion, J.P.Morgan started with the assets and Section 179 liabilities from the Appendix of chapter 4 in the Pensions Regulator's 2015 *Purple Book*. They then estimated the buy-out liabilities for each sector by scaling up the s179 figures. The scaling factor is the average buy-out to s179 ratio (also found in the appendix of the *Purple Book*) multiplied by the ratio of each industry's average wages to the national average wage (sourced from the *Annual Survey of Hours and Earnings*). Having calculated the percentage of both types of liabilities accounted for by each industry, J.P.Morgan Asset Management then sourced the GDP for each industry and calculated the percentage of the total accounted for by each one.

15 PwC Pensions Support Index 2017.

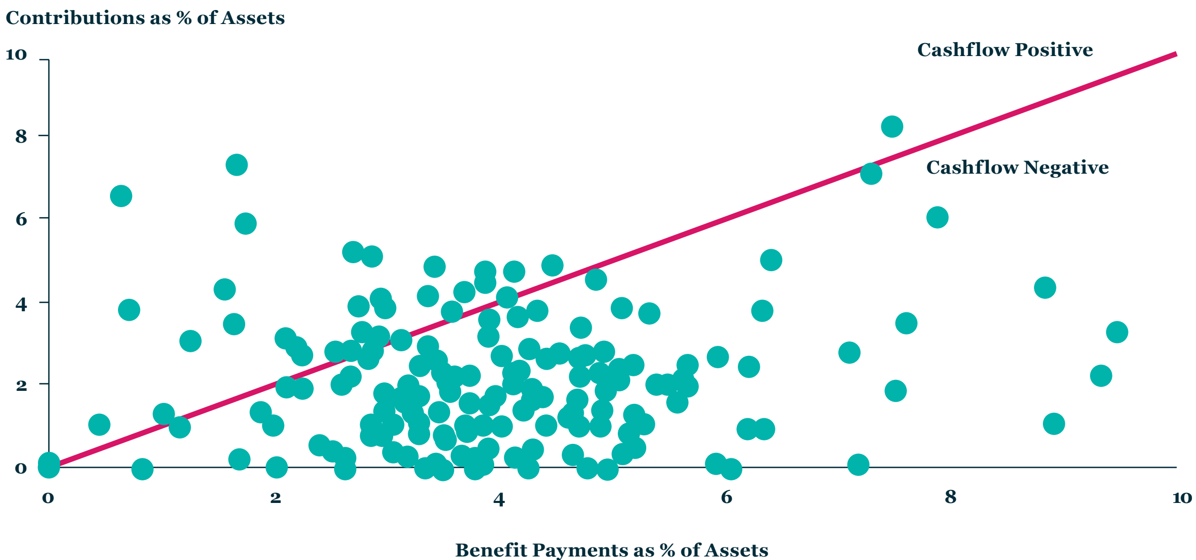
16 Modelling by Gazelle Corporate Finance commissioned by the DB Taskforce.

17 Risk of Ruin, Punter Southall, July 2017.

THE NECESSITY OF ACTION

Time is running out for UK DB schemes. Reports by Hymans Robertson and Goldman Sachs Asset Management have found that 50% of FTSE 350 DB schemes are at, or will soon reach, the level of maturity where they are cash flow negative, with the number anticipated to increase to 90% within five years[18,19].

FIGURE 4: SCHEME CASHFLOW



SOURCE: TROUBLE BENEATH THE SURFACE, GOLDMAN SACHS ASSET MANAGEMENT

However, the system shows no signs of fixing itself, given the current market and regulatory set-up. The Taskforce's first report found that there are several structural factors inherent in the UK DB system which hinder the ability of schemes to solve their underfunding problem: fragmentation, inflexible scheme resolution, a rigid approach to benefit change and sub-optimal risk bearing. This places the retirement savings of millions of DB scheme members at risk.

A GROWING CONSENSUS

There has been a recent spate of high-profile news stories about the problem of DB scheme underfunding, particularly when a sponsoring employer incurs financial difficulties. This has drawn an increased level of attention to the risks in the system.

The DB Taskforce's assessment of the extent of the problem facing UK DB schemes has been echoed in a range of government and regulatory policy work. The DWP's Green Paper '*Security and Sustainability in Defined Benefit Pension Schemes*' recognised that the system was "not operating optimally in all areas" and that while "the majority of employers should be able to continue to fund their schemes and manage the risk their schemes are running, the single biggest risk to the members of these schemes is the collapse of the sponsoring employer". The Work and Pensions Select Committee highlighted the "wider flaws in DB schemes and their regulation" as part of its inquiry into BHS and the DB system.

18 *Building Resilience to Risk*, Hymans Robertson, June 2016.
19 *Trouble Beneath the Surface*, Goldman Sachs, September 2016.

The pressure on both DB and DC schemes to improve investment returns and reduce underfunding has focused schemes' and regulators' attention on how to achieve value for money from investment managers and consultants – a key focus of the FCA's recent asset management market study. Initiatives on cost transparency under MiFID II have also meant schemes should now be equipped with the information needed to think about cost reduction, which can impact investment performance/returns.

There is also better policymaker understanding of the contribution of good scheme governance to investment. For instance, TPR's recent paper on 21st century trusteeship noted the importance of having trustees who are able to engage in investment matters "to ensure appropriate systems, reporting and controls are in place" and "[that] they are getting a quality service and value for money and that risks are being appropriately managed."

Finally, there is growing recognition of the benefits of scale and the disadvantages of a fragmented sector in inhibiting access to investment expertise and better governance. The FCA's final asset management market report recommended that the DWP continue to try to reduce the barriers to scheme consolidation, noting that this could lead to better value for investments.

The next chapter looks at some ways of facilitating consolidation, which we believe could lead to greater economies of scale and the availability of more resources to invest in good governance and improve access to investment expertise and skills.

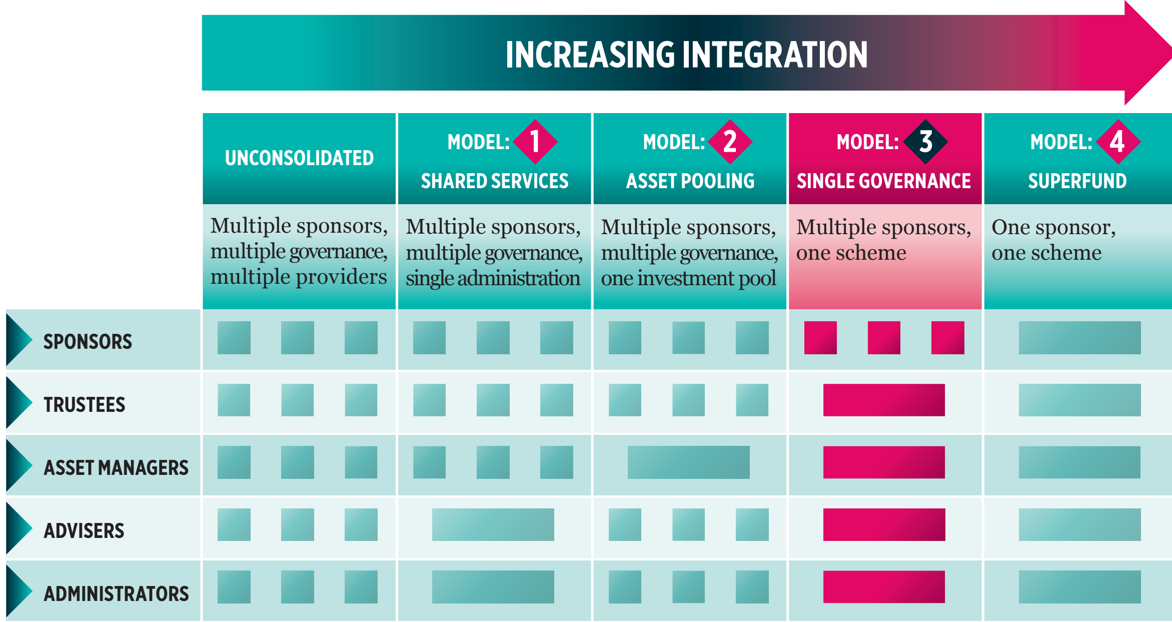
THE DB TASKFORCE HAS IDENTIFIED SEVERAL URGENT ISSUES FACING DB SCHEMES AND WAYS IN WHICH THE INDUSTRY, GOVERNMENT AND REGULATORS COULD TACKLE THESE.

HOW CONSOLIDATION COULD HELP

The Taskforce believes that consolidation could be a key part of the solution to the challenges facing DB schemes as it can help bring about economies of scale and improved governance. Our second report *The Case for Consolidation* set out the potential benefits of four models:

- **Shared services:** using one set of administrative functions and achieving cost-savings through economies of scale.
- **Asset pooling:** assets of distinct pension schemes are consolidated into asset pools to be managed centrally on behalf of the different schemes. Schemes retain their governance, administration and back office functions and most of their advisers.
- **Single governance:** assets of distinct pension schemes are consolidated into a single asset pool and governance, administration and back office functions are merged.
- **Full merger – Superfunds:** Superfunds are created to absorb and replace existing pension schemes. Employers and trustees are discharged from their obligations in respect of benefits that are paid from the Superfund scheme.

FIGURE 5: INTEGRATION MODELS



SOURCE: DB TASKFORCE

The Taskforce found that sharing services, having a single governance structure and pooling assets could produce economies of scale and also deliver a governance premium. However, it also estimated that the total annual cost savings for schemes merging all three aspects would be in the region of £1.2 billion per annum[20]. These savings, whilst beneficial, will not address the £400billion shortfall in DB funding.

OTHER SOLUTIONS

In its Interim Report, the Taskforce identified a number of important ways of helping schemes overcome their funding challenges, including:

- **Improving governance:** well-governed schemes are populated by highly -skilled individuals who can take balanced, informed and well-researched decisions on behalf of beneficiaries. Research[21] has estimated that the impact of good governance can be up to 1% of the fund's value per year.
- **Greater cost transparency:** consistent and standardised disclosure, where costs and charges are clearly presented, can help trustees to scrutinise the value for money they obtain from their investment managers and advisers.
- **Better alignment of interests:** increased complexity in pension scheme legislation and the diversity of assets under management as schemes search for yield has led to a lengthening list of pensions intermediaries. The FCA found evidence of poor value in the asset management market in its market study. Any reduction in reliance on intermediaries could potentially yield savings and improve investment quality.

