Victorious

Summary

- Over time, many forms of occupational pensions have evolved to meet varied and changing needs.
- Government, regulators and the industry continue to consider the potential for consolidation or adaptation of DB schemes.
- DC provision is set to dominate, but some single employer trust-based schemes may consolidate or be absorbed into master trusts.
- Poor outcomes for some DC savers may boost demand for collective DC schemes of some form, in some circumstances.
- Schemes will continue to evolve as the pattern of retirement itself changes.

David Adams explores which of the pensions industry's plethora of saving structures will dominate in the future

In any mature marketplace, the ranges of available products can evolve into a baffling array of choices. Pensions are no different. We now have single and multi-employer DB schemes, trust-based single employer DC schemes, contract-based DC schemes; and master trusts for both DB and DC. But although each will exist in some form for decades to come, which types of scheme will still be widely used in future? And what other forms of retirement saving might emerge?

One trend that has dominated pensions in recent years seems certain to continue. "DB is on the way down and DC is on the way up," says Pinsent Masons partner and head of pensions Carolyn Saunders. Active membership of private sector DB schemes was 1.3 million at the end of 2016, according to

the Office for National Statistics (ONS), but there were only around 500,000 active members in DB schemes still open to new members. 2017 saw further DB scheme closures.

"We've seen a continual wave of closures as the cost of those schemes has risen," says Institute and Faculty of Actuaries (IFoA) pensions board deputy chair Mark Williams. "Many DB schemes are still huge, so they're not an issue that's going to go away tomorrow. But will they form a major part of pension provision in 20 years' time? I don't think so."

The Pensions and Lifetime Savings Association (PLSA)'s DB Taskforce has considered how some DB schemes – or at least some functions like investment and administration – might be consolidated. PLSA policy lead on investment and DB Caroline Escott says the taskforce considered different options along a spectrum running from pooled administration and governance to full consolidation of assets and liabilities into 'superfunds'.

At the time of writing, the industry was also still awaiting the publication of a new white paper by the Department of Work and Pensions (DWP), looking at the future sustainability of DB schemes.

Existing multi-employer DB schemes also face challenges, including the problem of section 75 debts that effectively trap some employers in such schemes. But Escott is keen to stress that there are some very well-run multi-employer DB schemes. She also believes that DB master trusts may be used by more employers in future.

Then there are the DB public sector schemes. Every now and then, analysts hazard a guess as to the scale of the burden these schemes' liabilities impose on UK government finances. As the number of open DB schemes in the private sector continues to dwindle, calls to at least adapt the public service schemes, to move from final salary to career average arrangements, are likely to increase in number and volume.

DC domination helping drive consolidation

Although the number of people saving in DC schemes has been boosted dramatically by auto-enrolment, this highly successful policy may weaken some single employer, trust-based DC schemes, suggests Royal London director of policy and external communications (and former pensions minister) Steve Webb.

Auto-enrolment means membership of an occupational scheme is no longer a differentiator with which to attract staff, while the fact that in many industries employees change jobs every two to five years means many schemes will end up with large numbers of deferred members with small pots. "I think we will see many more firms moving either to using master trusts, or to group personal pensions," says Webb.

But PLSA deputy director for DC Nigel Peaple believes that many larger single-employer schemes will continue in their present form, "because those employers have the capacity and resourcing to run those well and they are probably embedded in the overall benefits package".

The future seems reasonably bright for contract-based DC arrangements. The independent governance committees (IGCs) running these schemes appear to be performing well in general; and contract-based DC is also an attractive option for some employers trying to meet auto-enrolment obligations.

But the big growth story of recent years is that of master trusts, of which membership is now above 10 million, according to The Pensions Regulator data. "Master trusts will continue to grow for a long time," says JLT Employee Benefits director Charles Cowling. "These things will become the equivalents of big insurance companies."

Not all the 60 or so master trusts running today will reach that scale: consolidation appears inevitable.

Pension Administration Standards Association (PASA) deputy chair Kim Gubler believes "regulation will strengthen the remaining players and strengthen trust in the sector".

Other forms of DC pension saving are also likely to remain popular and will continue to evolve to meet changing needs, including group SIPPs and group personal pensions. Yet as more people approaching retirement are more likely to be relying primarily on DC pension savings, it will become clear just how much money needs to be saved in a DC pension pot to provide a comfortable income in retirement.

"Many people will get to that point and not have enough money," says Barnett Waddingham senior consultant Malcolm Mclean. "That's not just about adequacy of income but also about how long that income has to last. There is a major problem brewing." Nor will planned increases in minimum

contribution rates for auto-enrolment pensions provide a complete solution.

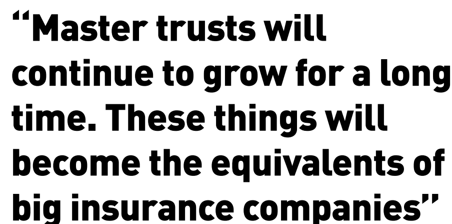
Growing support for collective provision

The fact that DC pensions cannot guarantee an income is one reason that some in the industry favour the introduction of collective defined contribution (CDC) pensions, based in part on the defined ambition concept promoted by Steve Webb during his tenure as pensions minister. Such schemes use risk and cost sharing, setting a target amount to be paid to members based on mixed risk investments, while retaining an option to alter the level of benefits paid out in the event of adverse economic conditions. Regulations outlined in the 2015 Pension Schemes Act that would have enabled implementation of defined ambition pensions were put on ice later that year and have not been revisited.

At the time of writing the House of Commons Work and Pensions Committee is running a consultation examining the potential benefits of CDC pensions, due to close at the end of January. At the same time, Royal Mail and the Communication Workers Union began to reveal details of an agreement to create an adapted version of the organisation's pension arrangements that will use some risk-sharing to provide retirement incomes. Both Peaple and Saunders can see the potential for similar arrangements to be developed by other employers in future.

Other voices in the industry favour other forms of collective pension provision. In a submission to the Work and Pensions Committee's inquiry, the Cass Business School's Pensions Institute director Dr David Blake suggested that collective individual DC (CIDC) schemes, which maintain individual accounts, might be more suitable vehicles for pension savings. They maintain a direct relationship between individuals' contributions and the benefit they receive as a pension, while retaining the advantages of economies of scale and some risk sharing.

One key determinant of the type of occupational schemes used most often in future will be the willingness of employers to take a paternalistic approach. Williams believes more employers will want to use employee benefits to help improve employees' financial health, just as they already seek to help them maintain good physical and mental health, to ensure they perform as effectively as possible in their work.



Providing such a service would tie in with the need, acknowledged by the whole industry and government, to improve levels of financial education and understanding within the general population. The proposed pensions dashboard and fintech tools that help individuals understand how much money they need to save to ensure a decent income in retirement may help.

At the same time, the nature of retirement itself is changing. "We're going to see more partial retirement, so, some income in retirement will come from work," says Williams. "That would mean some savings can be backloaded for long-term care."

As more people reach retirement relying on DC savings the hope is that this will also drive further product innovation in the decumulation phase, benefitting retirees, says Peaple. Yet while employers, regulators, politicians and service providers will all have a role to play to help ensure members end up with a decent income in retirement, ultimately individuals need to take some responsibility for putting money aside for use in later life. As Williams puts it: "Whatever form pensions take, it still requires people to put enough money in."

Written by David Adams, a freelance journalist