TUC

PensionsWatch 2013

A TUC Report on directors' pensions in the UK's top companies

Executive summary

1.1 The TUC established PensionsWatch in 2003 in order to give a picture of occupational pensions in the UK's largest public companies, with a focus on the pension provision for top company directors. The survey draws information from the most recent annual reports on the pension provisions for staff and directors at a number of major UK companies.

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

1.3 There is also an increasing trend towards providing cash payments for directors in lieu of a pension. Even in the few years that such payments have become common, they have increased significantly in value, and as a percentage of salary. Directors and employees are now worlds apart in terms of both pay and pensions and the increasingly generous nature of DC contributions and cash payments for directors means that this divide can be expected to grow further.

1.4 The key findings of this year's survey report were:

1.5 Of the 100 companies analysed, 46 provided defined benefit schemes to directors, though in a number of cases there is no further accrual taking place, 41 had defined contribution schemes, and 11 companies provided both types of scheme. One company offers a hybrid. The total number of directors covered by the survey is 294 of whom 39% have at least some DB pension entitlement, whilst almost 32% have DC provision. Several directors participated in both types of scheme. There has been a further growth in the provision of cash in lieu of pension for directors.

1.6 The total value of the directors' DB pensions analysed – expressed as the sum of all the transfer values available – is approximately £500 million.

1.7 The average transfer value for a director's pension is £4.73 million. For those directors with the biggest entitlements at each company, the average transfer value is £6.30 million.

1.8 The average accrued pension was £259,947 p.a. whilst the average accrued entitlement for the director with the highest pension in each company was £330,932 p.a.

1.9 For those directors in DC schemes, the average company contribution was £160,380, and the average contribution rate was around 23%. The average received by those with the highest contribution in each company was £202, 760.

1.10 For directors receiving cash payments the average was £169,679. The average employer cash contribution to the director who received the highest payment in each company is £224,936. The average level of payment as a percentage of salary was 29%.

1.11 Both the average DC contribution rate and the average cash in lieu payment, expressed as a percentage of salary, have grown in recent years. Companies are becoming more generous in their provision to directors in this area of executive reward.

1.12 The majority of directors with DB entitlements were able to retire on a full pension at age 60.

1.13 The 2013 PensionsWatch report confirms the picture of previous years of an 'upstairs downstairs' approach to pension provision in the UK's biggest companies. In addition to earning significantly more than other employees, many directors have also benefited from preferential treatment in retirement provision: better accrual or contribution rates than those available to employees, or, increasingly, large cash payments in lieu of a pension.

1.14 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 to enable more effective scrutiny more of 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.

Introduction

1.15 In 2003 the TUC initiated PensionsWatch as a way of monitoring pension provision in the UK's biggest companies, with a particular focus on directors. During this period there has been a significant change in the nature of pension provision in most companies, with defined benefit (DB) schemes, usually final salary-related, being replaced by defined contribution plans (DC).

1.16 For ordinary employees, in most cases where companies have shifted from DB to DC provision they have unfortunately also taken the opportunity to cut back the level of their pension contribution. According to figures from the Office for National Statistics, in 2011 the average employer contribution to an occupational DC scheme was 6.6%, compared to 14.2% for DB schemes.[1] In fact, this almost certainly underestimates the gap between directors and others, as the ONS figures refer to trust-based DC schemes. Contribution rates in contract-based DC schemes, which are the most common, are significantly lower.

1.17 Directors have also seen the nature of their pensions change, but they remain extremely generous in most cases. In 2003, in our first report, we found more than two thirds of companies were still providing DB pensions to at least some directors (though in some cases these schemes were closed to new members). In 2013, for the first time, under half of companies now have directors who have some DB entitlement. The fall in the proportion of directors with any DB entitlement has been sharper. By 2012 we had reached the point where no longer a majority of directors in the sample had any DB provision. This year we found 39% of directors had some DB entitlement, though not accruing further benefits in some cases, and we expect this figure to fall further in future.

