

The logo for The Pensions Regulator, featuring the text "The Pensions Regulator" in a purple serif font, followed by a stylized sunburst icon. The text and icon are partially overlaid by several light purple rectangular bars of varying lengths and orientations.

# The Pensions Regulator

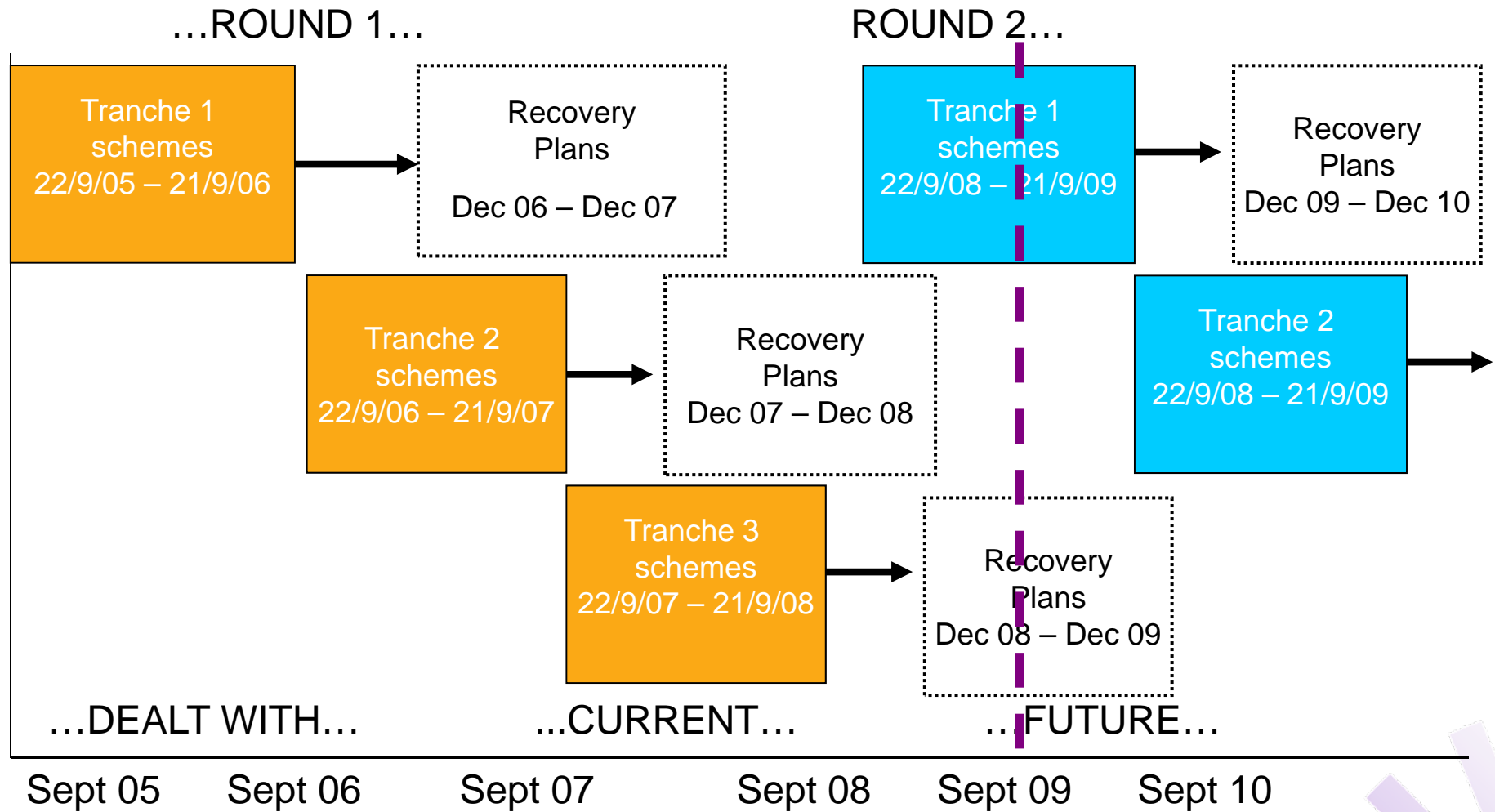
## **A duty of trust**

**Update on regulatory activity and funding principles**

David Hannant  
Risk & Funding  
June 2009

# All schemes must perform a triennial valuation

The process for trustees takes up to 15 months



# Robustness versus flexibility

Technical provisions:

- must be robust;
- need to reflect the situation as it really is, not as we may like it to be.

