QUANTUM ADVISORY
The Actuaries and Employee Benefit Consultants

QUANTUM News

Welcome

Our Winter edition of Quantum News is packed full of topical pension issues, aimed at keeping you up-to-date with recent news.

Look out for the following signposts, which will help you find articles most relevant to you:

- DB Specific information for defined benefit (final salary/CARE) pension schemes
- DC Specific information for defined contribution (money purchase) pension schemes
- i General information about employee benefits

Inside this issue

It's a risky business

DB Value at Risk (or VaR) has been around for a number of years, mainly in the confines of investment banking. For people that breathe pensions, VaR is now becoming an acronym. But what is VaR? Why are people talking about VaR? And how can VaR help trustees sleep at night?

VaR was nudged into the spotlight when the Pensions Regulator asked trustees whether their pension schemes had measured it recently. It was a new entry on their scheme return that caused many trustees to pick up the phone to their investment advisers in search of an answer. Pension schemes are now identifying VaR but are measuring it over longer time periods than the banks had traditionally (typically one, three or five years) and by understanding it trustees are not only able to complete one more (currently non obligatory) box on their scheme return, but they can actively demonstrate an understanding of the risk of implementing a certain investment strategy and the potential increase in funding deficit over a period.

VaR can be used to provide an indication of the level of financial risk in a pension scheme and gives a picture of how the world could look if things did not quite go as planned. Given a certain time horizon and probability value, VaR tells an interested onlooker of a potential change in the scheme's deficit arising from certain economic risks. By varying inflation, interest rates and other relevant factors, usually through a 'Monte Carlo' style simulation technique, investment advisers can analyse enough economic scenarios to compute the VaR statistic.

You might hear someone say that your portfolio has a "three-year 5% VaR of £1million". In this case, for every one in 20 economic scenarios, you should expect to see an increase of £1million in your deficit over a three year period. Furthermore, the

individual contributions made to the VaR by interest rate risk, inflation risk, credit risk and other factors can be illustrated to help trustees further understand the strengths and weaknesses of their portfolio.

There are limits to the powers of VaR. One notable limitation lies with the economic scenarios used to calculate it. The scenarios used are ones that could be reasonably expected at the outset, be they neutral, optimistic or pessimistic. A scenario of mass defaulting toxic debts, credit crunches and the countless consequences that followed were not expected in the early 2000's and such unforeseen destruction to funding levels would not be built into this single figure statistic.

Having said that, its simplicity and usefulness cannot be ignored and considering the new requirements for trustees to take an integrated approach to their funding requirements and investment risks, it is yet another useful acronym that trustees need to become accustomed to.

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A decade of reviewing the sponsor covenant – what have we learnt?

Darren Redmayne
Head of Lincoln Pensions

DB While sponsor covenant risk has always existed, the requirement for trustees to properly consider it, alongside other critical risks of a scheme, such as actuarial/funding and investment risks, really began following the creation of the Pensions Regulator (tPR) in April 2005. We are therefore a decade into reviewing the sponsor covenant as part of the triennial valuation process and more broadly, what have we learned over this period?

Trustees increasingly appreciate the need to review covenant and take appropriate advice

Until the arrival of formal covenant analysis there was a working presumption that the employer would always be there to cover funding needs that might arise during a scheme's life. As a consequence of tPR's statutory duty to reduce calls on the Pension Protection Fund, tPR asked trustees to focus on covenant risk. tPR has consistently strengthened (most notably in 2010 and again in 2014) its guidance regarding the importance of assessing covenant risk.

There is a much greater understanding of what sponsor covenant actually means

One reason that schemes and sponsors struggled with covenants in the early days was that there was not a clear definition of what it was or how it could be measured. It was left to practitioners led by firms like Lincoln Pensions and some of the accountants to establish services in this field.

tPR guidance is clearer about both defining and describing covenant. Put simply, covenant strength is a measure of the extent of a sponsor's ability to underwrite the risks of a given defined benefit scheme, being principally actuarial/funding and investment risks. It is not simply about covering a deficit or contributions (common mistakes) – it is about risk capacity.