1.18 Over the same period DC provision for directors initially grew in importance, as it did for other employees. However, the proportion of directors in the survey who have DC provision is lower this year than last. This appears to reflect the fact a growing number of directors are being provided with cash payments in lieu of pension. In the case of both DC provision and cash in lieu the value of the company contribution, as a percentage of salary, can be very significant and has been rising. As such, while the shift from DB is evident among directors' pensions, it is not associated with declining generosity of provision as it is for ordinary workers. Companies are becoming more generous towards directors.

1.19 A clear theme throughout the years in which we have produced the report has been the differential nature of pension provision. In addition to earning significantly more than other employees, inevitably making their pensions proportionately larger, many directors have also benefited from preferential treatment. When DB schemes were the norm, many directors were offered rapid

[1] ONS Occupational Pension Scheme Survey 2011, available at. http://www.ons.gov.uk/ons/dcp171778_279435.pdf

accrual rates, with 1/30ths common. In a DC environment, directors benefit from company contribution rates several times those available to most employees.

1.20 This 'upstairs downstairs' aspect of private sector pension provision has remained a constant throughout the period in which the TUC has been publishing PensionsWatch. Despite the TUC's call for a more equitable approach to pension provision, there have been no significant moves to address this issue. It is possible that there will be improved disclosure under the Government's new remuneration reporting rules, discussed in the conclusion. This might encourage investors to challenge such arrangements, something most have been unwilling to do to date.

1.21 In the meantime it seems likely that the pensions divide in the private sector will continue, and increasing DC contributions and cash in lieu payments may even make it worse.

The type of schemes on offer

1.22 Of the 98 companies where data was available, 46% continue to provide defined benefit schemes for at least some directors, though in many cases this reflects an historical accrued benefit with no further accrual taking place. The number providing defined contribution schemes is 42%. Overall 39% (117) of the 294 directors covered by the survey are members of DB pension schemes, with almost 32% (83) members of DC pension schemes. Some directors are members of both types of scheme, for example as a result of shifting from one type of scheme to another (meaning no further benefits accruing in the previous scheme).

1.23 The provision of cash payments as part of pension packages is an increasing trend across the sample as a whole. Recently there appears to have been a particular shift away from DC towards to cash payments. The majority of payments are made to directors who do not wish to participate in company schemes, though they may be put towards a personal pension, and some take the form of 'cash supplements' to other provision. Overall 61companies made cash payments to at least one director. This suggests a worrying lack of faith among directors in the type of pension products that the vast majority of workers will be enrolled into in the future.

1.24 Overall, the picture of a fundamentally different model of pension provision is clear. There has been a significant drop in the proportion of companies providing a DB pension to any director, from 70.5% in 2003 to 46% in 2013. The proportion of directors for whom an accrued DB entitlement is disclosed has dropped even further, from just under 80% in 2003 to 39% in 2013.

Changes to schemes

1.25 A number of the annual reports analyzed in this year's report make disclosures in respect of changes to group pension policy, with more evidence of the disappearance of DB provision.

1.26 **Kingfisher Plc's** final salary defined benefit pension plan closed to new members on the 30th of June 2012. The trend towards closing to future accrual is also evident. **Associated British foods Plc** closed its DB pension scheme to future accrual on the 15th of September 2012 and opened up a defined contribution scheme. **Schroders** reports that its DB scheme, closed to future accrual on 30 April 2011, had no active members as of 31 December 2011.

1.27 Companies switching from DB to DC take different approaches. **Experian Plc** closed its DB scheme to new members; no directors currently accrue a pension within the DB scheme and as of 2012 the company operates a defined contribution scheme for its entire workforce but with a contribution rate of 20% for its directors. Other companies offer comparable rates for all eligible employees and the board. **Easyjet Plc** has closed its defined benefit scheme to its directors and has offered the same basic 7% contribution rate to its DC scheme for both its employees and members of the board.