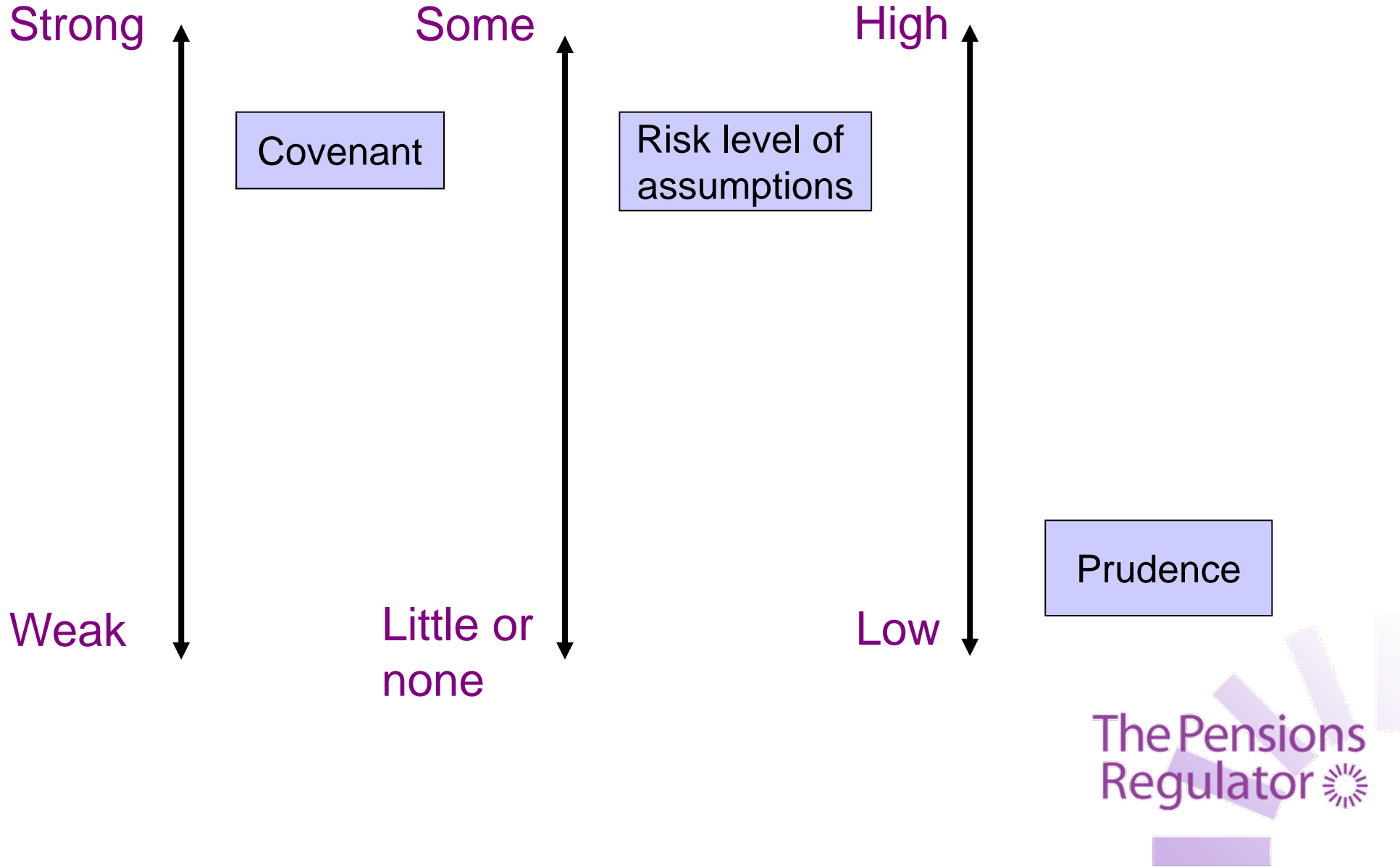
However:

Recovery plans can be flexible if needed.

