TUC

PensionsWatch 2010

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

Executive summary

1.1 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 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. They tend to accrue pensions at a more generous rate than employees, and the majority are still in final salary or other defined benefit (DB) schemes. Those in defined contribution (DC) schemes receive company contributions that are well above the average for ordinary employees in these types of scheme.

1.3 The key findings of the report were:

- Of the 102 companies analysed, 63.5% continue to provide defined benefit schemes to at least some directors whilst 48% provide defined contribution schemes.
- The total number of directors covered by the survey is 329. Many are members of more than one scheme. The majority of directors (54%) are members of DB pension schemes, whilst 31% are members of DC pension schemes. 31% of directors received cash payments either in lieu of participation in a company scheme or as top-ups. 7.6% of directors received payments to personal pension plans.

Defined benefit schemes:

- For directors having DB pensions, the total value – expressed as the sum of all the transfer values available – is £677 million. This figure is down £33 million on last year.
- The average transfer value for a director's pension is £3.8 million. For those directors with the biggest entitlements at each company, the average transfer value is £5.26 million.
- The average accrued pension was £227,726 p.a. whilst the average accrued entitlement for the director with the highest pension in each company was £298,503 p.a. The average occupational pension entitlement for the population as whole is £8,736 p.a. The average director's pension is therefore 26 times higher than the national average.
- The most common accrual rate for directors disclosed by companies is 1/30ths.
- The most common Normal Retirement Age for directors disclosed by companies is 60.

Defined contribution schemes:

- For those directors in DC schemes, the average company contribution was £134,760, and the average company contribution rate was 19%, about 3 times the rate typically available to employees. The average contribution received by those individual directors with the highest contribution in each company was

£185,446.

Cash payments:

- For directors receiving cash payments, typically in lieu of a pension, the average payment was £120,906. The average level of payment as a percentage of salary was 23.5%, the median was 25%. The average payment in lieu to the director who received the highest payment at each company was £166,006.

Staff schemes:

- A number of companies announced changes to their staff pension schemes during the last year, whether closing their DB scheme or changing the benefit arrangements for existing members.

1.4 On the basis of these findings, the TUC is reiterating its call 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, contribution rates, and arrangements relating to payments in lieu of contributions, 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. This could be addressed as part of the BIS review of narrative reporting. The TUC recommends that directors and employees should be members of the same schemes, on the same terms.

Introduction

2.1 There is an increasing interest in the large remuneration packages awarded to executive directors, although the spotlight has generally fallen on salaries 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 believes that pensions should be subject to the same level of scrutiny as other parts of directors' benefits packages.

2.2 The case of the enhanced pension authorised by the board of RBS for departing chief executive Fed Goodwin demonstrates both the enormous value of many directors' retirement provisions, and the lack of scrutiny paid to them by many investors. The option for RBS to award an unreduced early pension was disclosed in its annual report prior to the award to Fred Goodwin[1], and appears to conflict with the Association of British Insurers' guidelines on pay[2], yet it apparently went unchallenged by shareholders.

2.3 However, it does appear that some investors have woken up to the issues around executive pension provision. In July 2010 the National Association of

[1] "The RBS Fund rules allow all members who retire early at the request of their employer to receive a pension based on accrued service with no discount applied for early retirement." RBS Annual Report 2008

[2] "Pensions paid on early retirement should be subject to abatement." *Executive Remuneration – ABI Guidelines On Policies And Practices*, guidance point 2.3. http://www.ivis.co.uk/ExecutiveRemuneration.aspx

Pension Funds (NAPF) and Local Authority Pension Fund Forum (LAPFF) sent a joint letter to the chairs of the UK's major public companies calling on them to improve the quality of their reporting.[3] The areas in which improved disclosure is sought by the NAPF and LAPFF, such as accrual and contribution rates and payments in lieu, mirror a number of the concerns raised by the TUC in recent years.

2.4 Looking ahead, there is an opportunity for the Government to improve disclosure of directors' pensions by amending the current reporting requirements. BIS is currently consulting on the future of narrative reporting. The consultation includes questions about disclosure in respect of remuneration. This would seem to be an ideal opportunity for the Government to address the current gaps in the disclosure regime relating to boardroom pensions.

2.5 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 pension 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.

2.6 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 329 directors. The combined value of all the directors' DB pensions surveyed (calculated by looking at the sum of all the transfer values) is £677 million.

2.7 The most recent company reports have been used. 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, or otherwise indicate the award of payments in lieu of pension contributions. Many reports fail to include information on the accrual rates, contribution rates or retirement ages for directors, although some do. 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.

