A changing world

Paddy Briggs looks at the role of trustees in the new era of closed DB schemes

Once a DB pension scheme becomes closed to new entrants the principal duty remains, of course, to protect the financial security of the fund. But the changing role of the sponsor has implications for the trustees – especially those who may feel a particular obligation to fund members because they were elected by them.

When a fund closes to new employees it also changes subtly from the sponsor's perspective. The reasons why a pension scheme was set up in the first place included the wish on the part of the employer to be competitive on the compensation offer it makes to potential new recruits. The offer of an inflation-proofed final salary-based pension on retirement was a significant part of that offer. But by the late 1970s virtually every major private-sector employer had such a scheme in place, so the pension offer to potential employees was not an area of great competitive tension – schemes were available to all and the benefits attached to them broadly the same.

The decline of final salary pensions

The governments of the 1980s took a very different view from their predecessors. The 1986 Financial Services Act introduced personal pensions, made changes to contracting out and announced the taxation of pension fund surpluses.

Personal pension plans first became available in 1988 and this coincided with the removal of the ability of employers to require employees to join an occupational pension scheme. Now pension arrangements became more flexible and, although few realised it at the time, the ideology of 'freedom of choice' for individuals implicit in the personal pensions initiative was to be the death knell for defined-benefit pensions schemes – at least so far as new employees were concerned. Today only five FTSE100 companies now have a DB scheme that is open to new entrants.

The switch to defined contribution schemes for new entrants

From a DB scheme trustee perspective, the background to where we are now is important for one major reason – it explains why nearly all employers no longer see having a defined benefit pension scheme as being a necessary part of their compensation package offer.

Instead, most facilitate and modestly fund a far inferior defined contribution 'personal pension' scheme. This is partly a function of the changed competitive situation and partly because they will have to provide a workplace pension anyway for eligible staff by 2018 via automatic enrolment. This is the new paradigm – but, of course, existing DB schemes have not in the main disappeared and their proper governance remains an obligation that sponsors cannot evade – however much they might like to.

For trustees the changed status of a DB scheme is very significant

A trustee of a closed DB scheme today is in a very changed situation from that of an open scheme 10 or 15 years ago. Then the need to oversee the pension scheme was not just one of minimising future sponsor liabilities – there was also the need to ensure that the scheme was attractive as an element of the new employee compensation offer. The scheme was a recruitment asset.

My experience in Shell was that the fact we had a very good final-salary pension scheme was a definite asset when we were looking for new staff. Those days are gone and Shell has closed its schemes to new entrants – a decision that not only changes the way that the company sees the schemes but also the role of the trustee.

I imagine Shell would almost certainly rather not have its DB schemes at all – they are non-productive assets with perhaps their only benefit being that the around 4,000 active members of the schemes may be more inclined to stay because of them (in a time of staff reductions even this may not be seen as an advantage).

In addition, overseeing the schemes takes up management time, brings costs with it and is a diversion from the real business of the company. I would predict that Shell, like many other employers with closed schemes, will sell off the schemes to an insurer as soon as the funding ratio of the schemes is healthily positive with the prospect that it will remain so. That day is some time away however and for the foreseeable future Shell is stuck with the need to manage (and possibly even finance) their DB schemes.

But for now closed DB schemes aren't going away

While the pension funds may be an irritation to Shell and employers like them, they remain the absolute key to my enjoying a comfortable retirement – and there are over 30,000 Shell pensioner members like me. And we will gradually be joined by over 9,000 deferred members and the 4,000 actives – the scheme is going to have to be around for a long time to cater for their needs.

For the trustee, the management of assets – both to pay the annual £600 million pension benefits and other costs and to ensure asset growth to cover future liabilities – is the primary task. But it is in this changing world not the only one. Increased longevity has major implications for liability calculations. We are living longer and our assets are going increasingly to have to work harder to look after us. But a pension fund is not just about the financials, important though they are. It is increasingly about the members themselves.

A pension fund is about its members

In his lively polemic *The War on the Old*, professor John Sutherland neatly punctures the myth that the Baby Boomer generation is on some sort of geriatric gravy train whose main challenge is to decide which Caribbean Cruise to choose next. It is a sobering book discussing gerontophobia and intergenerational conflict openly and in my view accurately.

Not many would sink to the level of *The Times* columnist Giles Coren, who said: "Don't go telling me that we owe at least a debt of respect to the elderly? Respect for what… they just enjoyed high employment, good pay, fat benefits, enormous pension privileges…"

But in books like David Willets' *The Pinch: How the Baby Boomers Took Their Children's Future - And Why They Should Give It Back*, my generation is not infrequently vilified.

Sutherland's analysis is less combative and rather more accurate – not least his sobering statement that "old people are being neglected or institutionally abused, even dying, in large numbers – unnecessarily and wrongly" because of inadequate care.

It is this fact that I think should change the perspective of pension fund trustees. The larger our communities of old people get, the more difficult and costly it is for public services to care for them.

In some instances this is a matter of conventional welfare – the need for public money to help the elderly to make ends meet. But often it is not (just) about the cost of welfare but whether it exists at all. The NHS website describes well the scourge of loneliness and it is here that ex-employers and pension fund sponsors have a duty of care.

The value of sponsor- or scheme-funded pensioner welfare

The Shell pension funds and their sponsor have long taken the view that there is a duty of care beyond the payment of the pension.

Financial support has been given to pensioner associations that engage with the retired, arranging frequent social and other events. The costs to Shell are quite modest and the activity is mostly run by volunteers.

Along with this, Shell has funded a team of 45 pensioner liaison representatives (PLRs) whose job is to keep in touch with pensioners, visiting them from time to time and helping them. Linked to this there is a charity called the Shell Pensioners Benevolent Association, which dispenses grants to help pensioners in particular need.

The total cost to Shell of all of this activity is around £1 million per year – or around £30 per pensioner. The PLRs are the eyes, ears and legs of the pension schemes and provide invaluable support in helping the solution of pension issues where only a home visit will do. Above all, however, they help alleviate the scourge of loneliness for many.

Cutbacks on pensioner welfare funding

Shell pensioners were shocked at the end of last year to receive a letter from Shell advising that the PLR scheme would be summarily stopped this year and there would be no replacement for the valuable work the PLRs do.

Many of us active in pensioners' interests have protested against this decision, which we see as grossly insensitive and damaging. But, so far, to no avail. Shell is involved in some major bloodletting at the moment and it seems that non-core activities are particularly vulnerable to this swingeing cost-cutting. A million pounds chopped off the costs is no doubt welcome, even though it is, of course, a tiny drop in the ocean for a corporation with assets of $340 billion and annual profits of $2 billion.

One suggestion is that the cost of pensioner welfare (including the PLR scheme) be transferred to the DB pension schemes and no longer be a burden on the sponsor. The schemes have annual administration and other costs of £36 billion and this would add less than 3 per cent to these costs. Clearly this would be a matter for the scheme trustees and the regulator would need to be happy that the arrangement was within the law. This is currently being investigated.

Trustees are going to need to move beyond the purely financial if they are to discharge their duties to members in the brave new 'closed DB scheme' world. Retired members of pension schemes are living longer, which brings benefits, of course, but also personal challenges.

Paddy Briggs is a former trustee of the £14.6 billion Shell Contributory Pensions Fund