



# PensionsWatch 2008

Analysing the pensions of top company directors

Produced by PIRC for the TUC

## 1. Executive summary

PensionsWatch was established by the TUC to give a picture of occupational pension provision for top company directors in the UK. The survey data has been gathered from the most recent annual reports of major UK companies.

Workers in the UK are experiencing a trend towards riskier and less generous pensions. Despite this, many directors continue to receive substantial retirement benefits. They tend to accrue pensions at a more generous rate than employees, and the majority are in final salary 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, 51 provided defined benefit schemes to directors, 19 had defined contribution schemes, and a further 23 companies provide both types of pension. A small number of companies report that no pensions are provided for directors.
- The total number of directors covered by the survey is 346, the majority (76 per cent) of whom have DB pensions. Several directors had both types of scheme.
- The total value of the directors' pensions analysed – expressed as the sum of all the transfer values available – is £793 million.
- The average transfer value for a director's pension is £3 million. For those directors with the greatest entitlements at each company, the average transfer value is £5.2 million.
- The average accrued pension was £201,655p.a. whilst the average accrued entitlement for the director with the highest pension in each company was £333,664p.a. This is an increase of over 4 per cent on last year's figures.
- For those directors in DC schemes, the average company contribution was £91,734, and the average contribution rate was around 21 per cent. The average for those with the highest contribution in each company was £149,601.
- The majority of directors were able to retire on a full pension at age 60.
- A number of companies announced changes to 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.

It is vital that investors have the information they need to scrutinise the awards made to directors. The report demonstrates the need for greater clarity in reporting on pensions. More detailed information – particularly on accrual rates and contribution rates – should be provided and companies should make clear any differential treatment for executives and staff. The TUC is calling for directors and employees to be members of the same schemes, on the same terms.

## 2. Introduction

In the debate about executive remuneration, attention has tended to focus on the pay and bonuses that directors receive. Pensions are also an important part of these executive remuneration packages but can 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. Investors need clear information about executive remuneration as a whole, including pensions, in order to effectively scrutinise company pay and benefits policies and hold boards of directors to account.

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 346 directors. The combined value of all the directors' pensions surveyed (calculated by looking at the sum of all the transfer values) is £793 million. The average transfer value was £3 million, consistent with the figures from last year's report.

The most recent company reports have been used, which generally cover the calendar year 2007 or financial year 2007-8. 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, a number of 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, 51 provided defined benefit (DB) pensions to at least some directors, 19 had defined contribution (DC) schemes, and 23 companies provided both types of scheme. In some companies directors participate in a combination of DB and DC schemes. The clear majority (76 per cent) of directors in the survey have DB pensions. Seven companies report that they do not provide pensions to the board, and four of these companies report that they offer a cash payment in lieu of a pension scheme. For two companies information was not available when the research was undertaken.

There is an increasing trend across the sample as a whole towards cash payments in lieu of pensions. These vary in size as a percentage of salary, the highest in the sample being 60 per cent. According to a recent study by consultants Watson Wyatt, the median allowance for a chief executive in a FTSE100 company is 25 per cent of salary.<sup>1</sup> The move by some companies away from providing pensions to directors has also contributed to a drop in the number of directors covered by this report – 346 this year, compared to 375 in 2007.

There is a continuing trend, as 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.

During the period covered by this PensionsWatch report, three companies reported that they have closed some or all of their defined benefit provision to new entrants. **Lonmin** reports that on 30 July 2007 the DB scheme for executives was closed, the staff scheme having closed the previous year. **BG** states that with effect from 2 April 2007 new UK employees have been offered membership of a defined contribution stakeholder pension plan, but the company's annual report does not make clear whether this will also apply to directors. **Legal & General** states that its UK Senior Pension Plan, offered to executives, closed to new members on April 2007.

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. **Centrica** has converted its DB schemes for staff to career average provision and these remain open, whilst it appears that the DB scheme for directors is shut. **Standard Life** now offers career average provision in its closed DB scheme, this also affects the one director in the 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. **ITV** has altered the Normal Retirement Age, the accrual rate and member contributions to its staff scheme.

