



PensionsWatch 2007

An analysis of directors' pensions

1. Executive summary

The TUC has established PensionsWatch in order to give a picture of occupational pensions in the UK, with a focus on the pension provision for top company directors. The survey draws information from the most recent annual reports on the pensions provisions for staff and directors at a number of major UK companies.

While employees in the UK have seen a trend towards riskier and less generous pensions, directors continue to receive significant retirement benefits. They tend to accrue pensions at a more generous rate than employees, and the majority are still in final salary or defined benefit (DB) schemes. Those in defined contribution (DC) schemes receive company contributions that are well above the average for these types of scheme.

The key findings of the report were:

- Of the 102 companies analysed, 55 provided defined benefit schemes to directors, 16 had defined contribution schemes, and 31 companies provided both types of scheme. The total number of directors covered by the survey is 375, the majority of whom are in DB schemes. Several directors participated in both types of scheme.
- The total value of the directors' pensions analysed – expressed as the sum of all the transfer values available – is £891 million.
- The average transfer value for a director's pension is just over £3 million. For those directors with the biggest entitlements at each company, the average transfer value is £5.3 million.
- The average accrued pension was £193,000p.a. whilst the average accrued entitlement for the director with the highest pension in each company was £320,000p.a.
- For those directors in DC schemes, the average company contribution was £86,000, and the typical contribution rate was around 20%. The average received by those with the highest contribution in each company was £147,000.
- The majority of directors were able to retire on a full pension at age 60.
- At least 20 companies announced changes to their staff pension schemes during the last year, whether closing their DB scheme, changing the benefit arrangements for new and/or existing members, or increasing member contributions.

On the basis of these findings, the TUC is calling for greater clarity and reporting on pensions, in line with the disclosures required on pay, bonuses and other benefits for senior executives. More detailed information, particularly on accrual rates and contribution rates, should be provided by companies in order for investors to scrutinise more effectively the awards made to directors. In addition, companies should make clear any differential treatment for directors. The TUC recommends that directors and employees should be members of the same schemes, on the same terms.

2. Introduction

There is an increasing interest in the large remuneration packages awarded to executive directors, although the spotlight has generally fallen on pay and bonuses. Pensions are an important part of executive pay and benefits packages but can also be the most opaque element, with limited information available in the public realm. The TUC maintains that pensions should be subject to the same level of scrutiny as other parts of directors' benefits packages.

The TUC launched PensionsWatch in 2003 in order to track the pensions of directors and staff at the top firms in the UK. The central aim of the project is to give an insight into pensions provision at some of the biggest companies, with an emphasis on directors' benefits. The project focuses on establishing the nature and level of pensions provision made available to directors, and examining whether there are elements of differential treatment for directors and other employees.

The PensionsWatch database is compiled by examining the annual reports of top UK companies, drawn from the FTSE100 and a number of the other biggest employers in the country. This means that the sample changes slightly from year to year, but should provide a useful overall sense of the pensions landscape at the top companies. This year's study looked at 102 companies, gathering information on the pensions of 375 directors. The combined value of all the directors' pensions surveyed (calculated by looking at the sum of all the transfer values) is £891 million.

The most recent company reports have been used, which generally cover the calendar year 2006 or financial year 2006-7. The level of detail given in the reports varies, but most summarise the accrued annual pensions and transfer values for each director in DB schemes, or contributions in that year for DC schemes. Some reports also include information on the accrual rates, contribution rates and retirement ages for directors, although many do not. For employees, most reports set out the type of scheme and recent changes, although in many cases this information is complex, unclear and multi-layered due to successive changes.

3. What's on offer? – types of scheme

Of the 102 companies analysed, 55 provided defined benefit (DB) schemes to directors, 16 had defined contribution (DC) schemes, and 31 companies provided both types of scheme. Some directors participate in a combination of DB and DC schemes, often depending on when they joined the company, but the clear majority (79%) of directors in the survey were in DB schemes.

There is a clear trend, documented in previous PensionsWatch surveys, towards the closure of defined benefit schemes to new entrants. These are generally replaced by defined contribution schemes. Whilst this often affects directors and employees, some companies have separate arrangements for senior directors.

Our survey found that 59 companies had closed their employee defined benefit schemes or defined benefit sections of their pension schemes in previous years or during the period covered by their financial report. During the period covered by PensionsWatch, eight companies reported that they have or will be closing some or all of their defined benefit provision to new entrants, including for example Royal Bank of Scotland, Friends Provident and Vodafone. Some of the changes have been negotiated with unions and others imposed.

A small number of companies announced changes to their defined benefit provision for new staff entrants and in some cases existing scheme members, but have retained defined benefit provision in another form such as a career average scheme.