# Employer covenant

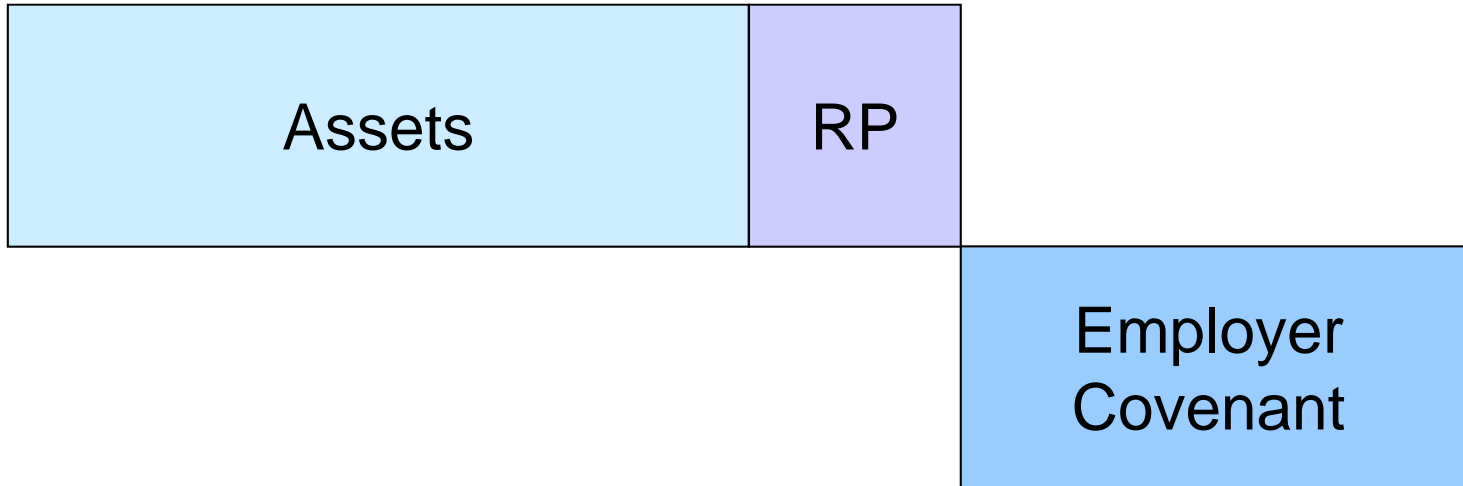
- Employers legal obligation and willingness to support the scheme
- Employer stands behind payments to cover ongoing payments; deficit repair; appropriate scheme expenses and underperformance
- For ongoing funding employer covenant provides security if actual experience is worse than assumed

