the promise for the next session of Parliament

"Measures will be brought forward to … help people save for later life." (The Queen's Speech 19 December 2019)

"The main benefits and elements of the [Pension Schemes] Bill [include]

- Creating a new pension scheme to give greater choice for employers and enable people to adequately save for retirement and better predict their income in later life,
- Providing a framework for the establishment, operation and regulation of collective money purchase schemes (commonly known as collective defined contribution pensions)." (Queen's Speech 2019: background briefing notes)

The probability is that the Pension Schemes Bill 2019, which was lost on the dissolution of Parliament before the election on 12 December 2019, or something similar to it, will be introduced during the present parliamentary session. The bill is expected to provide for collective money purchase benefits and schemes and the repeal of substantial parts of the Pension Schemes Act 2015.

collective money purchase – brief description

"Defined Ambition" was the term previously used by the government for a new category of risk sharing pensions to be introduced alongside defined benefit (DB) and defined contribution (DC) pension schemes. The new term for the same concept is collective defined contribution (CDC). The government wrote in 2014 "We want to encourage risk sharing to provide more certainty and stability in pensions for individuals than DC pension schemes [and] less variation in costs for employers than DB pension schemes". It introduced provisions for this purpose, in the Pension Schemes Act 2015, which have not been brought into force and are likely to be repealed and replaced by new provisions for CDC schemes,

The key to understanding CDC is to describe the present form of DC as "individual". Each member of a DC scheme has his or her individual savings "pot" to provide individual retirement benefits according to his or her individual means and expectations. In contrast with this, no member of a CDC scheme has an individual pot, but all contributions and investment returns are held collectively, as in a DB scheme, out of which a standardised level or rate of benefits is payable to all members; but not as DBs, because in a CDC scheme (a) the employer has no liability whatsoever except for fixed contributions and (b) member's benefits (eg a pension of 80$^{\text{ths}}$ of salary) can be increased or reduced on actuarial advice.

For a more detailed example, see the Royal Mail's anticipated pension design for its CDC scheme, published in November 2018, after it and the Communication Workers Union had agreed it, subject to legislation, at the following link.

https://www.royalmailgroup.com/media/10542/scheme-design-summary-booklet.pdf.

In short, a CDC pension scheme is not unlike a targeted money purchase scheme, or even older DB schemes, when there were no sanctions for insufficient funding and the DBs were no more than ambitions.

collective money purchase – expected advantages

The summary of the government's response: Delivering CDC pensions schemes, last updated 18 March 2019, states "Advantages of CDC schemes include that they:

Roderick Ramage
BSc(Econ) solicitor
authorised and regulated by the Solicitors' Regulation Authority number 231800
Copehale, Coppenhall, Stafford, ST18 9BW
01785-223030, roderick.ramage@law-office.co.uk, www.law-office.co.uk

- provide a savings and income in retirement option within one package that is potentially attractive to people who are uncomfortable making complex financial decisions at the point of retirement;
- enable the sharing of longevity risk between members, therefore providing each individual member with an element of longevity protection without the cost of accessing the insurance market; and
- allow employers to offer their employees a pension scheme, which offers an income in retirement in the form of a pension from the scheme's own assets, but without the risks and balance sheet impact of sponsoring a defined benefit plan."

Although the advantages of spreading risks and possibly negotiating better value terms for investment management are greater for big schemes than for small, the 2019 Bill contained no provision expressly preventing small schemes from giving CDC benefits and thereby being able to pay scheme pensions.

<u>the historic reasons for CDC</u>

The cost of funding and the benefits provided by pension schemes are no different in principle from the position and momentum of sub-atomic particles in quantum theory: in both cases neither variable can be measured accurately and simultaneously with the other. The rule in quantum physical is known as the Heisenberg uncertainty principle, My description of the rule in pensions is the finance director/employee friendly principle.

A DB scheme (whether final salary, average salary or some other measure) is employee friendly, because one knows throughout what the employee's pension will be in relation to his or her pensionable salary and length of pensionable service on retirement, but it is finance director unfriendly, because the cost of providing it is unknown and must be guessed on the basis of the scheme actuary's scrupulously careful and detailed calculations on a foundation of sand (assumptions of future interest rates, investment returns, longevity etc).

Conversely, a DC (money purchase) scheme is finance director friendly, because one knows throughout what the cost is, what contributions must be paid, but it is employee unfriendly because no one knows what pension he or she will received on retirement, the amount of which could be guessed on an actuary's calculation as above, except that few employees could afford an actuary and the financial services legislation, whose purpose is to protect consumers, makes it impossible for anyone else to guess them, except in the most generalised terms.

The stark choice between the two, FD friendly or employee friendly, crystallised on 24 July 2014, when (pursuant to the DPW's announcement on 27 July 2011, the day of the judgment in Bridge Trustees v Yates [2011] UKSC 42, that the government would introduce legislation to reverse the effect of the judgment) the Pensions Act 2011 s29, which altered the definition of "money purchase" in the Pensions Schemes Act 1993, came into force, but backdated to 1 January 1997. The finding in Bridge Trustees was that the payment of pensions out of the scheme's assets, using a table of factors provided by the actuary, did not prevent the benefits from being money purchase.

Before 29 June 1992, when s58B (Deficiencies in the assets of a scheme on winding up) was inserted in the Social Security Pensions Act 1975 by the Social Security Act 1990, final salary pensions were secure only if there was enough money, and winding up clauses abated benefits if the assets were insufficient.

In conclusion, if the Government introduces CDC as expected, it will in effect reverse its reversal of the Bridge Trustees decision, albeit with more regulation and provisions that a court cannot find that a CDC scheme is not money purchase.

END