UK PPI roundtable on CDC

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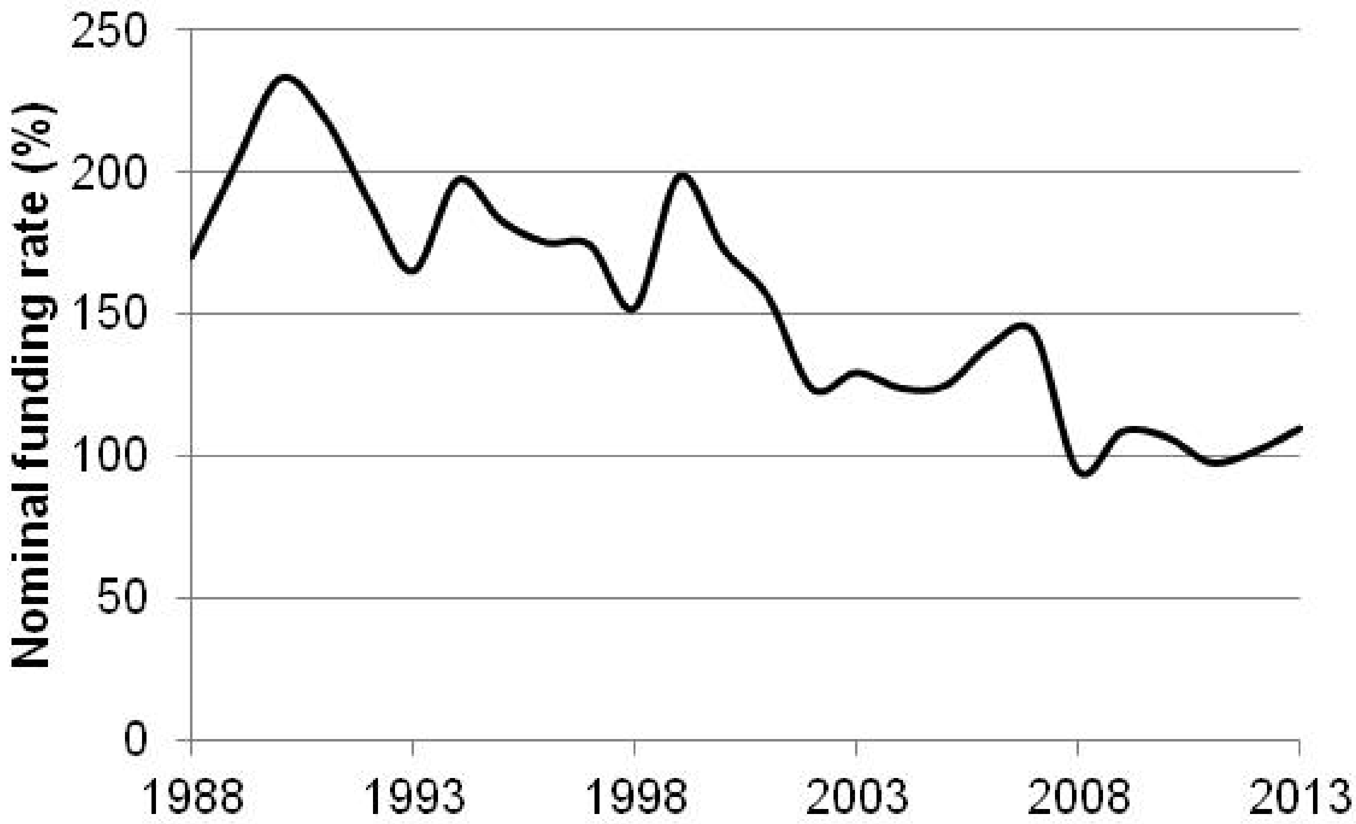
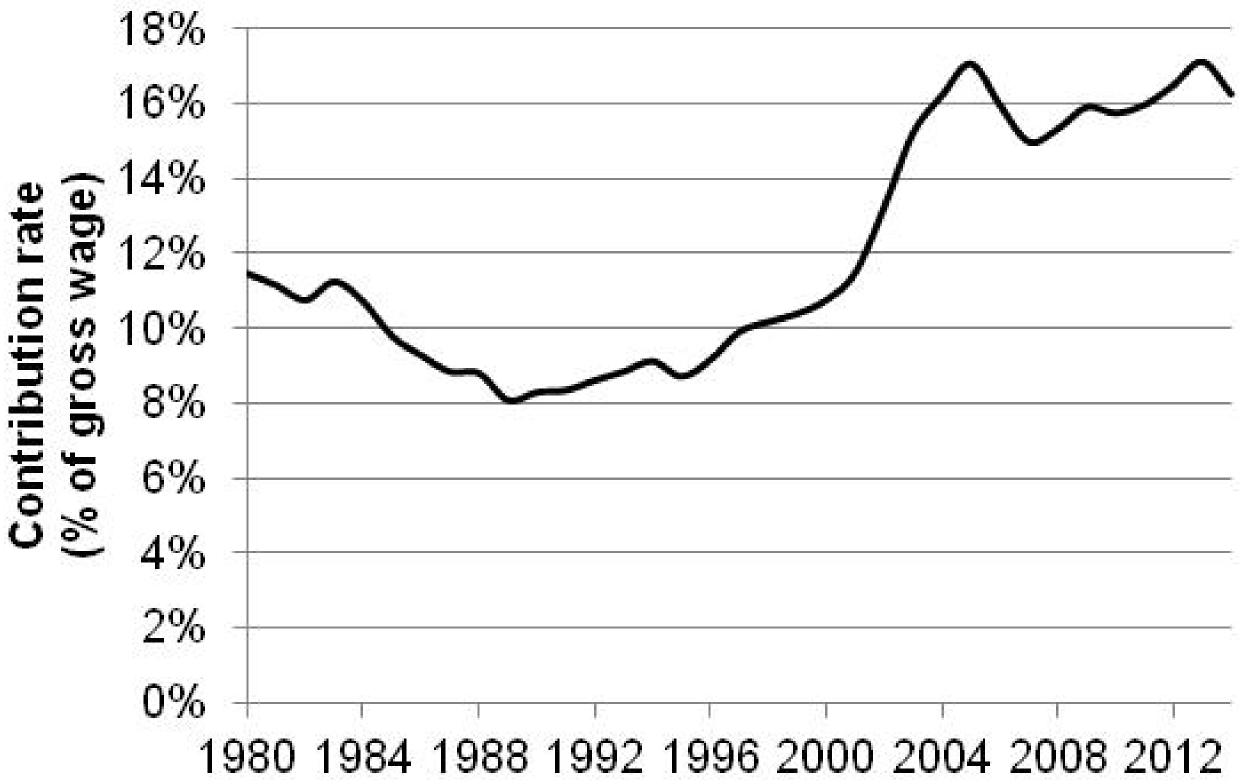
Understanding Society