1.28 There is also some evidence of companies shifting towards cash instead of pensions. **Babcock International Group Plc** closed its defined benefit scheme to future members and instead offers a cash supplement in lieu of pensions accrual for new directors. This is in place of a DB scheme that was previously offered to directors before May 2013. **Carnival Corp/Plc** closed its defined benefit scheme to new directors as of 2012, and plans are also in the pipeline for a cash payment in lieu of membership of a pension scheme.

Defined benefit pensions

Accrued benefits

1.29 Accrued benefits are the amount of pension payable to an individual on retirement, based on their service so far. The average accrued pension for the directors in the sample was £259,947 p.a. Among those directors with the highest accrued pension in each company, the average was £330,932 p.a. These figures compare to an average occupational pension of £201 per week (£10, 452 per year)[2] in the UK. The average director's pension is therefore over 25 times the national average. This is likely to understate the real gap since our research only captures the pensions of directors that are disclosed in annual reports. There will be many directors' pensions in payment which are very large but which are no longer publicly disclosed by the sponsoring company.

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

Top 5 Accrued Pensions

Company	Accrued Pension £	Director
Carnival Corp/Plc	1,230,584	A.Kirk Lanterman
AstraZeneca Plc	1,000,000	David Brennan
BAE Systems Plc	892,405	Linda Hudson
Royal Dutch Shell Plc	882,770	Peter Voser
BP Plc	854,452	Dr Byron Grote

Transfer values

1.30 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 £500 million. The average transfer value for a director's pension is just over £4.73 million. For those directors with the biggest entitlements at each company, the average transfer value is £6.30 million.

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

Top 5 Transfer Values

[2] *Pensioners' Income Series 2011/12*, page 47, available at http://research.dwp.gov.uk/asd/asd6/2010_11/pi_series_1011.pdf

Company	Transfer Value £	Director
BG Group Plc	22,242,000	Frank Chapman
Diageo Plc	19,179,000	Paul Walsh
Royal Dutch Shell Plc	17,402,396	Malcolm Brinded
AstraZeneca Plc	14,776,000	David Brennan
BP Plc	13,888,551	Robert Dudley

Accrual rates

1.32 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 1/60th indicates a pension worth 1/60th 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 rates was 1/60th. In previous years we have found 1/30th to be the most common, so this year's results may reflect the retirement of some directors on rapid accrual rates and/or changes in scheme design. The number of unusual accrual rates (such as 1/40th and 1/45th)

Number of directors	Accrual Rate
1.33 12	1.34 1/60th
1.35 1	1.36 1/56nd
1.37 1	1.38 1/54th
1.39 6	1.40 1/45th
1.41 6	1.42 1/40th
1.43 1	1.44 1/37th
1.45 4	1.46 1/36th
1.47 7	1.48 1/30th

found this year suggests that there may indeed have been some scheme changes. In addition, disclosure of accrual rates continues to be very limited, so the information we have been able to record may not provide a full picture of the extent of rapid accrual rates.

Normal retirement age

1.49 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 or higher. PensionsWatch examined the NRA offered to directors in the sample. Many companies do not make this explicit in their reports, but, as in previous years, the information which is provided shows that the most common age by far is 60. The next most common NRA is 62. A small number of companies have differing retirement ages for directors.

No of directors	NRA offered to Directors
53	60
15	62
11	65

Defined contribution schemes

Contributions to DC schemes

1.50 A significant number of directors at 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. 83 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. The average employer contribution to directors in DC pension schemes is £160,380, an increase of 11% on last year, while the average employer contribution to the director who received the highest payment in each company is £202,760.

