Indexation of pre-1997 private occupational Defined Benefit pensions: schemes which do not pay increases

- Approximate number of private occupational Defined Benefit (DB) pension schemes in total[1] as at 31 March 2016 is **5,800**.

- It is estimated that **24 per cent** of private occupational DB pension schemes have no indexation applied to pre-1997 benefits[2], as at 1 April 2016.

Scheme size

- Breakdown of schemes with no pre-1997 indexation by scheme size:

No. of members in the scheme	Percentage of all schemes with no pre-97 indexation
1-99	40%
100-499	44%
500-4,999	12%
5,000-10,000	2%
10,000	2%

Table 1. Source: the Pensions Regulator[3].

- On average, smaller schemes are more likely to have no indexation applied to pre-1997 benefits.
  Schemes with no pre-1997 indexation represent
  - 24% of all DB schemes (as mentioned above), but only
  - 14% of members, and
  - 10% of liabilities (measured on a technical provision basis[4]).

Employer size

- TPR's estimates suggest that it is unlikely that the majority of schemes with no pre-1997 indexation are the ones supported by the biggest employers.

- Employers with DB schemes that do not provide pre-1997 indexation employ 15% of all employees working for employers that offer private occupational DB pensions.[5]

[1] Source: the Purple Book 2016 (rounded to the nearest 100).
[2] Source: The Pension Regulator's (tPR) records, based on the information received directly from the schemes in response to the mandatory Annual Scheme Return.
[3] The estimates have been derived from information provided to tPR by Schemes on the Annual Scheme Return. All data is effective as at 01/04/2016, and based upon the Purple Book 2016 DB and Hybrid Scheme population.
[4] Technical Provisions - the actuarial calculation of the liabilities of the scheme.
[5] Where such data is publically available.

- DB members receiving no pre-1997 indexation account for 14% of DB members

Estimated cost of paying increases

- The Government Actuary's Department (GAD) have made an indicative high level estimate of how much it could cost schemes if government changed the legislation to mandate all pre-1997 benefits to be indexed by **CPI capped at 2.5% pa**.

- The estimate is based on data provided by tPR on the proportion of aggregate DB scheme liabilities that relate to schemes which currently have a practice of providing no indexation on pre-1997 excess[6] pension.

- Using this data, GAD estimated that requiring DB schemes to provide pension increases on pre-1997 excess of **at least CPI capped at 2.5%** pa might increase aggregate DB liabilities (measured on a Technical Provisions basis) by around **£15 billion**.

- It is important to note that this is a high level illustrative figure to be treated with caution because of the assumptions and approximations that have been made. The actual figure could be higher or lower given the significant uncertainties involved and the underlying assumptions that had to be made to estimate the cost.[7]

Summary

To require schemes to pay increases to pre-1997 pensions could affect a significant minority of schemes –

- about a quarter of the whole private occupational DB scheme population could potentially be affected

- affected schemes would include many small and very small (less than 100 members) schemes as well as some big ones.

- it could place an additional burden on schemes/sponsoring employers of approximately £15billion (although the figure could be higher or lower depending on the exact level of increase and on how various uncertainties around the assumptions play out in practice.)

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[6] The "excess" is the level of pension in excess of the amount of the Guaranteed Minimum Pension (GMP). The GMP is the amount which is paid in place of the additional State Pension for those people who had contracted out of the additional State Pension and paid lower National Insurance contributions because they were in an occupational pension scheme. GMPs earned between 1978 and 1988 are not increased and those earned between 1988 and 1997 are increased by inflation capped at 3%. Full inflation proofing of the GMP amount for people who reached State Pension age prior to April 2016 is provided through increases to the additional pension. Additional pension, and with it the calculation that provides, in effect, GMP indexation, ended when the new State Pension was introduced from 6 April 2016. However, most people who reach State Pension age after that date will benefit from the transitional arrangements and will do better over their lifetime than under the old arrangements.

[7] Producing a more precise estimate would require a disproportionate level of resources