# Assumptions and employer covenant



# TPs + covenant = self-sufficiency

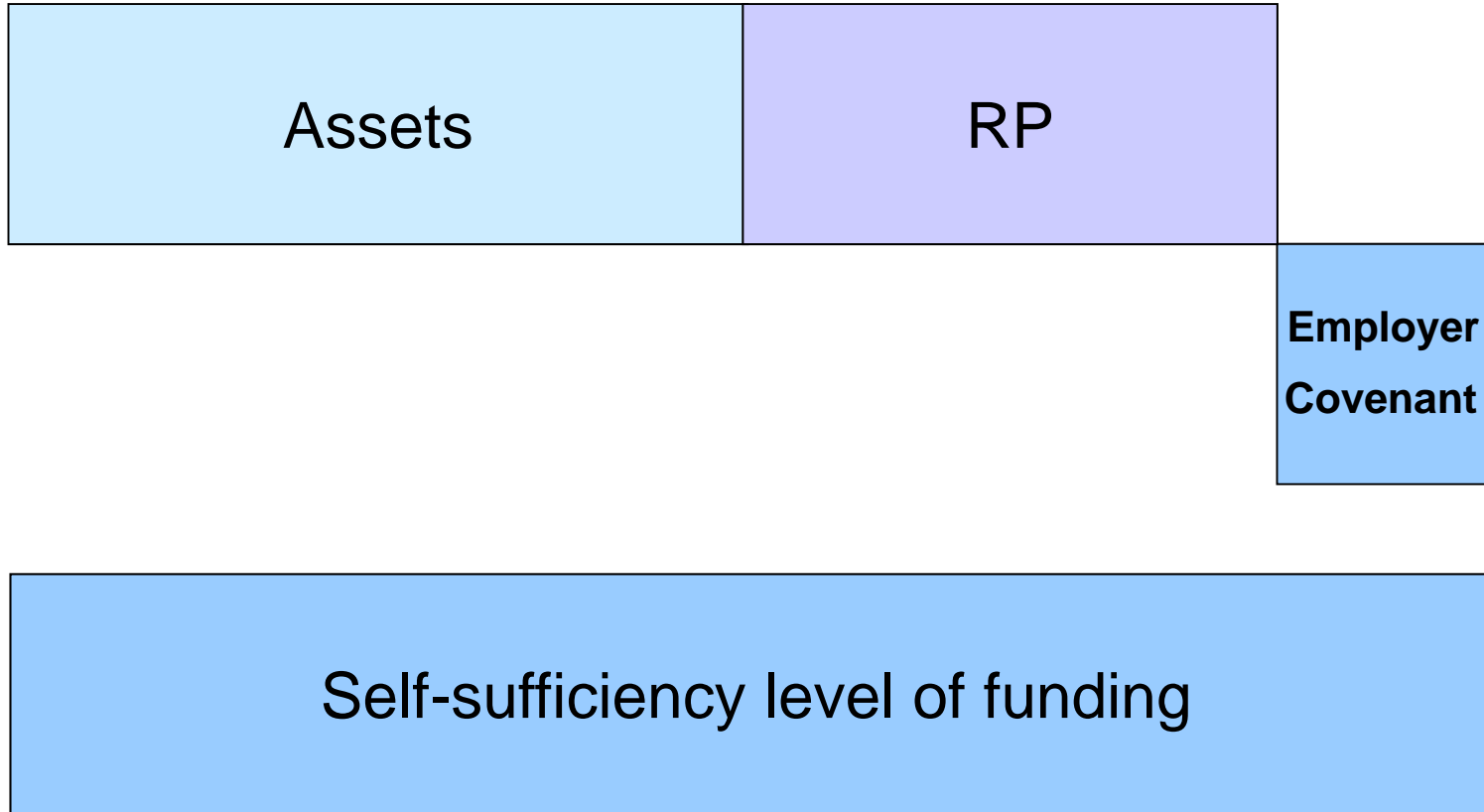
Technical provisions



Self-sufficiency level of funding

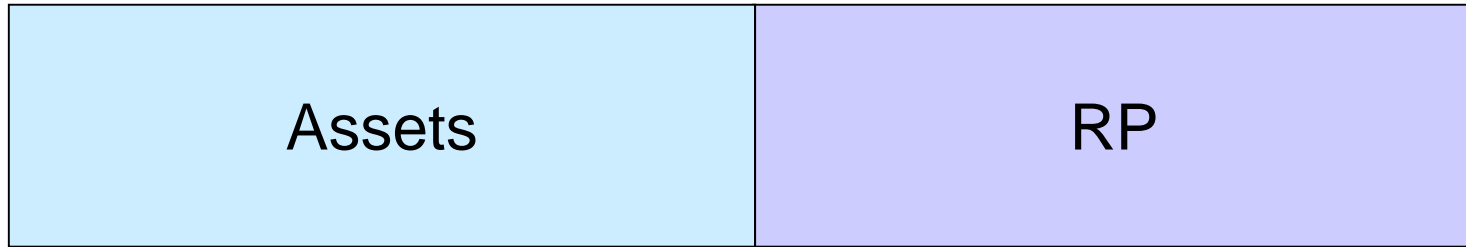
# TPs + covenant = self-sufficiency

Technical provisions

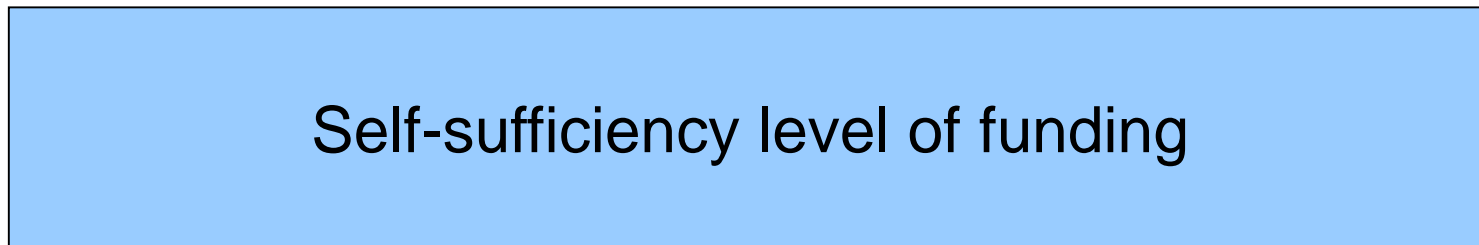


# TPs + covenant = self-sufficiency

Technical provisions



Employer  
Covenant



# What does this look like in figures?

## Past service

Basis	Buyout	Best est.	s179	FRS17	Scheme funding
Assets	38.5	38.5	38.5	38.5	
Liabilities	58.5	37.9	43.9	41.9	
(Deficit)	(20.0)	0.6	(5.4)	(3.4)	?
Funding level	60%	102%	88%	92%	