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<sup>1</sup> <http://www.watsonwyatt.com/europe/news/pressreleases/press.asp?ID=19485>

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

The amount of information given in company reports about directors' pensions varies widely. For defined benefit (DB) schemes, the remuneration reports are required to 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 £793 million.

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

Company	Highest Transfer Value £
BP <sup>2</sup>	21,552,000
Unilever*	15,137,001
Royal Dutch Shell**	13,367,170
Daily Mail	12,903,000
HSBC	12,780,000

\* Converted from Euro

\*\* Converted from US \$

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 £5.2 million. These figures are almost identical to those in the 2007 PensionsWatch study.

##### 4.2 Accrued benefits

Accrued benefits are the amount of pension payable to an individual on retirement, based on their service so far. A small number of directors of the UK's public companies have now entered the million-pound pensions club. The five highest single accrued pensions are set out in the table below.

<sup>2</sup> The BP group chief executive retired on 31 July 2007

Company	Highest Accrued Pension £
National Grid <sup>3</sup>	1,087,000
BP	1,050,000
Royal Bank of Scotland*	1,040,000
Royal Dutch Shell*	887,050
Carnival*	855,825

\* Converted from US \$

The average accrued pension for the directors in the sample was £201,655 p.a. Among those directors with the highest accrued pension in each company, the average was £333,664 p.a. Although the sample used is slightly smaller, these figures show an increase of over 4 per cent on last year's report, which found an average accrued pension of £193,000 p.a. amongst the directors studied and an average of over £320,000 p.a. for the directors with the highest accrued pension at each company.

These figures compare to an average occupational pension of £156 per week (£8,112 per year)<sup>4</sup> in the UK. The average director's pension is therefore around 25 times higher than the national average. This is similar to the figure in last year's PensionsWatch report.

### 4.3 Defined contribution pensions

Directors at some of the companies studied by PensionsWatch are increasingly shifting to building up pensions in 'money purchase' or defined contribution schemes. Some reports set out the contributions made to these schemes. 90 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*	1,646,411
WPP	400,000
SABMiller	285,000
Reckitt Benckiser	271,000
Anglo American	270,000

\* Converted from US \$

<sup>3</sup> A footnote to the company's disclosure on directors' pensions states: "[The director] joined the Board on 25 September 2007. In accordance with the buy out of his contractual severance arrangements, a payment of £4,769,306 (£3,232,670 net of excise tax) was made on 10 January 2008. This amount reflected the present value of the change in his SERP benefit and is additional to the benefits shown in the table.

<sup>4</sup> *Pensioners' Income Series 2006/7*, page 42 ([http://www.dwp.gov.uk/asd/asd6/PI\\_series\\_0607.pdf](http://www.dwp.gov.uk/asd/asd6/PI_series_0607.pdf))

The average employer contribution to directors in DC pension schemes is £91,734 (an increase from £86,000 in 2007), while the average employer contribution to the director who received the highest payment in each company is £149,601 (up from £147,000 last year).

## 5. Calculating directors' pensions

There is currently no requirement on companies to publish information about the accrual rates and contribution rates for directors' schemes, which determine how their pension entitlements are calculated. A small number of the company reports examined do include this information, and the TUC believes that this should be encouraged in order to provide greater transparency for investors and other stakeholders. Clear reporting of these factors would enable 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 13 companies. The next most common rate of accrual was  $1/60^{\text{th}}$ . Some companies offer different accrual rates to different directors.

Number of Companies	Accrual Rate
1	$1/80^{\text{th}}$
9	$1/60^{\text{th}}$
1	$1/54^{\text{th}}$
1	$1/52^{\text{nd}}$
1	$1/45^{\text{th}}$
1	$1/40^{\text{th}}$
13	$1/30^{\text{th}}$

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.<sup>5</sup>

<sup>5</sup> *Occupational Pension Schemes Survey 2006*, page 8  
<http://www.statistics.gov.uk/pdfdir/opss0707.pdf>

## 5.2 DC scheme contribution rates

Companies are increasingly 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. Most company contributions appear to be paid into a company-sponsored DC scheme, but some contributions are paid to directors to fund pension personal pension plans. It should also be noted that a number of companies offer different contribution rates for different directors.