The 2014 funding code has an even greater focus on covenants:

I. ***The new code places covenant at the heart of risk management*** – covenant assessment is considered one of the three fundamental areas of risk to a scheme. Trustees' advisory budgets are now reflecting this by having a sensible proportion for covenant work. [Para 39]

II. ***Trustees need to justify taking a DIY approach to covenant assessment*** – if trustees elect to assess the employer covenant without independent advice, they need to document why they consider themselves sufficiently equipped, independent and experienced to undertake the work. [Para 57]

III. ***The frequency of covenant assessment and monitoring has been clarified*** – a covenant assessment should be undertaken as part of each actuarial valuation. The assessment should be monitored at least annually. [Paras 63, 86]

IV. ***Factors impacting the amount of 'proportionate' covenant work have been identified*** – the size of the scheme (both absolute and relative to the employer), funding level and complexity are examples of factors that will impact the amount of work required. [Para 20]

V. ***Covenant is defined by tPR in terms of legal obligations and ability*** – over time tPR's definition of covenant has evolved from considering ability and willingness to considering ability and legal obligations. Wider groups are relevant but the focus is on evidencing support with legal commitments. [Paras 61, 67, 73]

VI. ***Clarification of how to consider "affordability" regarding deficit repair contributions*** – deficits should be repaid over an appropriate period in view of the risks of the scheme and the impact on the employer. When analysing affordability, relevant factors including the employer's plans for sustainable growth should be considered. [Para 143]

VII. ***Need to integrate covenant risk assessment into trustee decisions and governance framework*** – covenant, funding and investment decisions interact. Trustees should proportionately monitor key indicators so that they can make timely adjustments. The approach should be embedded within a trustee's governance framework. [Paras 40, 41]

VIII. ***Trustees should perform scenario testing and contingency planning*** – trustees should understand the extent of the scheme's reliance on the employer covenant over time on the basis of a range of plausible future scenarios. Trustees should undertake proportionate planning to address likely adverse outcomes. [Paras 43, 53, 62]

Lincoln Pensions' experience

In addition, based on Lincoln Pensions' practical experience, we would make the following three recommendations to trustees:

- the best time to evaluate the covenant is typically when the trustees do not think there is a need. Any issues can then be addressed outside the pressures of financial stress or corporate activity;
- a good relationship and receipt of relevant information from a sponsoring employer marks the beginning and not the end of a good covenant review process; and
- a covenant review process should be a platform for a collaborative discussion with a sponsoring employer about risk management and not a protracted argument about who is "right". You can have both a strong business (how a sponsoring employer may see it) and a weak covenant (owing to scheme risks beyond the capabilities of the sponsoring employer). Good communication is critical.

Darren Redmayne is Head of Lincoln Pensions, the largest independent sponsor covenant advisor.

Flexible and not so flexible benefits...

DC With effect from 6 April 2015, as part of the new pension flexibilities introduced, individuals no longer have to purchase an annuity with their accrued Defined Contribution (DC) benefits.

This new flexibility is seen as a great step for giving individuals the freedom to decide what to do with their DC benefits in retirement. It was recognised that individuals are given the responsibility to save for their retirement, therefore they should be given the freedom and responsibility to decide how they wish to use their benefits in retirement.

However, what individuals may not realise is that taking their benefits flexibly, especially before State Credit qualifying age, could have consequences when it comes to securing means-tested benefits they may be entitled to in the future.

The Department for Work & Pensions (DWP) has published information on the interaction between flexible benefits and the calculation of certain means-tested benefits, including:

- Employment and Support Allowance (income-related)
- Housing Benefit
- Income Support
- Job Seeker's Allowance (income-based)
- Pension Credit
- Universal Credit

How flexible benefits are treated against the calculation of these means-tested benefits depends on whether an individual has reached their State Credit qualifying age.

If an individual has reached their State Credit qualifying age, any income or cash already taken plus any DC funds yet to be taken for retirement are used when calculating an individuals' entitlement to any means-tested benefits.

If an individual is yet to reach their State Credit qualifying age, any income or cash taken from DC funds are used when calculating entitlement to means-tested benefits, but any DC funds yet to be taken for retirement **are not** included in the calculation.