20 Derived from £0.6 billion in administration savings, £0.25 billion investment management savings and £0.36 billion in governance savings.
21 Pension revolution: A Solution to the Pensions Crisis, Keith Ambachtscheer, 2007.

ENCOURAGING CONSOLIDATION

THE UK PENSIONS SYSTEM IS CHARACTERISED BY A LARGE NUMBER OF SCHEMES. THE PPF REPORTS 5794 SCHEMES IN ITS UNIVERSE WITH £1.5 TRILLION UNDER MANAGEMENT[22].

The average scheme has just over 1,800 members and £200 million of assets but most schemes are small: two-thirds have fewer than 1,000 members. The Netherlands, in contrast, has a similar level of assets under management (£1.3 trillion) but only 308 schemes; this is the result of a period of consolidation after the Dutch regulator (DNB) published a list of "potentially vulnerable schemes" and encouraged them to consider the benefits of merging some functions. DNB also created an extensive new governance structure. Australia's 2010 Cooper Review of the superannuation system led to a series of reforms including the introduction of a 'scale test', where the regulator assesses each scheme's governance and decides whether a fund is acting in the best interests of its members. This has led to a similar wave of consolidation, with the number of schemes with four or more members falling from 333 in 2012 to 242 in 2015.

THE BENEFITS OF SCALE

The Taskforce's Interim Report[23] summarised the growing body of evidence to show that the larger the scheme, the easier it is to:

- achieve economies and value for money through exerting pressure on consultants and managers;
- invest in and acquire skills to make it easier to pick and scrutinise investments; and
- improve governance and oversight of the scheme.

For instance, larger schemes are often able to take a long-term investment approach as they have the expertise and resources to integrate environmental, social and governance factors into their portfolio analysis, or invest in more illiquid asset classes such as infrastructure. Research demonstrates that such an investment approach can yield dividends[24,25]. Similarly, larger schemes can achieve greater diversification into alternative, growth-seeking asset classes such as hedge funds or private equity as they are better able to afford specialist skills and have sufficient money to access specialist asset classes.

UK policymakers have also been examining the possible benefits of scale for schemes. The DWP Green Paper on *Security and Sustainability in DB Pension Schemes* notes that small schemes have higher running costs as "they are not able to achieve the economies of scale which are available to larger schemes and are also less able to negotiate low cost investment management services", as well as stating that "in general, smaller schemes tend to have less effective governance and trusteeship."

22 *Purple Book*, Pension Protection Fund, December 2016.
23 DB Taskforce *Interim Report*, www.plsa.co.uk/PolicyandResearch/DocumentLibrary/0597-DB-Taskforce-Interim-Report.aspx.
24 Harvard Business School Working Paper 12-035 *The Impact of a Corporate Culture of Sustainability on Corporate Performance and Behaviour.*
25 Deutsche Asset Management and the University of Hamburg *ESG and financial performance: aggregated evidence from more than 200 empirical studies.*

FIGURE 6: DB SCHEME RUNNING COSTS

	ADMINISTRATION (£ PER MEMBER)				ADVICE (£ PER MEMBER)			
	PERCENTAGE OF TOTAL COSTS	AVERAGE COST	LOWEST COST	HIGHEST COST	PERCENTAGE OF TOTAL COSTS	AVERAGE COST	LOWEST COST	HIGHEST COST
Very large schemes (5,000+ members)	35%	£64	£21	£139	13%	£23	£8	£52
Large schemes (1,000-4,999 members)	31%	£87	£25	£214	23%	£65	£18	£158
Medium schemes (100-999 members)	36%	£182	£50	£368	29%	£146	£40	£296
Small schemes (12-99 members)	41%	£432	£108	£1,125	21%	£221	£55	£576

*costs have been rounded.

SOURCE: TPR

The final report of the FCA's asset management market study "found that smaller occupational pension schemes are less likely to be able to exert pressure on asset managers" and recommended that the DWP remove barriers to pension scheme consolidation and pooling. This echoes the findings of our second report that a greater sharing of services or consolidation in the way schemes manage their assets or governance structures would have a positive impact on the efficiency of DB schemes.

The FCA found that the UK asset management industry was "heavily intermediated" and that "institutional investors, particularly pension trustees, themselves act as agents on behalf of underlying investors…[and are] typically advised by an investment consultant". A key issue was the reliance of clients on investment consultants given the FCA's concerns and referral of the investment consulting market to the Competition and Markets Authority, due to concerns about sub-optimal outcomes for schemes - and therefore members.

The large number of small schemes in the UK DB system means that schemes may struggle to fix the problem of underfunding and deal with the issue of a weaker covenant by themselves. This is because in part smaller schemes often do not have access to the skills and expertise necessary to put in place effective investment strategies that achieve good value for money and the level of returns which could help solve underfunding. This means schemes end up in an unhealthy stasis, which is then exacerbated by a regulatory system providing trustees with a binary choice regarding scheme resolution: either supported by a solvent employer and achieving full funding, or unsupported by their employer and ending up transferring to the PPF[26].

The Taskforce's second report examined some possible models of consolidation, from shared services through to pooling assets and finally to a single governance model (with multiple sponsors and one scheme). Our analysis found that, on cautious assumptions, cost savings of £1.2 billion annually could be achieved by participating schemes using a combination of all these models, but that barriers to take-up remained.

Experience of recent years in the Netherlands and Australia demonstrates that consolidation will not happen without removal of existing barriers and appropriate incentivisation. This chapter outlines steps the government and regulators could take to encourage consolidation and help schemes achieve scale.

The existing barriers to consolidation can be split into two categories: behavioural and practical. For instance, there is anecdotal evidence that trustees and finance directors may have a tendency to prefer a 'wait and see' approach, as in the short term it is cheaper or appears less risky. There is currently little regulatory encouragement to overcome such tendencies.

26 Solutions such as regulated apportionment arrangements (RAA) exist but these are complex and expensive.

Yet there is also evidence that employers may view consolidation positively. For this report, the DB Taskforce commissioned quantitative research to understand employer appetite for and attitudes towards consolidation[27]. It found that 65% of surveyed employers would support the principle of consolidation. Support was particularly high for the principles of shared administration (72%), shared external advisers (66%), and pooling assets under one asset manager (54%).

Years of incremental regulatory change, industry developments and corporate mergers have also resulted in many schemes having an administratively complex and burdensome benefits structure. Creating a mechanism to simplify these benefits in an actuarially equivalent[28] way could remove the key practical barrier to bringing schemes together in an efficient way.

INCREASING EFFICIENCY

A way of breaking through the barriers outlined above to increase focus on the efficient running of schemes, including value for money, is essential. Ways in which this could be done include:

- A DB Chair's statement
- Benefit simplification

DB CHAIR'S STATEMENT

We believe a requirement on schemes to demonstrate to the Regulator and their members that they are operating efficiently through a DB Chair's statement, similar to that produced for DC schemes, could be an effective mechanism. Since 2015, trustees of DC schemes have been required to prepare an annual governance statement demonstrating how they are meeting new governance standards and signed by the Chair of trustees.

The requirement to produce an annual report on governance and investment issues has encouraged trustees to regularly take stock of their approach to trustee knowledge, investment governance and value for money. We believe that a similar approach could be effective in encouraging the trustees of DB schemes to undertake regular self-scrutiny and consider both the broader governance of the scheme and where it could be improved, as well as the benefits of consolidation.

We would envisage a requirement that trustees report annually in the DB Chair's statement to TPR and members as to how the scheme is operating in line with best practice. Should the scheme fail to meet benchmarked standards, they should be required to disclose what steps they are taking towards improvement. Should no improvements be made within 12 months, the Regulator should intervene and require the trustees to take whatever action is deemed necessary – this could also include some form of consolidation.

27 The PLSA commissioned IFF to undertake a poll of 100 businesses with 50 or more employees who operated a DB scheme; fieldwork was undertaken between 17 July and 8 August 2017.

28 Where aggregate 'before' and 'after' payments have the same current value.

MODEL CHAIR'S STATEMENT

Should report on:

INVESTMENT, FUNDING AND COVENANT (INTEGRATED RISK MANAGEMENT)

Aims and objectives of strategy (including latest SIP)

Why it is appropriate for the scheme, including when it was last reviewed

The level and nature of skilled advice sought

Performance measures, and success against targets

Key risks to the strategy, and how those risks are being managed

Reliance on employer covenant, and current assessment of it

TRANSPARENCY

An explanation of costs: investment, administration, other services

Commentary about VFM money comparison for those costs – are they within a benchmark? – including quality of services received

Areas where information not available, and steps for addressing gaps in future

GOVERNANCE

Levels of skills, experience, diversity within trustee board (compliance against TKU)
Commentary on board effectiveness (including when last reviewed) and training and development during the year

Analysis of board resources

Plans for addressing any gaps in the above

Frequency and focus of meetings

Quality of member communications, record keeping, payments etc.

CONSOLIDATION

Given VFM assessment, what steps are being taken towards further consolidation?
If no action being undertaken towards consolidation, a summary of reasons behind the decision including how members are better off in current structure than in a larger structure

BENEFIT SIMPLIFICATION

The DB schemes in the UK each operate a variety of complex benefit structures, which have evolved over time from historic practice, scheme or company mergers, reactions to legislation, case law or other factors. As a result we now have a system which manages tens of thousands of different benefit structures across 6,000 schemes.

This complexity is commonly agreed to be problematic, and despite technological advances presents barriers to the efficient administration of schemes, contributing to the large differentials in scheme costs (see Figure 7 below) and inhibiting member understanding and communication. It is also recognised as a barrier to the consolidation of schemes or scheme services.