Number of directors	Contribution rate
7	5%
2	8%
3	10%
1	12%
4	12.5%
6	15%
2	16%
6	20%
1	23%
16	25%
10	30%
1	33%
1	35%
1	40%
1	50%
1	55%

This indicates an average (mean) contribution rate of around 21 per cent for the directors covered (the median is 23 per cent). 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 6.4 percent (in open

schemes) to 7 percent (in closed schemes) in UK private sector DC schemes in general<sup>6</sup>.

### 5.3 Normal retirement age

With concerns growing over the long term funding of pensions, many schemes for workers in the public and private sectors are increasing the length of time people must work by moving to a Normal Retirement Age (NRA) of 65.

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. The next most common NRA is 65. Again a small number of companies have differing retirement ages for directors.

No of Companies	NRA offered to Directors
26	60
4	62
1	63
9	65

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<sup>6</sup> *Occupational Pension Schemes Survey 2007*, page 4  
<http://www.statistics.gov.uk/pdfdir/opss0708.pdf>

## 6. Case study - the financial sector

Given the turmoil in the financial markets and industries over the past year, attention has increasingly turned to executive remuneration in the sector. Investors need clear information in order to hold directors to account and ensure that rewards are clearly tied to good results. These rewards include the pension packages available to directors alongside pay and bonuses.

Companies in the finance sector make up just under a fifth of the sample in this year's PensionsWatch report, ranging from banks, to insurers, to investment-related companies. Of the 19 companies analysed, all but one report that at least one director has a DB pension entitlement. This is a higher proportion than for the sample as a whole.

Companies in this sector disclose little information about accrual or contribution rates for directors. Of the four companies disclosing an accrual rate, three state that it is 1/60ths. The other operates two accrual rates – 1/30ths and 1/40ths.

Four companies disclose information about contribution rates to DC schemes but these vary dramatically. One company offers the highest contribution rates disclosed in the sample – 55 per cent and 53 per cent. These contributions are paid to the directors concerned to fund personal pension arrangements. At the other end of the spectrum one company offers directors a 5 per cent contribution. One company offers a contribution of 15 per cent. The final company offers a normal contribution of 10 per cent, but will match director contributions up to a further 7 per cent.

Of the seven companies in the sector disclosing a Normal Retirement Age, five state that it is 60, one that it is 65, and one provides different NRAs to different directors (two have the NRA of 65, one has the NRA of 60).

Finally, it is notable that one of these companies explicitly states that it may provide a new employee with a final salary pension despite having recently closed its scheme. The company states that such an exception might be made if this will aid recruitment:

“The Company has reserved the right, in exceptional circumstances, to provide final salary benefits in respect of employees who were not members of the pension scheme prior to 1 July 2007. It is intended that this provision will only be used where there is a need to recruit or retain specific skills.”

## 6. Conclusion

Once again, PensionsWatch shows the substantial pensions packages offered to directors of major companies. The clear majority of directors can look forward to retiring on a full pension at age 60, accrued on generous terms in a final salary scheme.

In response to these findings, the TUC recommends that:

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

Pensions do not tend to be related to performance, and there is no clear case for differential treatment. Since directors earn more than their employees and therefore accrue greater pension benefits even when they have the same terms, a differential approach can rarely be justified. Indeed, different arrangements for directors and employees risk undermining good workplace relations.

There should also be greater clarity and reporting on pensions in general, with a requirement for companies to disclose more detailed information, particularly on the accrual rates and contribution rates that determine how pension savings build up. This should cover the pensions for directors and for employee schemes, making clear any changes to schemes or differential treatment for directors.

Shareholders – particularly the large institutional investors such as pension funds or insurance companies – could use this improved disclosure to scrutinise pensions provision for directors in the way that they are already increasingly scrutinising pay and bonuses. Investors can then use the information as part of their engagement with companies in order to ensure fair and proportionate rewards packages.