Increased balance sheet risk due to demographic trends and withdrawal of sponsors…



... and rather high levels of contributions (that cannot stabilize funding rates anymore)…



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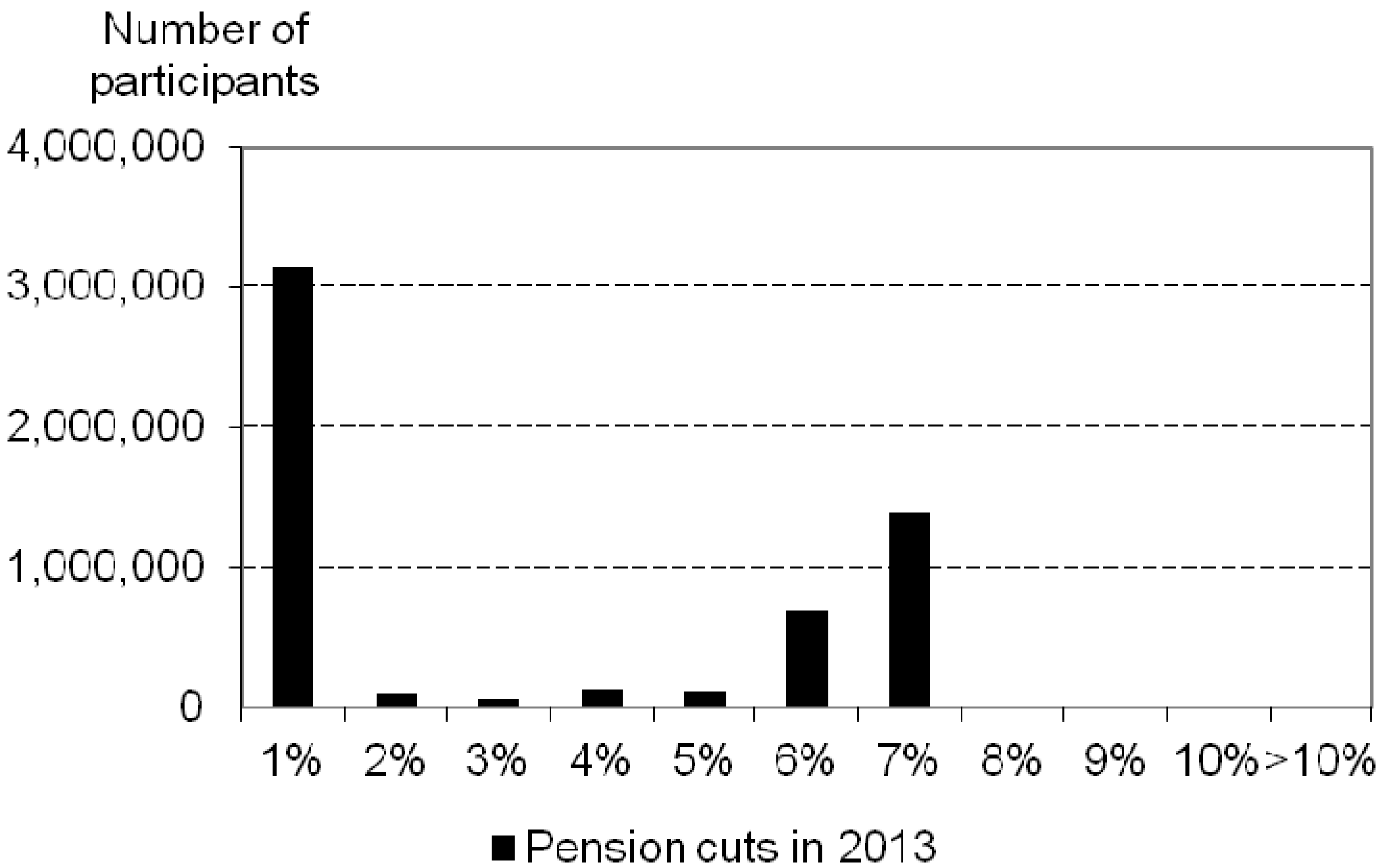
… have resulted in risky pension payments (including cuts in pensions in pay) …



