



THE INSTITUTE  
OF CHARTERED  
ACCOUNTANTS  
IN ENGLAND AND WALES

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Your ref:

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Dear Ms Ball

## **RISK SHARING CONSULTATION PUBLISHED IN JUNE 2008**

The Institute of Chartered Accountants in England and Wales (the 'Institute') is pleased to have the opportunity to comment on the consultation paper on *Risk Sharing* published by Department for Work and Pensions ('DWP') in June 2008.

The Institute operates under a Royal Charter, working in the public interest. Its regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the Financial Reporting Council. As a world leading professional accountancy body, the Institute provides leadership and practical support to over 128,000 members in more than 140 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. The Institute is a founding member of the Global Accounting Alliance with over 700,000 members worldwide.

### **General comments**

We welcome this initiative. Defined benefit (DB) pension provision is under huge pressures and any measures which encourage and/or help employers to continue providing the same level of benefits, which tend to be more generous than money purchase, is welcome.

We have not had an opportunity to survey our members at this stage but if DWP produced some draft proposals we should be pleased to consider the practicalities of getting our members' views on these.

## Answers to specific consultation questions

*1. Given that we have protected scheme members and are bringing in measures to combat undersaving, should we undertake a far-reaching deregulation of the way risks are shared in pension schemes?*

We are in favour of deregulation of the way in which risks are shared in pension schemes and would encourage a far reaching review.

We do not consider, however, that the Consultation gives enough emphasis to the impact and costs of regulation on pension provision generally. We would therefore encourage measures which reduce regulation beyond risk sharing. We also consider that the whole issue is extremely time sensitive with increasing closures of DB schemes and a general decline in high quality workplace pension provision. Action is needed urgently.

In order to provide greater clarity, we think that the process starts with setting out a continuum of risk. At one end is the traditional employer-backed balance of cost scheme; at the other end is the traditional money purchase arrangement. Each “new type of scheme” needs to be accurately placed on that continuum. Essentially, for any analysis of the regulatory burden, there is a dividing line on that continuum for whether any scheme is within the PPF regime.

*2. Are you aware of any additional evidence of the impact on pension outcomes of lower contributions into DC schemes when all these complicating factors are taken into account?*

We are only aware of anecdotal evidence on this point.

*3. Is our characterisation of the allocation of risks in DB and DC schemes correct?*

*4. Which parties are best placed to bear each risk?*

We have no specific comments to make in response to these questions. However, we consider that as a general rule risks and rewards should lie together so that if risks are increased and specifically taken by one party the potential reward should be greater and available to that party.

*5. Are you aware of any further international examples, or details of the experiences outlined above, which would be relevant to the debate on risk sharing in this country?*

We are not aware of any further examples: the list in the consultation paper appears to be complete.

*6. In general, do you believe greater flexibility in the way employers and employees can share pension risks would increase (or slow any decline in) the availability of high-quality workplace pension provision?*

We believe that greater risk sharing should slow down the decline of workplace pension provision and may even encourage the continuation of certain DB provision. It is unlikely however to encourage any significant new provision. It is also important that any new type of scheme fits easily within the exemptions for personal account provision – otherwise there is a real risk that the options will be unattractive to employers and “levelling down” to PA levels and scheme structure will be more prevalent.

*7. Would this greater flexibility encourage employers who are considering a move out of DB provision to continue to bear some risk rather moving fully to DC?*

*8. Would employers currently offering DC consider a move to a risk sharing arrangement?*

Yes, we believe that greater flexibility might encourage both results.

*9. Do employers consider the existing risk sharing options (for example cash balance schemes, career average) when looking at alterations to DB pension arrangements?*

We have not conducted research on this point so have no evidence on which to base a reply.

*10. Have you considered any options other than those outlined in this chapter?*

*11. Have the existing options proved inadequate and if so how?*

We have no comment on these two questions.

*12. What could be done to regulation, legislation to make the risk sharing alternatives discussed in this chapter easier to achieve?*

*13. What could be done in information or guidance to make the risk sharing alternatives discussed in this chapter easier to achieve?*

There needs to be clear categorisation so there is no doubt as to whether a scheme is DB or DC, and whether entry to PPF is available.

*14. Is the DB legislative framework disproportionate for cash balance schemes? Should the legislative framework be changed to allow schemes more freedom to apply revaluation and to increase annuity options available to members?*

We have no comment on this point.

*15. Are you aware of any issues related to age discrimination in cash balance schemes in the UK today? Is this an issue which is stopping employers from setting up cash balance schemes?*

Age discrimination is within Government control and an opt-out for occupational pension schemes is available as in Ireland. We consider, therefore, that the position could be deregulated quite easily.

*16. Would the introduction of conditional indexation schemes add significantly to the risk sharing already available to DB schemes?*

*17. Is sharing investment risk with pension scheme members through indexation and revaluation provisions a suitable response to the costs and risks facing DB scheme sponsors? Is it acceptable that this risk should be transferred to retirees?*

*18. Are there other approaches to conditional indexation which you consider to be better?*

*19. To what extent would DB scheme sponsors adopt this option as a middle ground for continuing to provide some sort of DB provision? If so, in what circumstances? If not, what might be adopted instead?*

*20. To what extent would DC scheme sponsors be expected to adopt a conditional indexation option to protect their employees from the risks inherent in DC provision?*

*21. Are the risks of implementing conditional indexation identified in this chapter appropriate? If not, which other risks do you think apply? How likely is it that these risks would materialise?*

*22. If risk sharing is adopted, what sort of protection for members is appropriate?*

*23. Does the fact that the risk sharing available to sponsors depends on the rate of inflation reduce the potential value of conditional indexation to them?*

We do not have specific answers to each question at the end of Chapter 6, but make the following general comments. We believe that indexation was a cost where the future impact was not fully understood. Although the impact of conditional indexation is unlikely to be significant, it is nevertheless desirable as it would encourage the continuation of certain schemes. It would also help to establish more of a level playing field with certain other EU jurisdictions. We therefore consider that it would be helpful if conditional indexation were encouraged.

*24. Would the introduction of conditional indexation schemes add significantly to the risk sharing already available to DB schemes?*

*25. Is sharing investment risk between pension scheme members through indexation and revaluation provisions a suitable response to the costs and risks facing DB scheme sponsors?*

*26. To what extent would DB scheme sponsors adopt this option as a middle ground for continuing to provide some sort of DB provision? If so, in what circumstances? If not, what might be adopted instead?*

*27. To what extent would DC scheme sponsors be expected to adopt a collective DC option to protect their employees from the risks inherent in DC provision?*

*28. Do you think members would accept this way of sharing risk?*

*29. Are the principles for the regulation of collective DC schemes appropriate? If not, which other principles would be appropriate? Would these schemes be able to operate under these principles?*

*30. Is the attraction of collective DC great enough to justify the creation of new regulatory regime for them? Are the other ways in which they would be permitted?*

*31. What else could be done to increase the certainty or predictability for members in DC schemes?*

We do not have sufficient experience of collective defined contribution schemes to comment on the issues discussed in Chapter 7.

Please contact me should you wish to discuss any of the points raised in this response.

Yours sincerely



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