A number of companies gave information on changes to their pension benefits or contributions during the latest financial year for existing and new staff members. These include BAE systems; British Airways; Corus; Diageo; Friends Provident; HBOS and Marks and Spencer.

4. What is it worth? - values of entitlements and transfers

The remuneration reports produced as part of company annual reports give varying amounts of information on director pensions. For defined benefit (DB) schemes, the reports list the transfer value of the pension and the accrued pension payable. Some reports also give details of directors' accrual rates and normal pension age, although many do not. For defined contribution (DC) schemes, some reports outline the contribution rates and the contributions made by the company in the past year.

4.1 Transfer values

The transfer value of a pension is the amount, calculated by actuaries, which would be paid from one pension scheme to another if a director moved all their accrued benefits. PensionsWatch found that the total transfer value of all the DB directors' pensions studied was £891 million.

The table below shows the five largest single transfer values at the companies examined by PensionsWatch.

Company	Highest Transfer Value £
BP ¹	21,700,000
Compass Group ²	15,760,000
Vodafone ³	15,186,500
National Grid ⁴	12,714,000
Unilever*	12,526,000

*Converted from Euro

The average transfer value for a director's pension is just over £3 million. For those directors with the biggest entitlements at each company, the average transfer value is £5.3 million. This compares to an average of £2.7 million and an average high of £4.9 million in the 2006 PensionsWatch study.

¹ The BP group chief executive retired on 31 July 2007

² The Compass Group annual report states that one director ceased to accrue pension benefits and began to draw his pension from 1 Oct 2005. He commuted part of his pension for a lump sum. The transfer value shows the actuarial position at 30 Sept 2006.

³ According to the Vodafone annual report, one director retired for pensions purposes on 6 April 2006 and took a lump sum of £1,361,601. The figures in the table exclude allowance for this figure. If allowance is included, the transfer value becomes £13,538,000.

⁴ The National Grid annual report states that this director retired on 31 December 2006. The value of the pension as at March 2007, which has increased by an additional £21,000 per annum, reflects compensation for the late payment of benefits to which he was entitled at the start of the year.

4.2 Accrued benefits

Accrued benefits are the amount of pension payable to an individual on retirement, based on their service so far. The highest single pension in this year's PensionsWatch is worth over £1 million per year.

The five highest single accrued pensions are set out in the table below

Company	Highest Accrued Pension £
BP	1,050,000
Royal Bank of Scotland Group	933,000*
Carnival	884,000*
Compass Group	830,000
Cadbury Schweppes	737,000

* Converted from US \$

The average accrued pension for the directors in the sample was £193,000 p.a. Among those directors with the highest accrued pension in each company, the average was £320,000 p.a. Although the sample used is slightly different, this indicates an increase on last year's report, which found an average accrued pension of £168,000 p.a. amongst the directors studied and an average of over £290,000 p.a. for the directors with the highest accrued pension at each company – an increase of 15% and 10% respectively.

These figures compare to an average occupational pension of £146 per week (£7,592 per year)⁵ in the UK. The average director's pension is therefore around 25 times higher than the national average. This gap appears to have widened slightly since last year's PensionsWatch, when the average director pension was 24 times the national average.

4.3 Defined contribution pensions

Increasingly, directors at some of the large companies studied by PensionsWatch are building up pensions in 'money purchase' or defined contribution schemes. Some reports set out the contributions made to these schemes. 96 directors were listed as receiving contributions as part of this type of scheme. The five highest recorded individual contributions are set out in the table below:

Company	DC pension scheme contribution £
Xstrata* ⁶	988,732
Vodafone Group	382,000
Anglo American	354,000

⁵ Pensioners' Income Series 2005/6, page 40 (http://www.dwp.gov.uk/asd/asd6/PI_series_0506.pdf)

⁶ The Xstrata report gives a single figure for pension related payments to directors including pension plan, FURBS and non-pensionable salary supplement payments.

WPP Group	337,000
Reckitt Benckiser	261,000

* Converted from US \$

The average employer contribution to directors in DC pension schemes is £86,000, while the average employer contribution to the director who received the highest payment in each company is £147,000.

5. Calculating directors' pensions

A small number of the company reports examined gave information on the accrual or contribution rates for directors pension schemes. There is currently no requirement on companies to publish this information. The TUC believes that greater transparency in this area would allow for effective scrutiny of the real nature and value of directors pensions and any differential treatment in comparison to other employees. We recommend that companies should be required to publish accrual and contribution rates for directors' and employees' pensions.

5.1 Accrual rate

In a final salary scheme, the accrual rate is the proportion of pay that a person receives as pension for each year that they have been in the scheme. For instance, an accrual rate of $1/60^{\text{th}}$ indicates a pension worth $1/60^{\text{th}}$ of final salary for every year of pensionable service in the scheme.