FIGURE 7: DB SCHEME RUNNING COSTS

	INVESTMENT (£ PER MEMBER)			
	PERCENTAGE OF TOTAL COSTS	AVERAGE COST	LOWEST COST	HIGHEST COST
Very large schemes (5,000+ members)	43%	£78	£25	£171
Large schemes (1,000-4,999 members)	27%	£76	£22	£186
Medium schemes (100-999 members)	20%	£101	£28	£204
Small schemes (12-99 members)	20%	£211	£53	£549

SOURCE: TPR

Although there are currently some routes for schemes to try and simplify their benefits, in our view they work imperfectly. They do not, for example, provide trustees and advisers with a framework that is straightforward to use, or in 'standardised' outcomes that result in common structures across schemes. Achieving common structures could both improve member communications and understanding and also act to facilitate consolidation.

We recommend the following changes, outlined in the box below.

BENEFIT HARMONISATION

GREATER SCHEME MODIFICATION POWER TO TRUSTEES

It is currently difficult for trustees to harmonise benefits, as in doing so they may fall foul of Section 67 of the Pensions Act 1995 (which applies whenever a change is made that may adversely affect members' rights). This is the case even when trustees and their advisers have certified that any restructured benefits would be actuarially equivalent, i.e. where the value of the member 'package' is the same for each individual as it was before the change.

It would be possible to add a further purpose to the Pensions Act which could allow trustees, with the consent of the employer, to modify their scheme, e.g. through harmonisation of benefits, as long as the actuarial equivalence was the same for each member. Please see Annex B for further details.

Alongside this, actuarial guidance should be changed/clarified to assist actuaries further when making the actuarial equivalence assessment on an individual member benefit basis.

A 'WHITE-LIST' REGIME

If trustees have carefully considered the case for benefit harmonisation – seeking appropriate advice, considering all relevant factors (including that the changes meet the actuarial equivalence requirement) – and have concluded that simplification is overall in members' best interests, they should feel confident that they can go ahead without recourse. One way of doing so would be to create a 'white-list' regime where legislation would set out a list of requirements trustees had to meet in order to simplify benefits.

This could be accompanied by a statutory discharge of trustee liabilities once they had met all the requirements.

The approach and options outlined above would provide trustees with greater comfort in making decisions to simplify in a way that gives individual members at least the same actuarially equivalent value of benefits following the conversion process as they had prior to simplification. It would also be important to provide protections for core rights, e.g. survivor's benefits or ability to access pension at agreed ages.

We do not pretend to think benefit simplification is an easy or cost-free exercise. But in our view it is worth undertaking, because rationalising benefits in individual schemes and across the sector will have many short- and long-term benefits, including:

- Improved scheme administration and governance
- Clearer communications enabling better member engagement with and decision-making re their benefits
- Reduced hedging costs
- Reduced buy-out costs
- Enhanced opportunities for scheme consolidation

We estimate that benefit simplification could reduce the cost of administration services by over 50%. Given that the size of the current market for hedging is £908 billion[29] and we estimate that over a 20-year period benefit simplification could remove a 5-6%[30] drag on hedging performance, this could, if realised[31], result in significant savings which would in most cases comfortably offset any of the short-term costs of a simplification exercise.

During any benefit simplification process, it is important to provide clear and timely communications about what is happening to scheme members. Schemes would need to ensure members understand the impact and advantages of simplification, and also reassure them that the new value of the benefits received following the conversion would be equivalent to what they received previously.

TRANSFORMING COVENANT RISK INTO FUNDING

The measures outlined above to encourage consolidation should help achieve greater value for money and improve the performance and governance of many schemes. However, they will not be sufficient to address the issue of a covenant that is at risk.

The Taskforce's Interim Report found that merging administration, governance and investment managers could lead to approximately £1.2 billion of annual savings through greater economies of scale. However, these existing consolidation options are unlikely to solve the problems of underfunded schemes where the employer covenant is already under pressure. A specific solution is needed that addresses the high level of risk attached to the weaker covenant groups (CG3 and CG4) and the way in which the current system offers schemes no permanent or reliable way to solve the problem of weak covenants, exposing scheme members to significant levels of risk.

The prospect of continuing to support an uncertain and fluctuating level of DB liabilities is a serious concern for employers. The CBI/Mercer Pensions Survey 2015 found that 65% of business leaders reported that the cost of their DB scheme has a negative impact on business investment, with 90% of leaders concerned or very concerned about volatile markets worsening their funding position.

The situation is exacerbated by the shift over the last 15 years to more stringent accounting standards, whose underlying assumptions can result in significant volatility in the financial results reported from year to year. Having this kind of liability on a firm's books can be an obstacle to obtaining external funding. The current system also lets those employers who are likely to struggle economically off the hook, allowing them to defer payments during which time it is possible that the firm – and the covenant – might collapse, and placing scheme members at risk of not receiving their full benefits.

29 KPMG, UK LDI Market Survey, June 2017.
30 Assumptions based on data provided by industry providers.
31 Limits on market capacity would prevent these savings being achieved across the whole market.

The key is to find a way of turning the uncertain promise of future support into tangible funding. That requires employers to pay more, sooner. Employers will be reluctant to do this given the experience of the last decade – billions of pounds in DRCs coupled with persistently high deficits – unless they get something tangible in return. We believe employers would pay more if as a result they could be released from future liability for the scheme.

> **FOR COMPANIES...THE COST OF THE SCHEME IS ALWAYS WHAT GETS REPORTED. IT IS THE FUTURE RISK TO THE COMPANY OF FUNDING THE SCHEME THAT WORRIES PEOPLE RATHER MORE. IT IS NOT WHAT WE ARE PAYING TODAY; IT IS WHAT WE MAY PAY TOMORROW.[32]**

Neil Carberry, CBI

That, in turn, would require a new vehicle which can take over schemes' assets and liabilities and secure members' benefits, potentially providing a win-win situation for both employers and members. Such schemes – which we call 'Superfunds' and which we first outlined in our second report – are the subject of the next section.

32 House of Commons, Work and Pensions Committee, Sixth Report of Session 2016-17.

ADDRESSING COVENANTS UNDER PRESSURE: SUPERFUNDS

THE TASKFORCE'S SECOND REPORT SET OUT THE PRINCIPLES FOR A NEW FORM OF CONSOLIDATION THROUGH THE CREATION OF SUPERFUNDS: VEHICLES DESIGNED SPECIFICALLY TO CONSOLIDATE BOTH THE ASSETS AND THE LIABILITIES OF PARTICIPATING PENSION SCHEMES. THIS HAS THE POTENTIAL TO:

- Significantly reduce risk to members' benefits;
- Offer a new, affordable option for employers to release themselves from legacy DB obligations, allowing them to invest more in jobs, wages and growth;
- Reduce the burden on the PPF; and
- Boost investment returns and economic growth through provision of better access to investment expertise and greater investment in illiquid assets such as infrastructure.

For this report, the Taskforce commissioned further analysis of the Superfund model to explore how a Superfund might work in practice. Key tests included the level and security of member benefits and costs of entry for different types of schemes with different covenant strengths. Our model has considered scenarios over a range of alternative discount rates and funding levels, with results indicating that there is the potential to create Superfunds which can provide members with 100% of their benefits, offer high levels of security, and are affordable for even those schemes which are facing the most significant underfunding and covenant risk challenges.

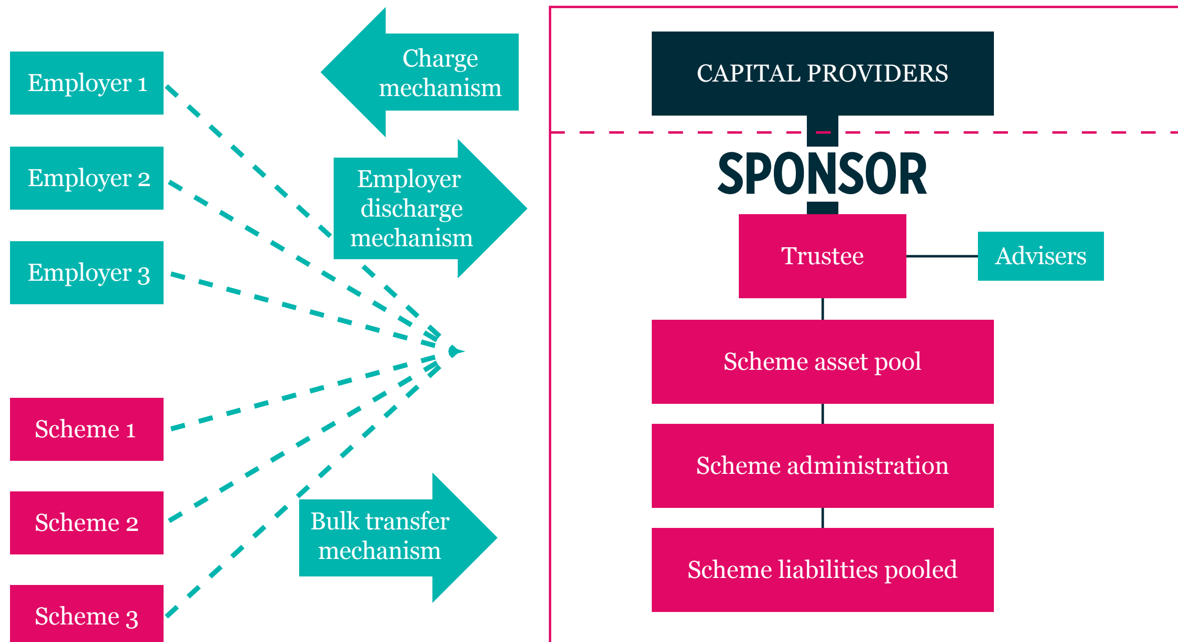
Our analysis is necessarily based on a number of assumptions. In presenting the results of the analysis here, we hope to stimulate debate, challenge and consideration of other ideas about the kind of radical reform that is needed to significantly reduce the risk to the outcomes for members of the weakest schemes in the sector.

WHAT WOULD A SUPERFUND LOOK LIKE?