What's on offer? – types of scheme

3.1 Of the 102 companies analysed, 66 (63.5%) continue to provide defined benefit schemes for at least some directors; the number providing defined contribution schemes is 49 (48%). The majority (54%) of the 329 directors

[3] http://www.napf.co.uk/DocumentArchive/Press%20Releases/00_2010/20100615_15-06-2010%20Investors%20Want%20Greater%20Transparency%20On%20Boardroom%20Pensions.pdf

covered by the survey are members of DB pension schemes, with 31% members of DC pension schemes. Some are members of both, either as a result of shifting from one type of scheme to another (meaning no further benefits accruing in the previous scheme) or because additional provision is offered to offset tax liabilities.

3.2 The provision of cash payments as part of pension packages is an increasing trend across the sample as a whole. 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. Overall 42 companies made cash payments to at least one director. In addition 15 companies made payments towards directors' personal pensions.

3.3 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.

3.4 A number of the annual reports analysed in this year's report make disclosures in respect of changes to group pension policy, including scheme closures. Capital Shopping Centres states that its DB scheme was closed in December 2009. Compass Group also states that it closed a scheme before September 2009.

3.5 Other companies continue to make changes to benefits. W M Morrison states that from 5 October 2009, the basis of future pension accrual in its pension scheme changed from final salary to career average. Royal & SunAlliance states that it made a number of changes to changes to its UK defined benefit schemes in February 2010. These included reducing the future rate of pension accrual from 60ths to a choice of 80ths or 100ths; increasing the level of existing employee contributions; reducing the cap on pensionable earnings to £75,000 and raising the schemes' retirement age from 62 to 65.

What is it worth? Values of entitlements and transfers

4.1 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 are required to list the transfer value of the pension and the accrued pension payable. Many reports fail to provide details of directors' accrual rates and normal pension age, although some do. For defined contribution (DC) schemes, some reports outline the contribution rates and the contributions made by the company in the past year.

Transfer values

4.2 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 £677 million. This is over £33m lower than the equivalent value last year. Given that the average transfer value of a director's DB entitlement is broadly similar to last year, the drop in the total figure is most likely attributable to a fall in numbers of directors participating in DB schemes over the period.

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

Company	Highest Transfer Value £	Director
Royal Dutch Shell	21,122,000	Jeroen van der Veer
HSBC	19,119,000	Stephen Green
Barclays	17,015,000	John Varley
Tesco	15,924,000	Sir Terry Leahy
BG Group	14,018,000	Frank Chapman

4.4 The average transfer value for a director's pension is £3.8 million. For those directors with the biggest entitlements at each company, the average transfer value is £5.26 million.

Accrued benefits

4.5 Accrued benefits are the amount of pension payable to an individual on retirement, based on their service so far. The five highest single accrued pensions are set out in the table below.

Company	Highest Accrued Pension pa £	Director
Royal Dutch Shell	1,359,000	Jeroen van der Veer
Carnival	1,233,951	A. Kirk Lanterman
Astrazeneca	915,000	David Brennan
Tesco	832,000	Sir Terry Leahy
HSBC	711,000	Stephen Green

4.6 The average accrued pension for the directors in the sample was £227,726 p.a. Among those directors with the highest accrued pension in each company, the average was £298,503 p.a. These figures compare to an average occupational pension of £168 per week (£8,736 per year)[4] in the UK. The average director's pension is therefore 26 times higher than the national average.

[4] *Pensioners' Income Series 2008/9*, page 41 (http://research.dwp.gov.uk/asd/asd6/PI_series_0809.pdf)

Defined contribution pensions

4.7 Increasingly, directors are building up pensions in 'money purchase' or defined contribution schemes. Some reports set out the contributions made to these schemes. 102 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	Company contribution £	% of quoted salary	Director
Xstrata	2,027,745	160	Mick Davis
Pearson	623,700	66	Marjorie Scardino
Barclays	596,568	54	John Varley
WPP	401,000	40	Sir Martin Sorrell
Anglo American	331,000	30	Cynthia Carroll

4.8 The average employer contribution to directors in DC pension schemes is £134,760, while the average employer contribution to the director who received the highest payment in each company is £185,446.

Cash payments

4.9 For directors not wishing to participate in sanctioned company pension schemes, equivalent cash payments in lieu are often made. In total 104 directors received cash payments. The five highest recorded individual payments are set out in the table below:

Company	Highest cash payments £	% of quoted salary	Director
Royal Bank of Scotland	420,000	34	Stephen Hester
Compass Group	308,000	35	Richard Cousins
Marks & Spencer	304,000	27	Sir Stuart Rose
Vodafone	292,000	30	Vittorio Colao
British Land	280,000	35	Chris Grigg

4.10 The average payment is £120,906, while the average employer cash contribution to the director who received the highest payment in each company is £166,006. The average level of payment as a percentage of salary was 23.5%, the median was 25%.