In order to prevent individuals from hiding their pension provision as a means to ensuring they meet the criteria for certain means-tested benefits, the DWP has launched a **deprivation rule**. If an individual has accessed their benefits flexibly and has been found to deliberately transfer, spend or give their money away in order to qualify for means-tested benefits, the 'deprived' income will be taken into account when determining eligibility.

The same calculation rules explained above are also used when determining how much individuals' can afford to contribute towards the cost of care. Costs for care are due to be capped at £75,000, but with this not coming in until 2017 at the earliest and with many current care costs reaching levels in excess of the cap, the way in which an individual takes their DC benefits flexibly before State Credit qualifying age could seriously affect the amount they may have to pay towards the seemingly increasing cost of care.

It is therefore imperative that individuals obtain guidance, and, where appropriate, advice on taking their benefits flexibly, as there may be unintended consequences of doing so in the future...

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Are we getting the most out of early intervention?

Awareness about health and wellbeing at work has improved greatly in recent years; most employers will have an Employee Assistance Programme (EAP) and those that provide Group Income Protection cover for their staff will most likely be able to benefit from a range of early intervention and support services from their insurer. After all, it is in the interest of both the insurer and employer to help an employee make an early return to work, as the longer an employee is off sick, the harder it is to make any kind of return.

For employers who do not offer Group Income Protection, they may be able to obtain guidance regarding returning employees to work via the Government's Fit for Work service. However, advocating Fit for Work is a difficult thing to do without following up with a number of carefully worded caveats.

Arguably, this is a step in the right direction, however, the elephant in the room, with the tag "presenteeism" stuck firmly on its trunk is at risk of trampling the good work. The cost of presenteeism in the workplace is thought to exceed the cost of sickness absence, which means even more lost performance and productivity, so how does an employer deal with this?

Currently, EAPs have been seen largely as a tick box requirement on the employer's duty of care checklist, and no compulsion has been placed upon an employee to use the services provided. However, in our experience many employees are unaware of the help available from an EAP, resulting in many insurers reporting little use of the facilities provided.

Our lifestyle has changed significantly over the last decade, with economic challenges and developments in technology driving us to do more in less time. This change exists in our personal and professional lives and one of the negative consequences of this change is stress, which is a big contributor to presenteeism.

Stress is a reaction to an event or set of circumstances, and not an actual medical condition. However, considering that the consequences of stress can affect work performance as well as ability to function within society, we need to engage with the help available if we are to deal with this properly.

Dealing with presenteeism requires a number of solutions. For the stress related element we would urge employers to take another look at their EAP, as promoting the help available from this service is an excellent place to start. Remember, an EAP does not require a person to be ill for them to make contact, they provide advice and support on a wide range of common concerns and they usually provide support for an employee's immediate family too.

For employers keen to do more, they could also consider resilience training to help line managers and key personnel recognise stress in themselves and their subordinates and develop suitable coping strategies. Delivering this as a group training session is ideal, as no one individual feels they are participating because their performance is under scrutiny. The coping skills taught are arguably life skills, not just work related ones.

Periodically check your EAP usage statistics with your service provider and look for changes in take up, to ensure that understanding has improved, if usage is non-existent then you know action is required.

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Reduction to Lifetime Allowance

What does this mean for scheme trustees?

The standard Lifetime Allowance (LTA) is being reduced again, this time to £1 million. That's a reduction of 20% from the current level of £1.25 million and 44% from the LTA's peak level of £1.8 million in April 2010. Pension savings in excess of the LTA will be taxed at 25% if they are used to provide a pension or at 55% if they are taken as a lump sum payment. The tax liability will fall due for payment when benefits are taken.

As before, the Government has announced that a form of transitional protection will be made available for those individuals who are, or might be, affected by the reduction of the LTA. Technical details are yet to be confirmed by HMRC at time of writing although it is widely expected that these will mirror the protections available as for 2014.