In essence:

- A Superfund would be an occupational pension scheme;
- It would need to be authorised and supervised by TPR in a regime, not unlike that introduced for DC Master Trusts;
- Trustees and employers would need to jointly agree to transfer their scheme (including all assets and liabilities) into the Superfund, with employers paying a fee upon entry to substantially reduce scheme underfunding;
- Superfunds would aim to pay members the full value of their benefits in more than 90% of scenarios;
- Payments would be simplified to a common structure, as entering schemes would have a variety of different scheme designs which could be complex to administer otherwise; and
- Superfunds would be PPF-eligible, ensuring Superfund scheme members get the same level of protection as they did in their previous scheme.

FIGURE 8: POTENTIAL SUPERFUND MODEL



WHO WOULD BE INVOLVED?

In essence:

- **The Superfund sponsor:** The sponsor of the Superfund would be treated as an 'employer' for statutory purposes. It would be independent from trustees and hold the same kind of powers as sponsors of occupational pension schemes[33]. It would be a single purpose commercial venture with capital at risk. The sponsor could appoint and remove trustees, subject to appropriate checks, and could provide executives or services to perform day-to-day operations, for an arm's-length fee.

  Our model envisages that the sponsor and capital providers of Superfunds would probably require a significant role in investment decision-making – usually the sole preserve of trustees. We think this would be necessary because investors would be putting capital at risk and providers of capital would need certainty and control over the investment strategy and operating model. The sponsor would submit a business plan incorporating the investment policy[34] to TPR for approval, with the Superfund trustees given responsibility for implementing investment strategy[35] in line with the policy.

- **Capital providers:** These would be the investors in a Superfund which provide capital to the sponsor both to establish the Superfund and provide its regulatory capital buffer[36]. We recognise that a Superfund would need to be commercially appealing in order to attract capital providers, and that commercial interest could derive from the following:

  - A provision in the regulatory framework for capital providers to make a financial return upon their investment[37] – this could happen in a variety of different ways including a) a return on capital based upon meeting agreed funding targets (see below), and b) refunds of capital being paid to the Superfund should it move into an ongoing surplus position relative to its funding levels; and/or

33 These would include amendments to the Trust Deed governing the Superfund; acceptance of bulk transfers into and out of the Superfund; contributions payable to the Superfund (NB as there are no active members, any contributions would be for deficit repair purposes); and the ability to wind up the Superfund – unless ordered by TPR.

34 We have modelled the asset allocation as resembling the PPF's relatively safe strategy although this would be adapted to be more or less return-seeking depending on the Superfund's investment objectives.

35 A Superfund would have higher asset returns thanks to economies of scale, strong governance and more resources to put towards investment expertise. This could provide an extra 0.5% annual return compared to individual schemes.

36 TPR may require a higher or lower level of capital buffer, depending on the amount of investment risk that the Superfund intends to bear.

37 In a way that does not harm member outcomes.

- The provision of additional chargeable services to the Superfund, e.g. for administration services.

- **Superfund trustees:** The Superfund would have a corporate trustee, which would chair the Committee. There would be at least three independent trustee directors, one or more of whom would have a member or consumer representative or advocacy background. Each of these trustees would have equal voting rights. The sponsor would retain the power to replace trustees in extreme circumstances. The trustees, not the sponsor, might however need to retain the freedom – as with DC Master Trusts – to replace all their advisers and administrators, including any executives provided by the sponsor should they wish to.

  Trustees would be required to monitor the Superfund's funding level, commission regular actuarial valuations, and supervise the scheme's administration and payment of benefits. Trustees would also be expected to have increased 'day-to-day' responsibilities in many areas relative to those of non-Superfund trustees.

- **Employers:** These would be the current sponsors of the DB scheme that are looking to transfer some or all of their liabilities to a Superfund. Once a transfer of all liabilities takes place, the employer's financial liabilities to their old scheme would cease.

- **Transferring scheme trustees:** These would be the trustees of the scheme that is considering entering a Superfund. Trustee consent would be necessary for the transfer of liabilities to go ahead. Transfers would take place without member consent but significant member communication in advance of any transfer would be expected[38].

  When a scheme has fully transferred to a Superfund, the employer and the transferring scheme trustees would have fully discharged their obligations.

  The duty upon trustees to make decisions in members' best interests means that they would only agree to transfer to a Superfund if they were confident it would provide an better outcome for members over and above the other options available, i.e. the status quo or buy-out. We believe that this would provide sufficient protection for members. It also would not disrupt the current market for buy-out; the best decision for trustees of CG1 or CG2 schemes who are examining their options and can afford buy-out will still be buy-out.

THE OVERARCHING FRAMEWORK

New legislation would be required to enable the creation and safe operation of Superfunds. In envisaging an appropriate operating environment for Superfunds we have sought to supplement the current regulatory framework rather than propose wholesale change to legislation.

Given the potential for the authorisation and supervisory role of TPR in the realm of Superfunds to evolve, it could be appropriate to provide TPR with the authority to set out a large proportion of its new supervisory role in this area through codes of practice[39] or similar.

Superfunds established under trust and operated as occupational pension schemes could be governed by the existing pension legislation (subject to the amendments identified below). They would also be tax registered under the Finance Act 2004. This arrangement would minimise the need for extensive changes to legislation. The main changes needed to existing legislation are outlined in Annex B.

38 Good member communication both before and throughout any transfer process will be vital.
39 In a way similar to the approach taken by the Financial Conduct Authority (FCA) through its regular release of new guidance.

The Pensions Regulator

A Superfund operating as an occupational DB scheme should be supervised by TPR and eligible for the PPF, like other pension schemes. The sponsor and trustees operating a Superfund would need specific authorisation from TPR. This could follow and develop on the authorisation measures shortly to be introduced for DC Master Trusts[40].

TPR would need to impose and monitor the governance structures and standards that apply to all Superfunds. For a Superfund to achieve TPR authorisation it would need to show that:

- The people involved with the Superfund are fit and proper;
- It is financially sustainable, i.e. the Sponsor has sufficient assets to support the operation of the Superfund;
- It has adequate skill, systems and processes to ensure it is managed effectively; and
- It has an adequate continuity strategy and sufficient capital.

A Superfund could demonstrate this by submitting to TPR a business plan which would cover areas including investment policy, funding triggers (see below) and other aspects of operation. TPR would need to approve the business plan which would provide the basis upon which the ongoing operation of the Superfund would be supervised. Although changes could be made to the business plan, these would need to be decided by agreement between the sponsor and trustees and would also be subject to approval by the Regulator. If the Superfund had funding problems or failed to deliver against its business plan without effective mitigation, TPR would have the ability to direct a Superfund to cease accepting new transfers, to wind up or to require a merger with another Superfund.

The Pension Protection Fund

The purpose of Superfunds is to enhance the security and protect the value of scheme members' benefits. Our modelling (below) demonstrates that in 90% or more of cases a Superfund will succeed in fulfilling this role.

We believe that in the case of a Superfund winding up or the Superfund sponsor becoming insolvent, the Superfund should – like any other DB pension scheme – be eligible for the PPF. We expect that entry would not have a dilutive effect on PPF funding as any Superfund should be wound up before Superfund member benefits fell to PPF levels.

Further consideration would need to be given to the PPF eligibility of Superfunds, the levy regime and how Superfund benefits would need to be reflected in PPF compensation. Papers published by the PPF in 2017 on how to approach schemes which have entered an ongoing governance arrangement[41] could provide a strong base from which to consider amending legislation.

PROCESSES

The funding level

Superfunds would require robust funding plans to give transferring scheme trustees and employers sufficient confidence that the Superfund would provide member benefits over the long term and minimise the risk of any claims on the PPF. Continued funding strength could be enhanced through the benefits of scale, which would improve investment skills, reduce costs and boost investment returns.

The Superfund sponsor would need to provide a buffer in the form of a long-term capital reserve to ensure its continued solvency in event of any unexpectedly 'stressful' events and reduce any possible systemic risk. This would be necessary to ensure security of member benefits and would

40 Pension Schemes Act 2017.
41 Determination by the Board of the PPF under section 175(5) of the Pensions Act 2004 www.pensionprotectionfund.org.uk/DocumentLibrary/Documents/1718%20Final%20Determination%20for%20March%20publication.pdf.

be based on the Superfund's initial funding levels. Our analysis indicates that a sensible buffer for operating a private Superfund would be 10% of risk-weighted assets (RWA) or approximately 5% of total Superfund initial assets. This would flex in line with regulatory requirements, trustee decisions or growth in the level of assets in the Superfund.

While the capital buffer and premiums paid by transferring scheme employers would secure strong initial funding levels, it is important that Superfund funding is maintained on an ongoing basis. We believe that a tiered funding regime which governs all aspects of funding, from revenue distribution through to winding-up triggers, would be a sensible approach. How this might work in practice is set out in the table below. The different funding levels – X, Y and Z – would take into account the sponsor's assets, the capital buffer and also the expected premiums to be paid by the transferring employers over a given period, e.g. the next 12 months. Taken together with the annual valuation results, these factors would dictate the approach of TPR, the sponsor's executive team and trustees to the Superfund's operation until the next actuarial valuation.

The precise levels at which X, Y and Z are set would vary for each superfund – depending on, for instance, levels of investment risk or the capital buffer – and would need to be agreed between the trustees and sponsor before being submitted for approval to TPR as part of the business plan.

FUNDING LEVEL (% OF FUNDING)	WHAT HAPPENS
X' or above (e.g. over 105%)	Sponsor can distribute an agreed percentage of assets above X to the capital providers.
Between 'X' and 'Y' (e.g. between 100-105%)	Superfund can operate and continue to accept transfers in from other schemes.
Between 'Y' and 'Z' (e.g. between 90-100%)	No new transfers in can be accepted by the Superfund unless additional capital buffer is added to the sponsor or the sponsor makes payments to the Superfund to bring funding to above a certain level. No impact on existing members' benefits.
Below 'Z' (e.g. below 90%)	The Regulator can direct the Superfund to wind up or merge at levels above PPF benefits.

It will be important to manage the balance of interests between new entrants and scheme members which have already transferred. To ensure clarity for all parties, we would support setting out parameters, e.g. on specific funding levels required in the business plan. This could include, for instance, allowing transfers in from schemes which are below the agreed funding level in exchange for set levels of increases in the contribution to the capital buffer.