All figures are in £million

# Assessing covenant

- Trustees and employers need to work together
- Objective independent review is often helpful

Covenant assessment should answer the questions:

- effect of corporate structure and legal obligations to the scheme
- employers ability to meet ongoing demands as they fall due
- the employers ability to stand behind any adverse experience in an on-going situation, including the investment risk taken by the scheme
- scheme's position on insolvency
- options for alternative security, shape of payments

# Flexibility in recovery plans

- Once there is agreement on prudent technical provisions, the recovery plan can be agreed
- Recovery plans should reflect what is possible and reasonably affordable... but members should not be disadvantaged by terms of plan
- However, there is a significant degree of flexibility

# Example of a flexible recovery plan

- Deficit = £14 million
- Company cash-constrained;
  - reasonable expectations of recovery in year 4.
- Payments £1 million yrs 1-4
- Payments £1.5 million yrs 5-8
- Payments £2 million yrs 9-10

In addition:

If company reaches certain triggers e.g. profit of over £1 million a year it will pay 25% profit a year to pension scheme.

# In summary...

- Scheme funding regime flexible enough to cope in the downturn
- Technical provisions must be robust and need to reflect the situation as it really is
- Importance of the employer covenant
- Recovery plans should reflect what is possible and reasonably affordable

# Introducing the case study

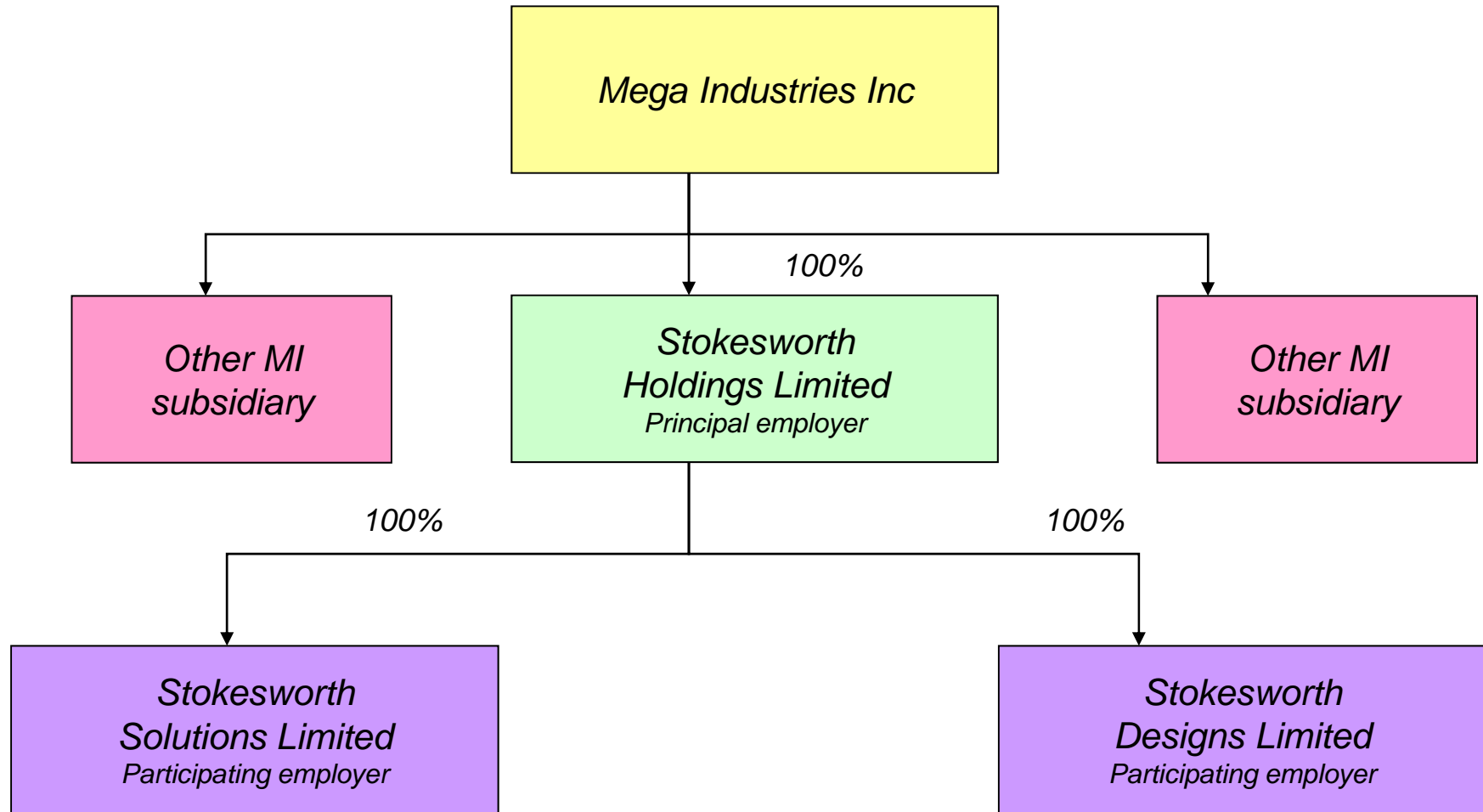
***Stokesworth Holdings Limited***

(and its subsidiaries)