Top 5 DC Contributions

Company	Contributions £	Director
WPP Plc	586,000	Sir Martin Sorrell
Lloyds Banking Group Plc	549,000	António Horta-Osório
BHP Billiton Group	541,974	Marius Kloppers
RIO TINTO GROUP	424,000	Sam Walsh
SABMILLER PLC	388,500	Graham Mackay

1.51 The average contribution for directors continues to rise and this probably reflects two underlying trends. The first is the continuing growth in executive salaries. Whilst base pay has become a less important element of executive remuneration, relative to bonuses and share awards, it has still grown at a healthy rate. Any increase in base pay will automatically boost a pension contribution calculated as a percentage of salary. At the same time there has been a noticeable increase in the average contribution rate paid by companies into directors' DC pensions, which is explored further below. A combination of these factors has accelerated the growth in average DC contributions.

DC scheme contribution rates

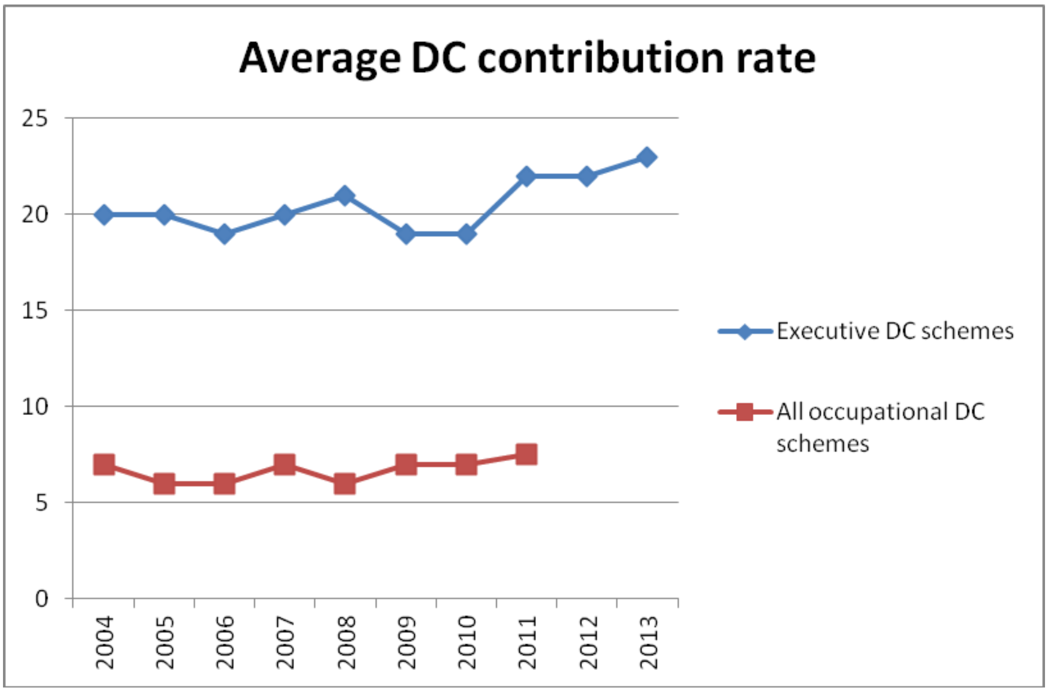
1.52 There is not currently any requirement on companies to set out the contribution rates for directors in DC schemes as part of reporting on executive remuneration. The figures outlined in the table below are taken from those company reports that do publish this information, and show that the contribution rates tend to be generous proportions of directors' salaries. Most company contributions appear to be paid into a company-sponsored DC scheme, but some contributions go into directors' 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
4	5%
2	7%
4	8%
1	10%
1	11%
1	12%
1	15%
1	16%
3	20%
15	25%
2	28%
13	30%
2	31%
2	34%
2	35%
2	36%
1	38%
1	40%
1	45%
1	50%

1.53 The figures collected for this year's report produce an average contribution rate of around 24% for the directors covered. Looking at the ten-year trend in contribution rates, we can see that the average has risen steadily over time. We need to be cautious of reading too much into the early figures as the number of companies both offering a DC scheme to directors and disclosing a contribution rate was relatively small. Nonetheless there is a clear upwards trend, and this is confirmed by another recent analysis of FTSE100 executive pensions.[3]