MAKING THE SUPERFUND TRANSFER DECISION

The decision to transfer to a Superfund is a significant one which will entail careful consideration by those parties responsible for decision-making on all sides. Entry to a Superfund will be subject to a tripartite agreement between scheme trustees, the scheme employer and the Superfund. To be viable the Superfund will need to be in a position to specify the terms of entry for each scheme and obtain full disclosure of the assets, liabilities and commitments of transferring schemes.

FIGURE 9: THE TRUSTEE DECISION

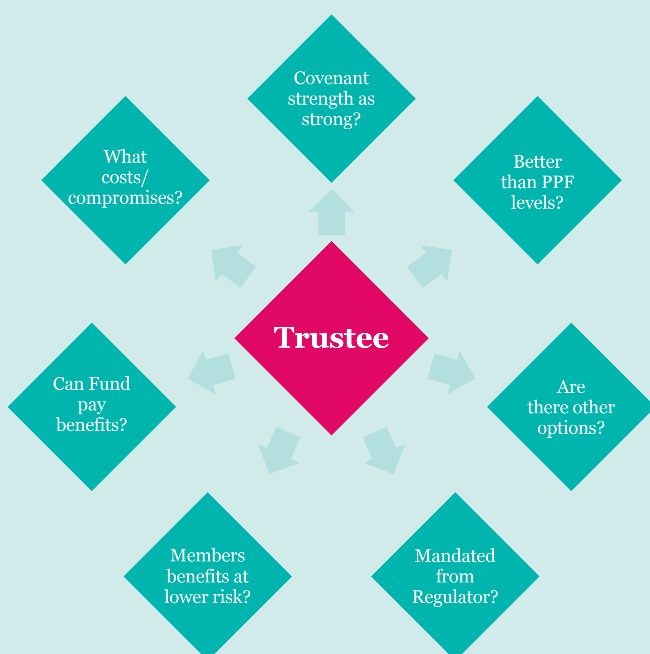
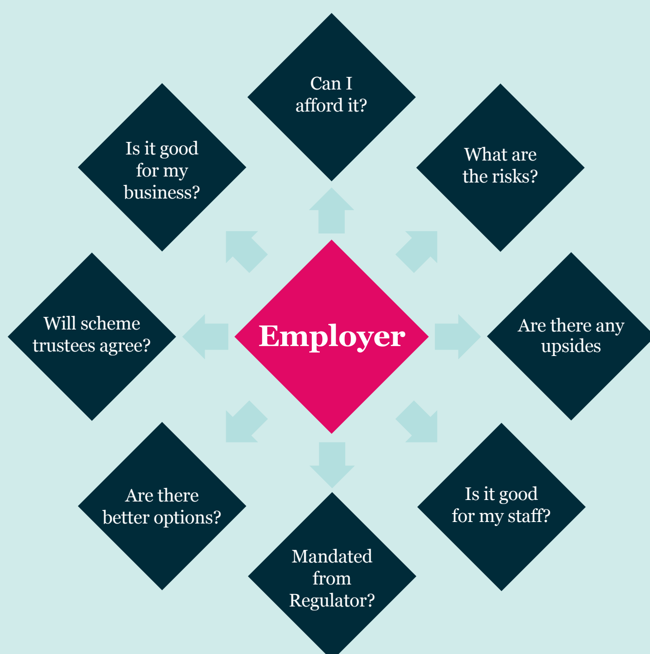


FIGURE 10: THE EMPLOYER DECISION



The transfer of a pension scheme to a Superfund would discharge the employer from its obligations to the pension scheme. One of the most pertinent factors governing the employer decision would be the cost of entering a Superfund: can it afford the payments relative to current and future cash flow?

Trustees also need to ask whether a move to the Superfund will be better than the status quo; the rationale for CG3 and CG4 schemes to transfer liabilities to a Superfund is likely to be stronger than for those schemes with strong covenants.

There will be practical barriers to overcome, including concerns about the potential for upfront costs pre-transfer, the resourcing or technical complexity requirements needed to complete the process. Behavioural barriers such as being 'first mover', the risk of moral hazard or adverse selection will also need to be overcome.

SECURITY AND AFFORDABILITY

We concluded our second report by recognising the need to undertake further exploration of a potentially viable Superfund model. With the support of Gazelle Corporate Finance we have considered a model which could provide:

- An increased likelihood that members would see their benefits paid in full, and that trustees and the Regulator could make an advance judgement on that increase in probability so that they would be able to consider requests to transfer into a Superfund;
- A reasonable chance that employers could afford the cost of entry, measured against their net cash flow; and
- For sponsors to earn a return on the capital they put at risk.

Following the design of the model, LCP assisted with modelling the Superfund cashflows.

ASSUMPTIONS

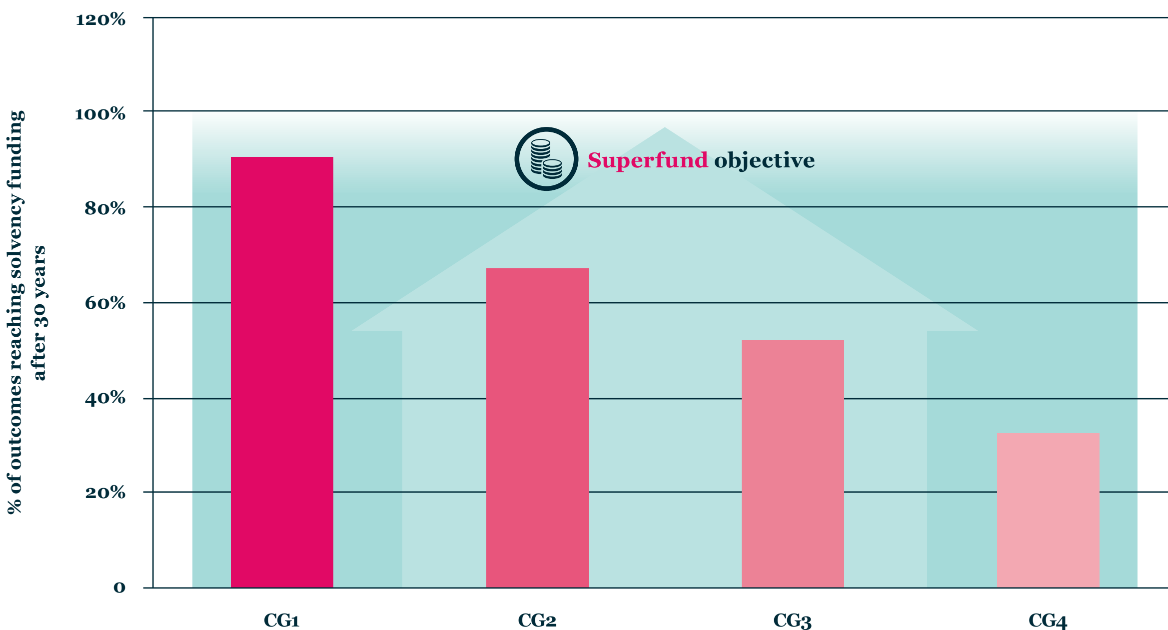
In order to examine these issues, we have had to consider and reach agreement on a range of assumptions about possible Superfund investment and funding policies, the nature of ceding schemes, the corporate debt market and the cost of capital. These are set out in detail in Annex A. We recognise that assumptions are always debatable and that the levels of solvency funding that the government and regulator require to deliver a robust regime will be fundamental to the viability of the model. We expect and welcome further healthy discussion from industry, government and elsewhere on the assumptions we have used to reach our conclusions.

THE BENEFITS FOR MEMBERS

Our objective with this model is to ensure an improved prospect of members – particularly those who belong to schemes in the CG3 and CG4 categories – receiving the full value of their benefits.

While we believe that schemes and sponsors from all the CG groupings should be allowed to access the benefits of Superfunds, the case for doing so would be significantly stronger for CG2, CG3 and the average CG4 employer. CG1 employers would remain the target market for buy-outs and this would probably continue to be the best third-party solution for those schemes with an extremely strong covenant and employer.

FIGURE 11: BENEFIT SECURITY BY EMPLOYER COVENANT GRADE



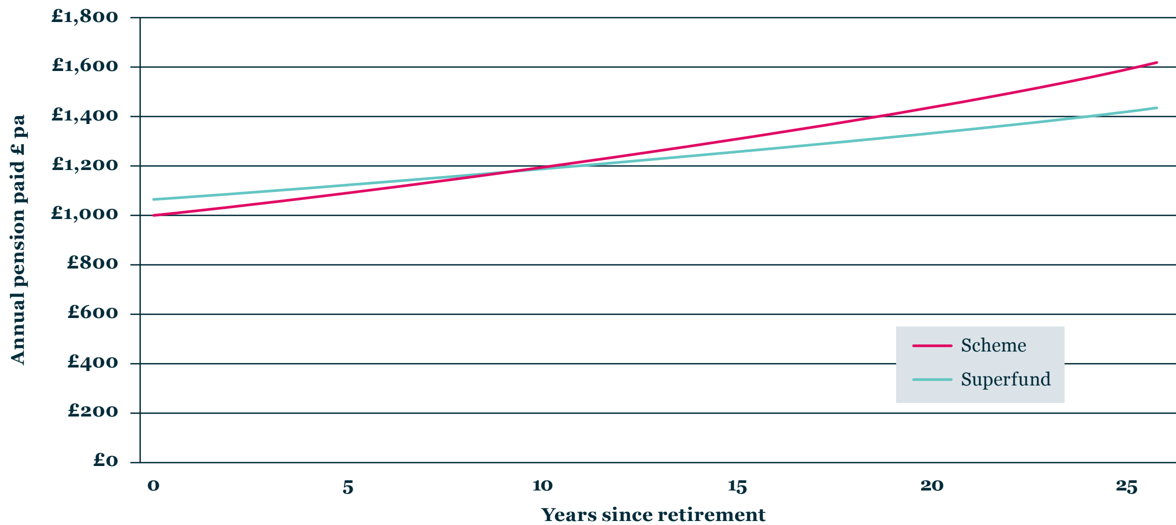
Our analysis indicates that members could be more likely to receive the full expected value of their benefits through a Superfund, except where their scheme is backed by the strongest of employers. This is because the Superfund would benefit from a high initial funding level as well as better investment returns through unlocking economies of scale[42] – the model predicts this could provide an extra 0.5% annual return compared to individual schemes.