and

***Stokesworth Retirement Benefits Scheme***

# The group

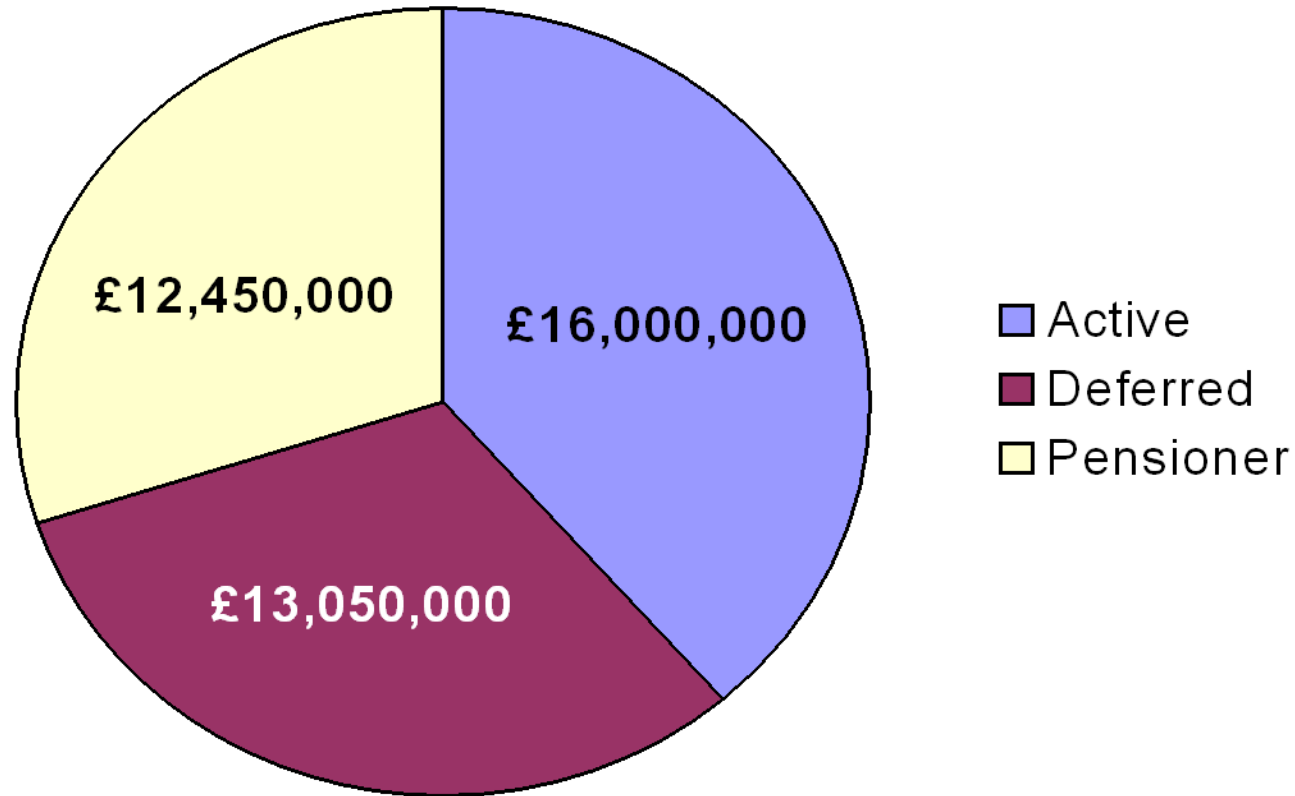


# Stokesworth Retirement Benefits Scheme

- The scheme operates on a conventional final salary basis
- Closed to new entrants in 2003
- Following a review in 2006, future accrual was reduced from 1/60 to 1/80
- Employee contributions of 6% of pay
- Total membership - 591
  - Active - 216
  - Deferred - 232
  - Pensioners - 143
- Scheme assets invested 60% in equities and 40% in bonds

# Stokesworth Retirement Benefits Scheme

Liabilities by membership – 30/09/05 Part 3 valuation

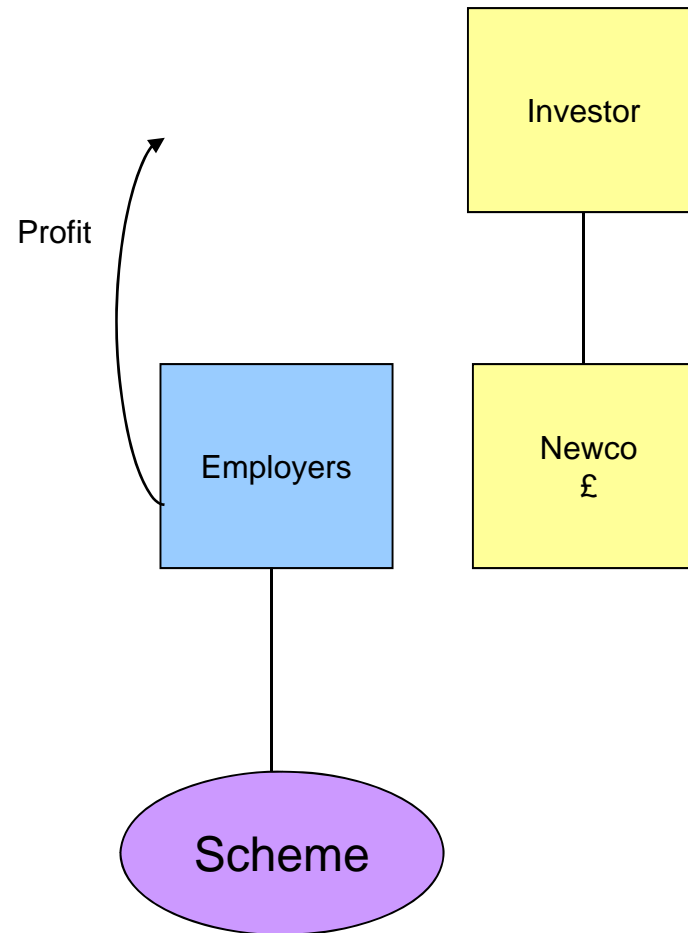


# De-risking solutions suggested

- Buyout of pensioner members' liabilities with an insurer
- Closure of the scheme to future accrual
- Transfer incentive exercise aimed at deferred members
- Pension scheme transferred to a pension specialist sponsoring employer (uninsured buyout)

# Uninsured buyout proposal

- *Newco* substituted for existing employers
- *Newco* has some cash but no business
- Any surplus generated from scheme returned to *Newco* and then as profits to investor



# Buyout vs. Buy-in

- Buyout is where an insurance company takes on assets and liabilities of the defined benefit scheme
- Buy-in is where the scheme buys an insurance policy in respect of members for whom the scheme retains the liabilities. The insurance policy provides a stream of income, just like other scheme investments.

# Breakout

- What are the advantages/risks of these potential solutions?
- What is the trustees' role if any of these de-risking solutions are taken forward?
- What additional information should the trustees look to obtain?

# General discussion / Q & A

The top left of the slide features several overlapping, semi-transparent purple rectangular bars of varying lengths and orientations, creating a layered, abstract graphic effect.

# The Pensions Regulator

**Thank you**