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… and have revealed the weaknesses of Dutch collective pension schemes…

Criteria *	
Weaknesses of Dutch occupational plans **= strengths of “capital frame”**	
Clear risk profiles for communication	✗
Clear risk profiles for investment (tailor-made, age-groups)	✗
Clear ownership rights (complete policies, proper valuation)	✗
Able to accommodate elements of individual choice	✗
Strengths of Dutch occupational plans **= strengths of “annuity frame”**	
Advanced risk management based on lifelong income	✓
Address behavioral and agency problems	✓
Pooling of idiosyncratic longevity risk	✓
Sensible way of dealing with systematic longevity risk	✓

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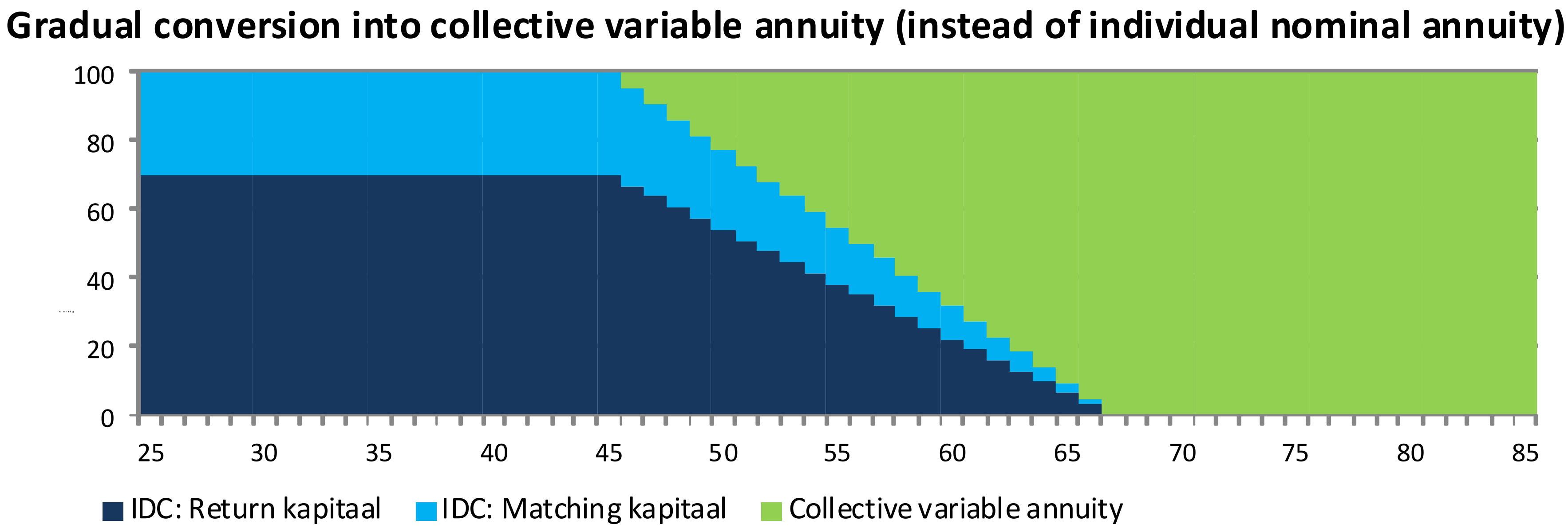
* Bovenberg, Mehlkopf and Nijman: “The promise of Defined-Ambition plans: lessons for the United States”, forthcoming in: R. Shea en O. Mitchell (eds), Reimagining Pensions: the next 40 years, Oxford University Press]