Because we expect Superfunds to offer simple, streamlined benefits[43] – one of the benefits of removing barriers to aligning liabilities highlighted above – it is likely that members would also see a change in the shape of payments: typically a shift from RPI uprating in their current scheme to a usually lower CPI uprating in a Superfund. An uplift to the starting pension would ensure that lifetime value was equivalent, even if the pattern of payments over time changed.

42 Investment returns would be boosted in two ways: firstly, through reduced costs from greater negotiating power, and secondly through access to better investment and governance expertise.

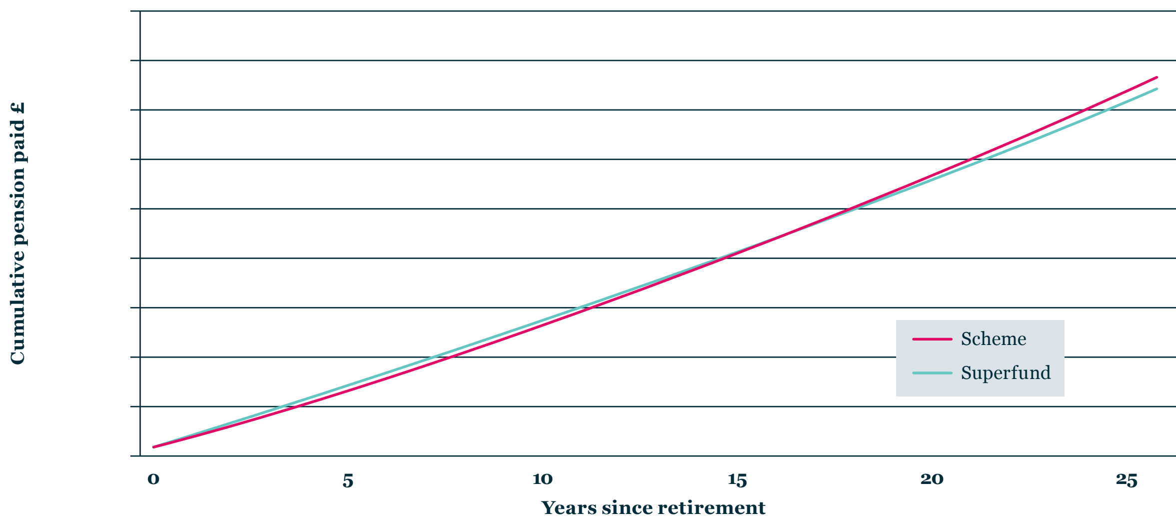
43 We recognise that it might be possible to establish a Superfund without streamlined benefits.

FIGURE 12: COMPARISON: ANNUAL PENSION PAID



SOURCE: LCP

FIGURE 13: COMPARISON: CUMULATIVE PENSION PAID



SOURCE: LCP

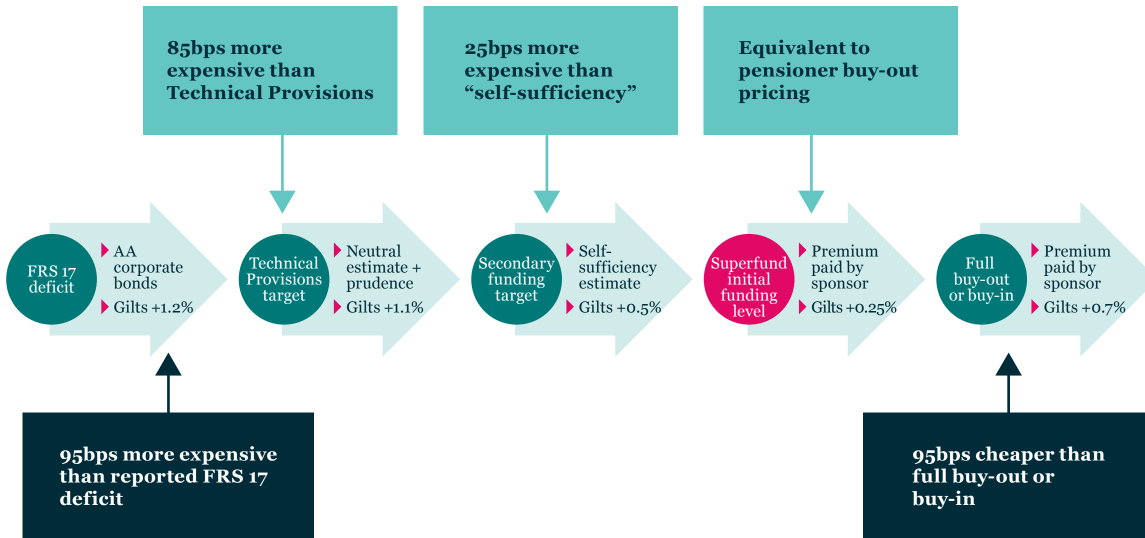
HOW IT COULD WORK FOR EMPLOYERS

In order to release themselves from ongoing liability for their pension scheme, sponsoring employers would need to find a way to bring their scheme's financial position up to the Superfund's agreed entry level. This could be through an entry premium. The level of a premium would depend on a number of factors including the scheme's funding position, the Superfund's pricing basis and the shape and duration of the payment plan.

We explored the scope of entry-level pricing for a range of options in this area, some of which are set out in the table below. Pension schemes (and TPR) typically use the rate of interest, or discount rate[44], attached to UK government bonds (considered secure, low-risk investments) as the baseline for pricing their liabilities. The precise rate used varies for each scheme depending on its level of prudence. We have set out a range of rates used in Figure 14 below. Our central modelling assumption is based on a Superfund pricing its funding level using a discount rate of gilts +0.25% meaning it would typically be 80-85% of the cost of buyout[45].

44 Annual funding statement for defined benefit pension schemes, TPR, 2017.
45 Mercer Global Pension Buyout Index.

FIGURE 14: PRICING APPROACHES



SOURCE: GAZELLE

Figure 15 shows how affordability might look to a sample CG3 scheme. Faced with a deficit of approximately £400 million this sponsor is currently committed to a nine-year recovery plan, with annual contributions of around £40 million. Entry to a Superfund would cost around £600 million as a one-off payment or £65 million per year[46] as a 10-year debt plan. The cost is more than current recovery plans[47], necessarily to ensure Superfunds can start and continue at adequate funding levels, but within the net cashflow. The estimated buy-out cost would be £1016m.

Our employer research found that 39% of respondents would be interested in transferring their scheme into a Superfund[48]. The survey was conducted with employers who did not have an in-depth understanding of the full implications of Superfunds for their schemes, but indicates support for the principles of the model.

FIGURE 15: SHAPE OF EMPLOYER PAYMENTS

MODELLED CG3 SCHEME	
Technical provisions	**£2,492m**
Assets	**£2,066m**
Funding ratio	**82.9%**
Recovery plan (years)	**9**
Deficit recovery contributions (pa, net of tax relief [49])	**£40m**

An employer considering Superfund entry may have recourse to a significant alternative source of funding (such as a group parent) and thereby raise sufficient capital to make a higher one-off entry payment. However, we envisage that in most cases the employer might either need to pay a mix of lower entry payments and/or commit to a contractual, regular debt payment schedule to the Superfund over the course of, say, 10 years[50].

46 Data used assumes inflation and interest rate hedging.
47 Although significantly cheaper than buyout.
48 Interviews included a short synopsis of the Superfund model.
49 Tax relief based on long-term corporation tax rate of 17% from 2020.
50 This would need to take the form of secured debts (which the Superfund might insure against) from the sponsor or a strong group company.

As the table below indicates, entry to the Superfund could be more affordable for CG1 and CG2 employers, however in practice we believe it is less likely that trustees in these schemes would choose to transfer to a Superfund given their relatively healthy position. It would be affordable for CG3 on a cash flow basis, however for some and in particular, CG4 employers may require recourse to external sources of funding. In order to extend the benefits of Superfunds to this group, we modelled further options to increase affordability. We found that with relatively modest changes, entry could become affordable[51] even for the weakest schemes.

FIGURE 16: AFFORDABILITY ANALYSIS

	SCHEME STARTING POSITION				SUPERFUND ENTRY		
	Technical Provisions £m	Funding	Recovery plan Years	Net DRCs £m	Net single premium £m	Debt plan (10 years) £m pa	Debt plan/net cashflow
CG1	2,436	88%	6	39	528	54	2.9
CG2	2,496	85%	7	44	552	58	2.3
CG3	2,492	83%	9	39	600	65	1.2
CG4	2,573	79%	9	50	626	68	0.7
CG4*	2,573	79%	9	50	570	51	1.0

* With 2.5% cap on indexation and 12-year debt plan

We believe that having such an additional option could help a range of schemes. There are currently 930 CG3 and 890 CG4 schemes in the UK which are in deficit[52] and have completed TPR recovery plan submissions, and which we can therefore expect to be at a higher risk of entering the PPF. These are broad groups with very different circumstances and it is impossible to generalise about uptake without examination of individual circumstances. Nevertheless we believe our modelling demonstrates that entry to a Superfund could be feasible for typical schemes in these groups and that the members and sponsors of many of these schemes – including those which are most at risk – could benefit from transferring to a Superfund.

Employers could benefit from eliminating the threat that their uncertain and fluctuating pension scheme liabilities pose to business growth and viability. A business which successfully managed to detach itself from its pensions liabilities could face fewer obstacles to accessing growth capital. Their employees could have improved job security and potentially new employment opportunities.

If they could transfer their scheme to a Superfund, 28% of employers[53] could invest in the business itself including in capital or infrastructure expenditure, with 49% instead investing in employee benefits such as pensions or training.