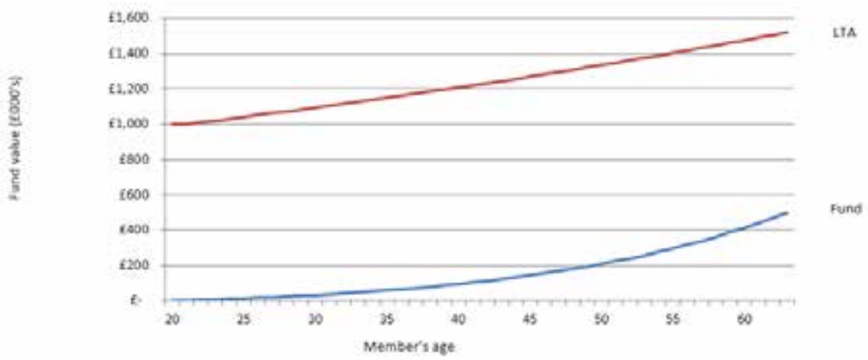
So what does this further erosion of the LTA mean for pension schemes and trustees? Trustees will not ordinarily know if their members are affected by the LTA, unless their pension accruals under the scheme exceed the LTA. Most affected members will breach the LTA as a result of an aggregated value of their current and past pension accruals. Trustees may therefore wish to provide members with generic and member specific information, in so far as it relates to their scheme, to assist members with their retirement planning.

Generic and member specific communications such as trustee newsletters and annual benefit statements present an ideal opportunity to engage with members. Providing information via these channels will prove to be more efficient, in terms of time and cost, than on an ad hoc basis.

A commonly overlooked issue is one of life assurance benefits provided through a scheme's trust structure, written under a registered policy. In the event of death, life assurance benefits insured and paid in this manner are assessable against the LTA. In addition, perils exist for protection holders before death, as participating in a registered group life assurance scheme could result in the loss of a member's Enhanced or Fixed Protection. Consideration should therefore be given to the establishment of an excepted or relevant life assurance policy to address these issues.

A graph comparing the growth of a 20 year old's DC pot against Lifetime Allowance.

Assumes member is earning £20,000 at age 20, paying 10% contributions, salary increases of 3% pa, return on the fund of 5% per annum



The reduction to the LTA is more likely to be an issue for employers rather than trustees. The most likely demographic to be affected, certainly over the short term, will be higher paid management and senior executives with material defined benefit accrual(s). A curtailment, or reduction of pension benefit accrual is likely to necessitate a renegotiation of employment contracts to reflect alternative forms of remuneration, such as higher (non-pensionable) earnings.

A material impact in the defined contribution sphere is likely to occur, if at all, over the longer term (see graph above). Although, admittedly this forecast is reliant upon a number of unknowns such as investment growth, contribution levels and future political fiddling with the LTA.

In summary, trustees will be limited in how they can help members as the LTA encapsulates a wider universe of pension entitlements, not just those accrued under their particular scheme. However, the provision of generic and member specific information will go some way to assist members in making an informed decision with regard to their future retirement planning.

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Why not hedge your bets?

DB Executive summary

Recent publications have been saturated with sensationalised articles predicting the demise of hedge funds and the general inability of such vehicles to outperform versus traditional assets. Surely then, it is only a matter of time before hedge fund investing becomes a bed time story, firmly relegated to the pages of history? At Quantum Advisory, we do not subscribe to this opinion. We believe that hedge funds can be effective in improving risk adjusted returns across the market cycle when held as part of a diversified portfolio.

What is a hedge fund?

The term hedge fund covers a myriad of investment strategies, with no clear definition. In some respects, hedge funds are similar to mutual funds, being composed of a pool of underlying assets and having discretion for the manager to invest in a variety of securities. However, unlike mutual funds, hedge funds:

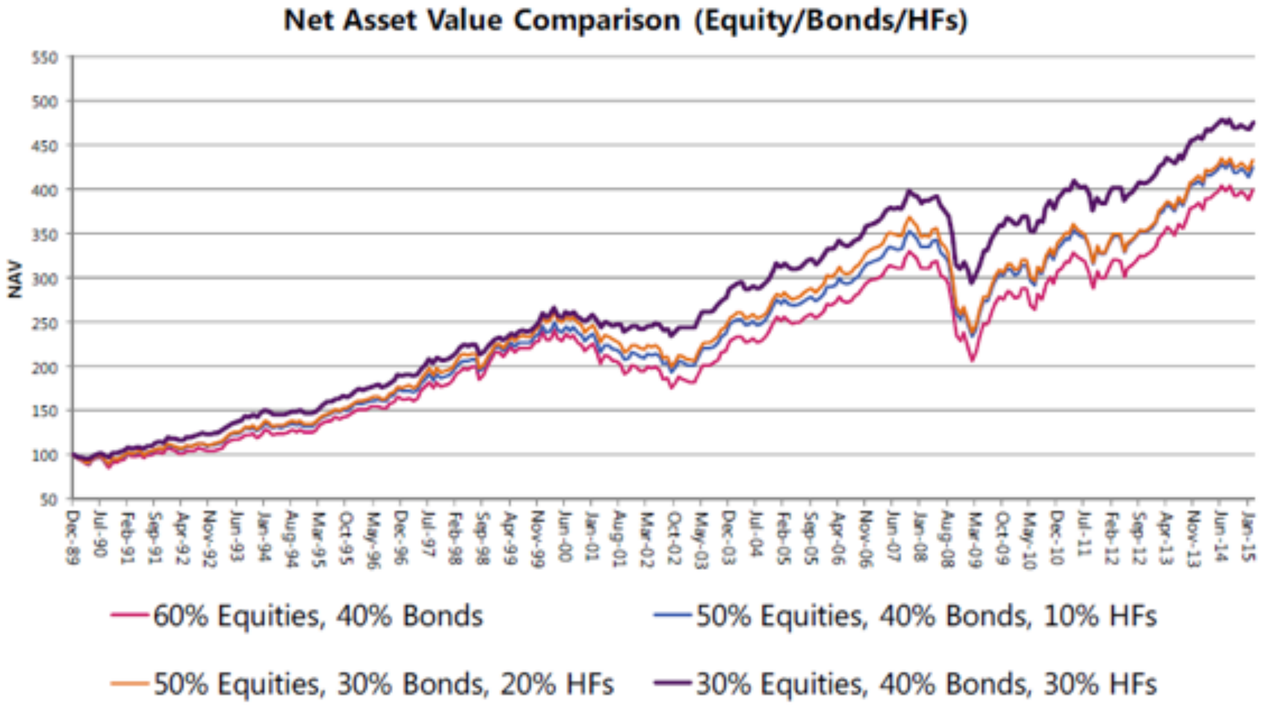
- are subject to less stringent regulatory oversight by financial authorities, although this is likely to change, and as such are able to invest in a wider variety of securities and strategies. Hedge funds invest in both traditional assets e.g. equities and bonds and non-traditional assets e.g. derivatives. They follow a variety of investment strategies, making comprehensive use of long-short strategies (positive and negative weights in various asset classes) and leverage (investing with borrowed money);
- are less liquid than most other investment vehicles; often being subject to “lock-up” periods (a defined length of time during which investors are unable to sell units); and
- charge a flat fee e.g. 2% of assets under management and a performance related fee e.g. 20% of profits generated above the return on cash.

Evolution of the hedge fund industry

The hedge fund industry has experienced considerable growth over the past 25 years; expanding from c.600 hedge funds in the 1990’s to over 10,000 in 2015. Furthermore, the investor base has undergone institutionalisation and now includes pension funds and insurance companies as well as high net worth individuals.

These two factors have impacted the hedge fund industry in the following ways:

- a deeper pool of potential funds to choose from has made it harder to identify managers that offer a truly attractive alpha generation strategy i.e. return generated in excess of market return; and
- hedge fund strategies have become increasingly more sophisticated in response to the higher demands of institutional clients. Historically, the concepts of risk adjusted return and volatility control were foreign to many hedge funds, but now form a cornerstone of the industry.