1.54 In comparison, the average contribution to all DC schemes is less than a third of that offered to directors. It is currently 6.6% according to the ONS[4], and the figure has remained around the 6% over the long-term.[5] As noted earlier, this probably underestimates the gap between contribution rates for directors and those offered to other employees, given the low contributions paid to contract-based based DC schemes. For example, 2012 data from the Annual Survey of Hours and Earnings shows that almost 30% of DC contract-based scheme members have an employer contribution below 4%, and a further 40% have contribution between 4 and 8%.[6] In trust-based DC, 13% have an employer contribution below 4% and 29% have between 4 and 8%. This issue will be explored further in the forthcoming TUC Pension Scorecard 2013.

1.55 We also note that the most LCP report finds four companies – Admiral, Capita, easyJet and Hargreaves Lansdown – which explicitly state that they offer DC pensions to their executives on the same terms as other employees. However such an approach is rare.



[3] Lane Clark and Peacock's 2011 and 2013 executive pension surveys found that the median employer contribution has increased from 20% in 2009 to 22% in 2011 and to 25% in 2013.
[4] ONS Occupational Pension Scheme Survey 2011. http://www.ons.gov.uk/ons/dcp171778_279435.pdf
[5] For example the NAPF Annual Survey 2002 found an average employer DC contribution of 6%.
[6] Data available at http://www.ons.gov.uk/ons/rel/ashe/annual-survey-of-hours-and-earnings-pension-tables/2012-provisional-results/index.html

Cash payments

1.56 As we have noted in previous surveys, a growing number of directors are being provided with cash payments in lieu of, or in some case in addition to, pension provision. The average payment of this type found in this year's research is £169,679 while the average employer cash contribution to the director who received the highest payment in each company is £224,936.

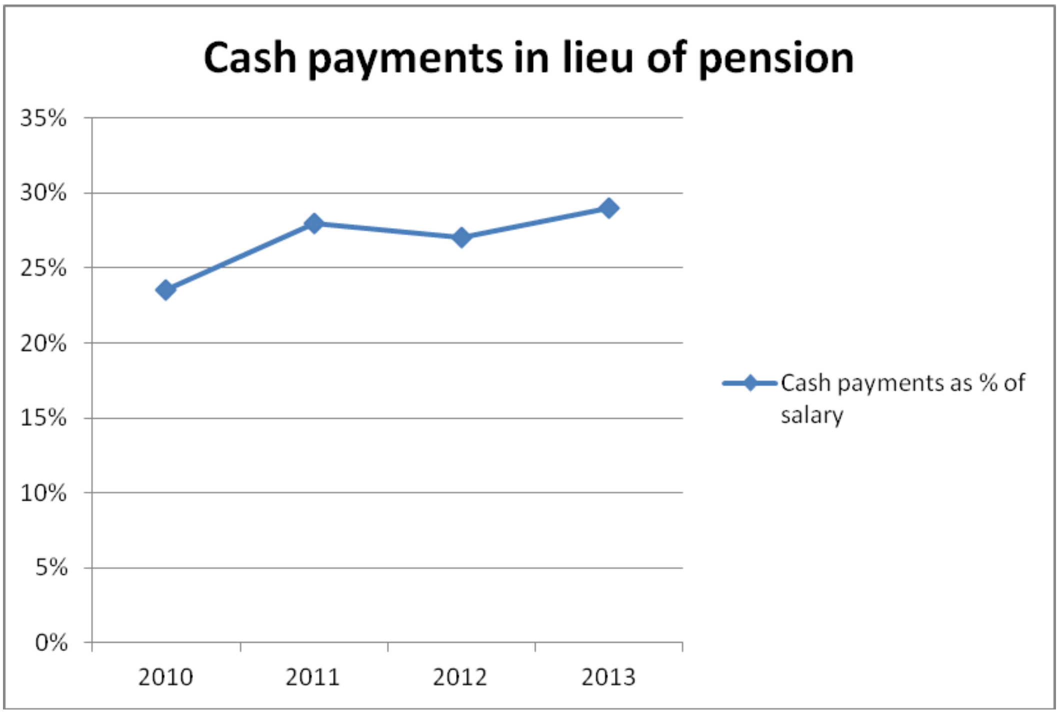
1.57 The five highest recorded individual payments are set out in the table below.