A system that supported the creation of Superfunds could benefit the government and regulatory bodies because Superfunds could reduce the risk of claims on the PPF, and there could also be a multiplier effect as the 'wealth' impact of the material uplift in benefit security might feed through to investment in the wider economy. Furthermore, the Superfund model could be used to solve the issue of detached or 'orphan' schemes, i.e. those schemes which have been restructured in varied and complex ways using the regulated apportionment arrangement (RAA) mechanism. Finally, a system with fewer, larger schemes might also potentially be regulated more easily and cost-effectively[54].

51 Affordability for schemes in the broader CG4 group would be improved by, for example, extending the debt period from 10 to 12 years or limiting indexation to 2.5%.
52 TPR.
53 Of those that expressed an opinion.
54 TPR evidence to Work and Pensions Select Committee, Written Evidence: The Pensions Regulator, October 2016.

CONDITIONAL INDEXATION

One way which could make scheme consolidation into a specific vehicle even more affordable would be to substitute guaranteed increases in indexation with conditional increases. However, this would mean greater risk-sharing between members and the sponsor, potentially requiring additional government oversight. How this could work is set out in the box below.

RISK-SHARING SUPERFUNDS

It could be possible to establish a risk-sharing Superfund within the legal and regulatory framework set out in the report. This could also typically result in uplift to the face value of member benefits – often a substantial increase.

A risk-sharing Superfund is different because it substitutes guaranteed increases in indexation with conditional increases. Conditional increases could target indexation at 2.5% CPI[55] but would award increases at more or less than the target level based upon the funding level of the Superfund or its investment performance.

Members of a risk-sharing Superfund could receive higher increases than the targeted CPI if the financial conditions permit.

The cost of entering a risk-sharing Superfund could be 10-15% lower than a Superfund providing guaranteed levels of indexation. This is for two primary reasons:

- The funding requirements would be lower under a conditional Superfund, because indexation levels are not guaranteed.
- The elimination of that guarantee means that the risk-sharing Superfund could invest a material proportion of its assets in return-seeking classes instead of matching assets.

Further variations of conditional indexation would also be possible. For example, there could be an approach which included a 'ground floor' level of indexation of say 1% or one which smoothed indexation levels over a fixed number of years.

55 In the Netherlands, collective defined contribution (CDC) schemes allow for CPI indexation to be decreased when funding falls below a defined level.

CONCLUSION

Allowing for the monetisation of covenants through Superfunds would require changes to the legislative and regulatory landscape. However we believe these would be feasible and could potentially produce a significant improvement in the outcomes of millions of members, as well as benefits for UK employers, regulators and government.

This could be achieved by transforming a weak covenant into tangible funding, while pooling investment and administrative functions and improving the quality of governance could lead to better investment returns. Our modelling provides further evidence that Superfund entry could be affordable to many schemes with members at high risk of not receiving their benefits in full.

The recent high-profile cases of BHS, the British Steel Pension Scheme and others have highlighted the challenges facing DB schemes and their sponsors in the public consciousness. Enabling the creation of Superfunds could mean fewer high-profile employer defaults and might encourage people to engage with their retirement, including a better understanding of the potential risks to their own benefits. A broader public understanding of the challenges that schemes and employers are facing can only be positive, and in engaging members could help mitigate the risk of a crisis in confidence in pensions in the future.

CONCLUSION AND RECOMMENDATIONS

IT IS CLEAR THAT A LARGE PART OF THE DB SYSTEM IS UNDERFUNDED. WHILE MOST SCHEMES IN DEFICIT SHOULD REACH A SUSTAINABLE FUNDING POSITION BY DRAWING ON THE RESOURCES OF THE SPONSORING EMPLOYER, OTHERS WILL NOT. WITH EMPLOYER COVENANTS INCREASINGLY UNDER PRESSURE IN SOME SECTORS, IT IS VITAL THAT GOVERNMENT, THE REGULATORS AND THE INDUSTRY WORK TOGETHER TO ACT NOW AND PROTECT THE MILLIONS OF PENSIONERS WHOSE RETIREMENT SAVINGS ARE AT RISK.

The Taskforce's second report outlined The Case for Consolidation and the positive impact it could have on member outcomes. This report has explored in greater detail the issue of covenant risk, and developed a number of recommendations to overcome the barriers to consolidation and broaden the range of options available to trustees:

A DB Chair's statement. This could help overcome some of the existing behavioural biases against consolidation by encouraging trustees to take stock of their approach to trustee knowledge, investment governance and value for money. This would improve the efficient running of schemes. TPR could also use this mechanism to ensure trustees explicitly consider the potential benefits of consolidation for their scheme. **DWP could introduce a requirement for DB schemes to include such a statement within the scheme's annual report and accounts to explain how the scheme has performed against specific quality standards.**

Easing Benefit Simplification. The current complexity of some schemes to administer is not only a barrier to greater efficiency for all schemes, and better member communication but also remains a practical obstacle to consolidating schemes in a way which maximises the potential gains from economies of scale. However the current standards which govern the process for reshaping scheme benefits in an actuarially equivalent way remain unclear. **DWP should reform the guidance/standards/regulations governing actuarial equivalence so schemes and advisers can implement such simplification with greater confidence and certainty.**

Facilitating Covenant Exchange. There needs to be an option available to schemes struggling with both underfunding and employer covenant risk, which allows them to exchange an unknown and intangible covenant for stronger and more secure backing from a larger sponsor. A Superfund vehicle could consolidate assets and liabilities of participating pension schemes, reducing the risk to members' benefits and offering a new option which could release employers from legacy DB obligations and allow them to invest in business growth. **Work should be undertaken by DWP, together with industry and TPR, to develop a regime that supports greater scheme consolidation and realises the potential benefits of covenant monetisation through Superfunds.**

ANNEX A – ASSUMPTIONS

FIRST LOSS POLICY

We assume a first loss policy – i.e. where the policy holder agrees to accept compensation for less than the full amount – is applied to the Superfund portfolio of employer payments.

By utilising this policy the credit ratings on the debts can be enhanced from B- to A-. This reduces the probability of loss from ca. 30% (for B- credits) to around 3.5% for A- credits over 10 years.

Assuming a 50% loss on a default, the portfolio loss exposure provision for this A- debt portfolio would then be only 1.75%.

The first loss policy would provide the Superfund with capital covering the first 10% of losses. The cost of providing capital based on these assumptions would be about 12% per year.

SCHEME BENEFITS

	CEDING SCHEME	SUPERFUND
Normal retirement age	65	65
Spouse's benefits (pre- and post-retirement)	50%	50%
Revaluation in deferment	Statutory	Statutory
Pension increases in payment Pre-1997 Pre-2006 Post-2006	 Fixed (0%) Limited RPI (0%, 5%) Limited RPI (0%, 2.5%)	 Fixed (0%) Limited CPI (0%, 5%) Limited CPI (0%, 2.5%)
Early and late retirement factors	Cost-neutral	Cost-neutral
Commutation factors	At 80% of cost-neutral	At 80% of cost-neutral
Starting benefits		Uplifted from ceding scheme to produce actuarially equivalent lifetime values

SUPERFUND OPERATING MODEL

TARGET	PAYMENT OF FULL BENEFITS IN MORE THAN 90% OF CASES
Initial funding level	Gilts + 0.25%
Capital buffer	10% of risk-weighted assets
Cost of capital	12%
Investment policy (based on PPF's strategic asset allocation)	Cash and bonds 60% Alternatives 20% Equities 10% Hybrid assets 10%
Investment outperformance	0.5% pa compared with individual schemes (from economies of scale allowing access to greater investment expertise etc.)
Cost of employer debt (premium over upfront payments includes credit risk etc.)	CG1 – 1.02 CG2 – 1.05 CG3 – 1.08 CG4 – 1.08

DETAILED MODELLING RESULTS

Superfund initial funding of Gilts +0.0%

	NOTIONAL GROSS PREMIUM (£M)	DEBT UPLIFT FACTOR (X)	ADJUSTED PREMIUM (£M)	SINGLE PREMIUM (NET OF TAX RELIEF) (£M)	10 YEAR DEBT PAYMENT PLAN COST P.A. (£M)
CG1	750	1.02	765	623	63
CG2	779	1.05	818	647	68
CG3	837	1.08 (1st loss)	904	695	75
CG4	868	1.08 (1st loss)	937	720	78

Employer affordability "ready-reckoner"

	DR CONTRIBUTIONS (NET OF TAX RELIEF) (£M)	NOTIONAL NET CASH FLOW COVER (X)	NOTIONAL SPONSOR NET CASH FLOW (£M)	10 YEAR DEBT PAYMENT PLAN COST P.A. (£M)	SUPERFUND DEBT PLAN COVER (X)
CG1	39	4.0	156	63	2.5
CG2	44	3.0	132	68	1.9
CG3	39	2.0	79	75	1.0
CG4	50	1.0	50	78	0.6

At gilts + 0.25% Superfund entry becomes approximately 15% cheaper but many CG4 schemes may still be unable to afford entry.

Superfund initial funding of Gilts +0.25%

	NOTIONAL GROSS PREMIUM (£M)	DEBT UPLIFT FACTOR (X)	ADJUSTED PREMIUM (£M)	SINGLE PREMIUM (NET OF TAX RELIEF) (£M)	10 YEAR DEBT PAYMENT PLAN COST P.A. (£M)
CG1	636	1.02	648	528	54
CG2	665	1.05	698	552	58
CG3	723	1.08 (1st loss)	781	600	65
CG4	754	1.08 (1st loss)	814	626	68

Employer affordability “ready-reckoner”

	DR CONTRIBUTIONS (NET OF TAX RELIEF) (£M)	NOTIONAL NET CASH FLOW COVER (X)	NOTIONAL SPONSOR NET CASH FLOW (£M)	10 YEAR DEBT PAYMENT PLAN COST P.A. (£M)	SUPERFUND DEBT PLAN COVER (X)
CG1	39	4.0	156	54	2.9
CG2	44	3.0	132	58	2.3
CG3	39	2.0	79	65	1.2
CG4	50	1.0	50	68	0.7

If we deploy a PPF 2.5% CPI cap and extend the debt repayment plan to 12 years for CG4 employers, affordability is significantly boosted.