… causing companies to propose new individual DC schemes with collective elements



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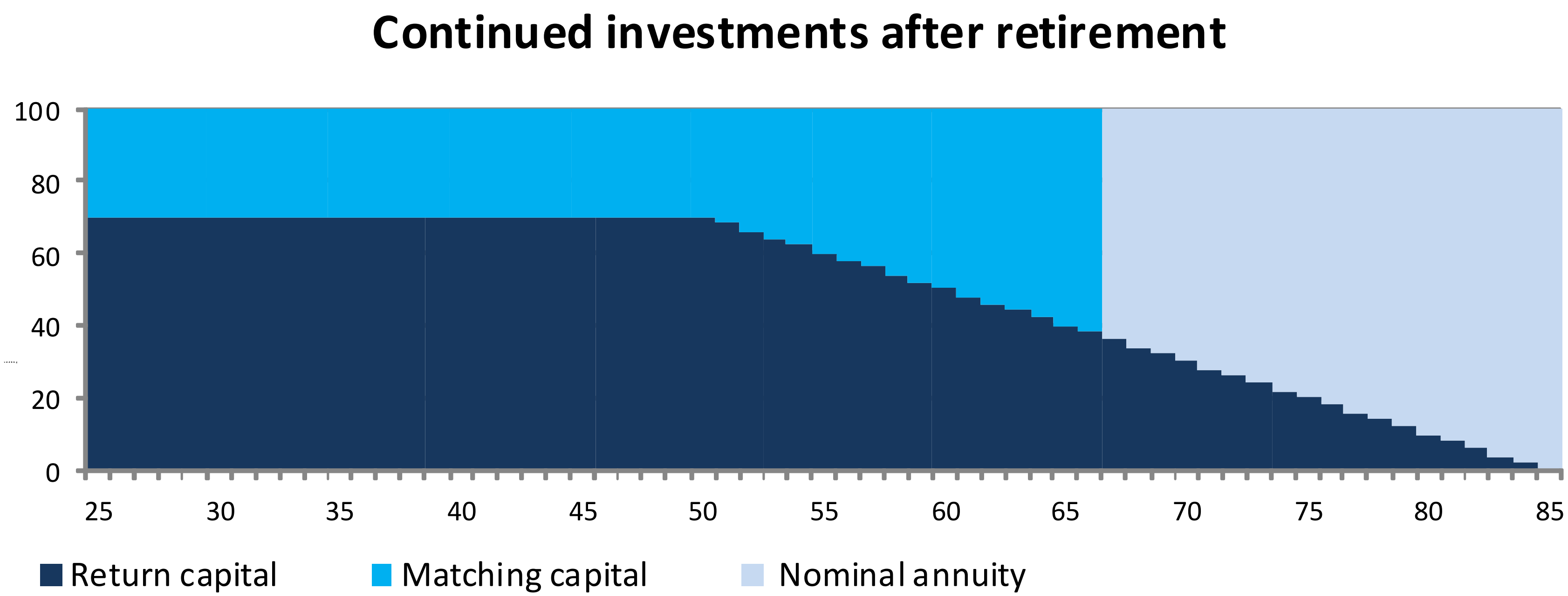
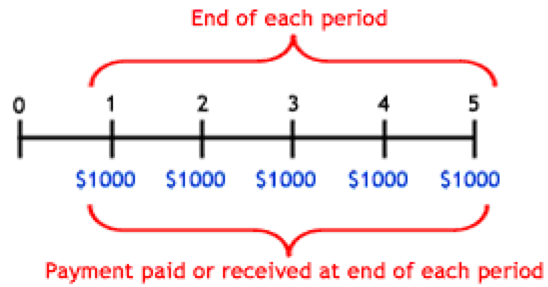
… or individual DC schemes with continued investments after retirement…



... which all aim to combine the best of both worlds…

- New proposals aim to combine the strengths of…

“capital” frame of DC & “annuity” frame of DB



… and require new legislation that should meet the following criteria:

- Individual ownership rights within the collective
  - No shortages surplusses passed onto future members
  - Individual amounts add up to the collective
  - Funding rate equal to 100% at the end of each year
- Symmetric rule for risk sharing based on riskfree rate
  - Ex-ante fair
  - No discretion to boards to redistribute between generations
- Possibilities for participants to choose different provider
- Prevent losses from being shifted (far) into the future
- Restricting the annual volatility of pension outcomes
- ‘Duty of care’ and ‘prudent person’
- Communication that is simple and understandable

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