Top 5 Cash payments

Company	Cash payments £	Director
CRH Plc	799,778	Myles Lee
HSBC Holdings Plc	750,000	DJ Flint
HSBC Holdings Plc	625,000	ST Gulliver
Royal Bank of Scotland Group	420,000	Stephen Hester
Royal Bank of Scotland Group	408,000	Bruce Van Saun

1.58 The average level of payment as a percentage of salary was 29%. This corresponds with a median contribution of 30% found by Lane Clark & Peacock in their most recent analysis of directors' pensions.[7] In common with DC contribution rates, the average cash payment as a percentage of salary has been rising over time, with no obvious justification. As LCP put it "30% is the new 25%".[8] It seems that the ratcheting-up effect of peer group comparisons has an effect in this area, as more and more companies settle on 30% as the 'magic number' for a cash in lieu payment simply because others are doing so. Given that directors' base salaries are likely to be rising too this inflation in payments in lieu will inevitably push up the average payment, as a cash figure, more rapidly.

[7] *LCP FTSE100 Executive Pension Survey 2013* , available at http://www.lcp.uk.com/news--publications/news/2013/pa/executive-pensions-survey-2013/.
[8] LCP press release, 8th July 2013, available at http://www.lcp.uk.com/news--publications/news/2013/pa/executive-pensions-survey-2013/


Cash payments in lieu of pension
35%
30%
25%
20%
15%
10%
5%
0%
2010
2011
2012
2013
Cash payments as % of salary

Conclusion

1.59 PensionsWatch continues to demonstrate that the pensions packages provided to directors of major companies are often offered on preferential terms. Whilst the DB to DC shift has affected directors almost as much as other employees, they have been compensated with very large DC contributions or payments in lieu of salary. Where directors continue to build up DB pensions, many benefit from rapid accrual rates and the large majority can look forward to retiring on a full pension at age 60.

1.60 This year's survey provides evidence of growing generosity on the part of companies towards directors who not in DB schemes. As a percentage of salary, both the average contribution rate and the average cash payment in lieu of pension continue to rise. Our findings are confirmed by other research on executive pension provision. Yet company contributions to employees' pensions have not seen similar growth. Although there are examples of companies stating that employees are offered the same terms these are rare, and it is clear that in the large majority of cases directors benefit from much more generous arrangements.

1.61 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.

1.62 Reporting could also be improved. The Government has introduced a statutory instrument, which will come into force from 1st October, which is intended to enhance executive remuneration reporting as part of its broader policy work in this area. This does not explicitly require disclosure of some of the information that the TUC believes should be reported, such as accrual rates.[9] However the Government's consultation on the new regulations provided a mock-up of a company's disclosure which suggested that accrual rates would be disclosed[10], and there has previously been pressure from some investors for such disclosure.[11] Guidance on reporting under the new regulations is expected soon, so it is possible that this issue will yet be dealt with.

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[9] The Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013, available at http://www.legislation.gov.uk/ukdsi/2013/9780111100318/schedule

[10] See 'Pension' section of Annex A, page 40, available at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/31358/12-888-directors-pay-consultation-remuneration-reporting.pdf

[11] See NAPF and LAPFF joint letter on directors' pensions, available at http://www.napf.co.uk/PressCentre/Press_releases/0024_061510_Investors_want_greater_transparency_0610.aspx