Superfund initial funding of Gilts +0.25%

	DR CONTRIBUTIONS (NET OF TAX RELIEF) (£M)	NOTIONAL NET CASH FLOW COVER (X)	NOTIONAL SPONSOR NET CASH FLOW (£M)	12 YEAR DEBT PAYMENT PLAN COST P.A. (£M)	SUPERFUND DEBT PLAN COVER (X)
CG4	50	1.0	50	60	0.8

Superfund initial funding of Gilts +0.25% & 2.5% cap on CPI

	DR CONTRIBUTIONS (NET OF TAX RELIEF) (£M)	NOTIONAL NET CASH FLOW COVER (X)	NOTIONAL SPONSOR NET CASH FLOW (£M)	12 YEAR DEBT PAYMENT PLAN COST P.A. (£M)	SUPERFUND DEBT PLAN COVER (X)
CG4	50	1.0	50	51	1.0

Modelling and assumptions developed with the support of Gazelle Corporate Finance.

ANNEX B – LEGISLATIVE CHANGES REQUIRED

Below we suggest the key legislative changes that would be needed to establish and operate a Superfund under the legal framework described elsewhere in the report.

REGULATORY	Specific legislation is needed to allow TPR to authorise and supervise Superfunds. The PSA 2017 contains such legislation although it is limited to Master Trusts providing DC benefits. A similar framework should be applicable to Superfunds – either by extending the ambit of the PSA17 or by having separate legislation. TPR would issue a specific code of practice (under section 90 PA 2004) which is applicable to Superfunds.
TAX – EMPLOYER	Legislation to provide that payments made by an employer to the sponsor of an authorised Superfund as part of the transfer process are treated as contributions made to a registered pension scheme (with relief spreading where applicable).
TAX – MEMBERS	Introduce specific provisions to the Finance Act 2004 so that where pension benefits are 'simplified' there will be no annual allowance or lifetime allowance implications (or loss of LTA protections). To guard against abuse benefit simplification would have to be done on similar terms for all members (or all categories of members, e.g. all pensioners) and on terms which do not increase the actuarial value of liabilities on a scheme-wide (rather than member by member) basis.
PENSIONS LEGISLATION	Adjust Regulation 12 Preservation Regulations 1991 to permit transfers without member consent to a Superfund subject to either: (a) Receipt of an actuarial equivalence certificate (standard transfers); or (b) Clearance from TPR and the consent of the PPF (distressed transfers). Regulation under section 35(7) PA 1995 – exempting authorised Superfunds from the section (investment principles). Instead investment policy to be agreed between sponsor and trustees and included in business plan submitted to TPR.

ANNEX C – TASKFORCE MEMBERS

ASHOK GUPTA (CHAIR)

Ashok is Chair of EValue and a non-executive director of New Ireland Assurance, a J.P. Morgan European Smaller Companies Trust, the Ethical Journalism Network, and is a member of the FRC Codes and Standards Committee and Actuarial Council. He also chairs eValue Investment Solutions.

He was recently joint deputy chair of a Bank of England Working Group on Procyclicality. He was formerly Chair of AA Insurance Services, Chair of Skandia UK, a Founder Director of the Phoenix Group, a NED of the Pensions Regulator and NED of J Rothschild Assurance plc (now St James Place Capital).

His executive career has included Group Strategy Director at CGU (now Aviva), FD & Actuary of Scottish Amicable and a Principal of Towers Perrin.

DUNCAN BUCHANAN

Duncan is a partner in the London Pensions group of Hogan Lovells International LLP. Duncan advises both employers and trustees on the operation of work based pension schemes. He has advised schemes entering and exiting the PPF and also on restructuring benefits. Duncan is the immediate past President of the Society of Pension Professionals and is a member of the Association of Pension Lawyers.

FRANK JOHNSON

Frank joined RPMI Railpen Investments in 2004 as Finance Director and became Managing Director, Investments in 2009, supporting the Trustee of the multi-employer rail industry pension schemes. He oversaw the investment business streams of RPMI and Railpen Investments, with assets under management of some £20 billion, until his retirement from RPMI in 2015.

Frank is an independent non-executive director at First State Investments, UK and at GO Investment Partners. He is also a non-executive director of the Pensions and Lifetime Savings Association and Chairman of the Association's Defined Benefit Council. He also sits on the board of the Railway Benefit Fund, a registered charity.

Frank is a chartered accountant and holds a Commerce degree. Before joining RPMI, Frank held a number of finance director posts in the transport sector.

PAUL JOHNSON

Paul is a senior associate at Frontier Economics and a Research Fellow at the Institute for Fiscal Studies. Paul has worked in the economics of public policy for 20 years including stints as a director at HM Treasury, Chief Economist at the Department for Education and Skills and Deputy Director at the IFS. Paul has also been deputy head of the Government Economic Service and a council member of the ESRC.

Paul has researched and published widely on pensions. He was recently asked to lead a review of auto-enrolment by the government, and was a member of the advisory Pension Provision Group set up by the last government. He is a member of the council of the PPI.

JACKIE PEEL

Jackie is UK & Ireland Benefits Director at Mars, a multinational food company. Her principal responsibilities are for the defined benefit (final salary and cash balance) and defined contribution pensions arrangements. She is also a member of the Mars Global Benefits Leadership Team which steers the company's strategic direction for benefits. Jackie has also held in-house pension roles at Barclays Bank and was Pensions Director at VT Group plc where she was a Trustee of the Shipbuilding Industries Pension Scheme.

She is a non-executive director of the PLSA and vice-chair of the Association's Defined Benefit Council.

Before moving in-house, Jackie spent 17 years with Aon Hewitt in various roles specialising in Executive benefits and Global benefits.

TIM SHARP

Tim is a Policy Officer in the Economics and Social Affairs Department at the Trades Union Congress where he oversees its work on pensions and investment issues. He develops and promotes the TUC's policy agenda in these

areas and supports its network of pension trustees. Tim has worked at the TUC since June 2014 having previously been the London-based City Editor for Scotland's Herald newspaper. Tim has an MA in Politics from the University of Edinburgh and an MA in History from Birkbeck, University of London as well as the Financial Planning Certificate from the Chartered Insurance Institute.

STEPHEN SOPER

Stephen has recently joined PwC in the role of Senior Pensions Adviser. He previously held the positions of Interim Chief Executive and Executive Director for Defined Benefit (DB) Regulation on the board of the Pensions Regulator.

A Chartered Banker, Stephen began his career at RBS in 1986 within the international banking division and subsequently worked in executive positions at the Allied Dunbar Group, Zurich Financial Services, Eagle Star and Aon.

ROBERT TALBUT

Robert Talbut was CIO of Royal London Asset Management for ten years through to the end of 2014 and has worked in financial services for over 30. His experience covers portfolio management, business strategy, people management and remuneration and finance. He had previous asset/ business management roles at Threadneedle, ISIS/F&C and Chase Manhattan. He has provided strategic asset allocation advice to a range of institutional clients and has a strong interest in the accountability of management to shareholders and of institutions to their ultimate clients.

He now performs a range of consultancy and NED roles spanning asset management, insurance, pensions and charities.

PAUL TRICKETT

Paul is a non-executive director at Aviva Life UK, Thomas Miller Holdings and Insight Investment. He is chair of Railpen Investments and the Aberforth Smaller Companies investment trust. Previously Paul has held roles as Head of the EMEA Global Portfolio Solutions Group at GSAM, Head of EMEA Investment Consulting at Towers Watson and CEO of the British Coal Pension schemes.

KEVIN WESBROOM

Kevin is an experienced pension consultant who has been advising pension clients for nearly 35 years. He is a qualified actuary and currently the UK lead for Global Risk Services, a fusion of actuarial and investment skills designed to help clients make sense of rapidly changing investment markets and new developments such as buy out, longevity and risk driven solutions.

He is practising what he has been preaching about phased retirement by working four days a week. If his views about the shape of future pensions are right, then his final phasing into full time retirement, and the end of private sector DB pension provision, could come together in 10 years time!

LESLEY WILLIAMS

Lesley is Group Pensions Director at Whitbread, with responsibility for corporate pensions strategy and to the Trustee Company for the operation of the Pension Fund and its investments. The Whitbread pension fund has a closed DB and open DC section. Lesley has worked in the pensions industry for almost 30 years, with previous positions in Gateway Foodmarkets, Abbey National, the Pearl Group and Henderson Global Investors. She is a Fellow of the PMI and has an MBA. She has been a Council member of the Pensions and Lifetime Savings Association since 2009, and became chair of the Association in October 2015.

ANNEX D – TERMS OF REFERENCE

TO UNDERTAKE A REVIEW OF THE CHALLENGES CURRENTLY FACING FUNDED DEFINED BENEFIT (DB) PENSION SCHEMES, AND MAKE RECOMMENDATIONS TO GOVERNMENT WHICH WILL (A) HELP ENSURE THE SUSTAINABILITY OF OPEN DB SCHEMES AND (B) HELP CLOSED DB SCHEMES RUN OFF MORE EFFICIENTLY AND ULTIMATELY SECURE MEMBER BENEFITS.

In reaching its recommendations the DB Taskforce will:

- examine the challenges facing funded DB schemes and the potential impact of these challenges on members' benefits, the health of sponsoring employers, workplace pensions provision and the wider economy;
- assess a broad set of solutions to the many and varied challenges facing DB schemes and in particular DB schemes' own assessment of the feasibility, impact and risks associated with these various solutions; and
- consider the balance between scheme members, employers and other employees.

The Taskforce will seek evidence from DB schemes and their sponsoring employers as well as government, regulators, scheme advisers and a wide range of industry stakeholders in order to fully assess the impact of any proposals and build a consensus around solutions to support DB pensions.

The Taskforce will ultimately issue a report setting out the Taskforce's view of the DB landscape and set out recommendations which can be used by government, regulators, employers and the industry to help ensure a sustainable DB pensions system.

DB
TASKFORCE
OPPORTUNITIES FOR CHANGE

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