The table below sets out the accrual rates for directors in the PensionsWatch survey, where the information was provided in the company reports. The most common accrual rate was $1/30^{\text{th}}$, stated by 12 companies. Several others implied a similar accrual rate by stating that a pension of two-thirds of final salary could be achieved after 20 years of service. The next most common rate of accrual was $1/60^{\text{th}}$. Some companies offer different accrual rates to different directors, hence the combinations set out in the table.

Number of Companies	Accrual Rate
9	$1/60^{\text{th}}$
12	$1/30^{\text{th}}$
1	$1/45^{\text{th}}$
3	$1/60^{\text{th}}$ and $1/80^{\text{th}}$
1	$1/60^{\text{th}}$ and $1/30^{\text{th}}$
1	$1/30^{\text{th}}$ and $1/52^{\text{nd}}$
1	$1/37.5^{\text{th}}$ and $1/50^{\text{th}}$

In comparison, government statistics show that in 2006, 60 per cent of active members of private sector DB pension schemes had accrual rates of $1/60^{\text{th}}$. In the public sector, the most common accrual rate (for 93 per cent of active members) was $1/80^{\text{th}}$ or $1/80^{\text{th}}$ plus a lump sum.⁷

⁷ *Occupational Pension Schemes Survey 2006*, page 8
<http://www.statistics.gov.uk/pdffdir/opss0707.pdf>

5.2 DC scheme contribution rates

Increasingly, companies are closing defined benefit schemes in favour of defined contribution schemes for both employees and directors. There is not currently any requirement on companies to set out the contribution rates for directors in DC schemes as part of reporting on executive remuneration. The figures outlined in the table below are taken from those company reports that do publish this information, and show that the contribution rates tend to be generous proportions of executives' salaries. It should be noted that some companies offer different contribution rates for different directors.

Number of directors	Contribution rate
1	5%
6	12%
2	15%
2	25%
6	30%
1	35%

This indicates an average contribution rate of around 20% for the directors covered. Whilst the lack of reporting means that this is a small sample, it does suggest a trend of generous contribution rates. This contrasts with the average employer contribution rate of 5.8% in UK private sector DC schemes in general⁸.

5.3 Normal retirement age

As concerns rise over the long term funding of pensions, many schemes for workers in the public and private sector are moving to a Normal Retirement Age (NRA) of 65. This has been a controversial issue and a point of some debate in the media, with criticism from some in the private sector of the provisions for public sector employees.

PensionsWatch examined the NRA offered to directors in the sample. Many companies do not make this explicit in their reports, but the information provided by a number of companies shows that the most common age by far is 60. Several other companies state an NRA of 65 but allow directors to retire at age 60 on their full pension.

No of Companies	NRA offered to Directors
38	60
6	62
5	65

⁸ *Occupational Pension Schemes Survey 2006*, page 7
<http://www.statistics.gov.uk/pdfdir/opss0707.pdf>

6. Conclusion

PensionsWatch demonstrates the significant pensions packages offered to directors of major companies. The report shows that generous accruals in DB schemes remain the norm for senior directors, the clear majority of whom can look forward to retiring on a full pension at age 60.

On the basis of these findings, the TUC is calling for directors and employees to be members of the same pension schemes, on the same terms. Pensions are not generally performance related, and there is no clear case for differential treatment. Indeed, different arrangements for directors and employees risk undermining good workplace relations. Since directors earn more than their employees and therefore accrue greater pension benefits on the same terms, there cannot be a justification for offering a differential approach.

There should also be greater clarity and reporting on pensions, with a requirement for companies to disclose more detailed information, particularly on accrual rates and contribution rates. This would enable investors to scrutinise more effectively the awards made to directors. In addition, companies should make clear any differential treatment for directors.

Given greater information, shareholders and investors – particularly the large institutional investors such as pension or insurance funds – would be able to scrutinise pensions provision for directors and engage with companies as their shareholders in order to ensure fair and proportionate rewards packages. The TUC's guidance for pension scheme trustees makes specific reference to the scrutiny of directors pensions.

The report also highlights the shift to DC provision in staff schemes. It should be reiterated that the TUC wishes to retain and encourage DB provision. However, where DB is not possible, we would rather employers adopt risk-sharing approaches rather than pure DC pension provision. Therefore where employers would otherwise switch to DC provision, then measures that would encourage them to opt for risk-sharing are to be welcomed.

The TUC's recommendations, drawn from the findings of this report, are:

- Directors and staff should be members of the same schemes, on the same terms.
- There should be fuller reporting on company pensions provision for directors and employees, including the mandatory disclosure of accrual and contribution rates.
- Clearer information on pensions arrangements should be made available to investors.