4.11 In addition some reports indicated that payments were made towards directors' personal pension schemes. In total 25 received payments towards personal pension schemes. The average payment towards a personal pension was £181,072, whilst the average of the highest payments at each company was £210,740.

4.12 More generally, the move by an increasing number of companies to provide cash instead of a pension, or to fund a personal pension, is likely to have an impact on company reporting. In some cases these types of payments may be rolled in with other 'emoluments', making them harder to detect. This may result in the number of directors being covered in any review of executive retirement provision shrinking.

Calculating directors' pensions

5.1 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 although, as noted in the introduction, some investors are seeking more 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 with other employees. We recommend that companies should be required to publish accrual and contribution rates for directors' and employees' pensions.

Accrual rate

5.2 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.

5.3 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 1/30th, stated by 16 companies. The next most common rate of accrual was 1/60th. Some companies offer different accrual rates to different directors. By comparison, the most common accrual rates available to employees are typically 1/60ths or 1/80ths.

Number of Companies	Accrual Rate
15	1/30th
1	1/40th
2	1/45th
1	1/50th
1	1/52nd
13	1/60th
1	1/80th

5.4 We believe the lack of clear disclosure in this area disguises the fact that a number of other companies also offer rapid accrual rates to directors.

DC scheme contribution rates

5.5 Increasingly, companies are closing defined benefit schemes in favour of defined contribution schemes for both employees and directors. There is not currently any requirement for 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 as such this does not include a number of directors included in the table in paragraph 4.7. Company disclosures clearly show that the contribution rates tend to be a generous proportion of executives' salaries. It should also be noted that a number of companies offer different contribution rates for different directors.

Number of directors	Contribution rate
2	3%
2	4%
7	5%
1	5.75%
2	6%
7	10%
1	12.5%
1	12.6%
6	15%
1	16%
1	18%

2	20%
2	23%
15	25%
7	30%
1	35.5%
1	38%
1	40%
1	50%
1	60%

5.6 This indicates an average (mean) contribution rate of 19% for the directors covered (the median is also 19%). In comparison, the Association of Consulting Actuaries estimates an average company contribution to DC schemes of 6.7%.[5]

Normal retirement age

5.7 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.

5.8 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. A minority adopt a retirement age between the two.

No of Companies	NRA offered to Directors
31	60
8	62
11	65

Early retirement provisions

5.9 In light of the Fred Goodwin case, early retirement provisions are under increased scrutiny. Indeed, the consultation document issued in July 2009 as part

[5] http://www.aca.org.uk/files/ACA_Pension_trends_report_No.1__-1_September_2009-20090828155500.pdf

of the Walker Review put forward the recommendation that the potential for enhanced benefits to be paid should be disclosed.[6] The recommendation was subsequently reworked to capture other cases whereby contractual terms might be enhanced for a departing executive, and lost any specific focus on pensions.[7]

5.10 Very few companies in the sample provided an explicit reference to early retirement provisions, highlighting the need for improved disclosure. Of the few that do make statements some, like Barclays, say that specific individuals can retire early with an unreduced pension.[8] Others state that an early pension can be provided but may be subject to reduction, indicating remuneration committee discretion may be exercised. A handful of others state that a reduction factor will be applied to pension paid early, with some setting out what that factor is.

Conclusion

6.1 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, if not earlier.

6.2 On the basis of these findings, the TUC is reiterating its call for directors and employees to be members of the same pension schemes, on the same terms. 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. Different arrangements for directors and employees risk undermining good workplace relations.

6.3 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 in relation to employees. Improved disclosure of directors' pensions entitlements could be addressed by the current BIS consultation on narrative reporting, which includes questions on remuneration.

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[6] *"Recommendation 37 The remuneration committee report should state whether any executive board member or senior executive has the right or opportunity to receive enhanced pension benefits beyond those already disclosed and whether the committee has exercised its discretion during the year to enhance pension benefits either generally or for any member of this group."*

[7] *"Recommendation 37 The remuneration committee report should state whether any executive board member or "high end" employee has the right or opportunity to receive enhanced benefits, whether while in continued employment or on termination, resignation, retirement or in the wake of any other event such as a change of control, beyond those already disclosed in the directors' remuneration report and whether the committee has exercised its discretion during the year to enhance such benefits either generally or for any member of this group."*

[8] *"Should John Varley retire at 55, an unreduced pension of 60% of pensionable salary would be provided."*

6.4 Given greater information, shareholders – particularly the large institutional investors such as pension funds or insurance companies – would be better equipped to scrutinise pensions provision for directors and engage with companies 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 notes 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 than pure DC pension provision. Therefore, where employers would otherwise switch to DC provision, 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 pension provision for directors and employees, including mandatory disclosure of accrual and contribution rates.
- Clearer information on pension arrangements should be made available to investors.