Source: Aurum

The case for hedge funds

With quality managers becoming increasingly difficult to identify, the limited budget of most trustee boards and the supposed decline of recent hedge fund returns, many are asking "why invest in hedge funds?" To answer this question it is important to take a step back and re-evaluate the role they can play to fulfil within a scheme's investment strategy. Rather than the traditional absolute, high return generation strategies of the past, there is a penchant now for strong risk adjusted returns with low correlation to traditional asset classes. The benefit of diversification, coupled with downside risk management, should result in improved risk adjusted returns when combined with a portfolio of traditional assets.

Improved risk adjusted performance should allow portfolios containing an allocation to hedge funds to outperform otherwise comparable portfolios through the compounding of positive returns and avoiding loss asymmetry i.e. a loss requires an even greater gain in order to recover to the original level. This point is demonstrated in the diagram above.

Accessing hedge funds

Quantum's favoured point of access is through a fund of hedge funds, an investment portfolio consisting of exposure to multiple hedge funds. Whilst this approach can be marginally more expensive due to the additional layer of fees, the following advantages should be considered:

- manager selection expertise;
- diversification across hedge fund strategies (with a lower initial upfront investment); and
- an added layer of due diligence.

Conclusion

Faced with the threat of rising interest rates and low but steady economic growth in the UK and US, traditional asset classes may fail to provide the return and diversification benefits previously experienced. The appointment of a quality fund of hedge fund manager can provide investors with additional diversification and access to alternative strategies delivering opportunity for additional sources of return.

In light of this, perhaps our earlier question *"why invest in hedge funds?"* should really be *"why **not** invest in hedge funds?"*

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Pensions monitor

DC Penal exit charges

According to the Financial Conduct Authority (FCA), nearly 150,000 individuals could be hit by charges in excess of 5% of their fund values if they choose to transfer their defined contribution benefits in an attempt to take advantage of the new retirement flexibilities introduced from April 2015.

The FCA's analysis showed that some 200,000 policies were accessed in the three months following the new tax year, although this has slowed down more recently as those holding pension policies have had more time to consider all the options available to them. Further complications have arisen due to some providers requiring potential transferees to take advice or comply with procedures that exceed the minimum required by law.

In spite of the flexibilities being introduced, there is no legal requirement for any scheme or policy to offer the full range, or indeed any of the flexibilities. It has been estimated that over 80% of policy holders could access the new flexibilities without transferring their benefits, however, the range of options available to them remains limited. Subsequently, many retirees have therefore transferred their benefits elsewhere in order to make use of the full range of flexibilities available to them.

Whilst providers continue to develop their products to suit their clients' needs, this is made difficult by changes in legislation and sentiment amongst those with such savings.

It is early days as yet and insufficient history to show whether the flexibilities have been a resounding success........or failure.

DC Pension Wise

Harriet Baldwin, the Economic Secretary to the Treasury has disclosed that the Department for Work and Pensions (DWP) will take on the responsibility for Pension Wise before April 2016. Pension Wise, was launched earlier this year to provide guidance to individuals who have defined contribution benefits and are aged 50 or above. Pension Wise is currently within the Treasury's remit although the DWP is a more logical choice given its delivery obligations.

Pension Wise has been (relatively) poorly received by those seeking guidance over their options in retirement so the DWP will have to ensure that it is more open in the information that it releases than the Treasury has been to date. Information available at the time of writing shows that whilst around 70,000 individuals have made contact with Pension Wise, only around 8,000 appointments have been made – this is an extremely low number considering that some 320,000 individuals retire each year. Disappointingly, those more able to afford their retirement were less likely to engage with Pension Wise.

Discussions are taking place between the Treasury and the Financial Conduct Authority to see whether the financial advice available in the marketplace could work better for individuals. This includes taking a fresh look at the role of Pension Wise and seeing whether its scope should be widened into an advisory (rather than a pure guidance) offering. Whilst this must be an improvement, we only hope that the forthcoming change in responsibilities will not push the review onto the back burner or delay the publication of the findings.

DB GMP reconciliations...time is running out

It may be that you have tackled the issue of reconciling data for Guaranteed Minimum Pensions (GMPs) with HM Revenue and Customs (HMRC). If you have then you are amongst the few (i.e. 20% or so) schemes that have to date, despite time running out.

Trustees have until April 2016 to register for HMRC's Scheme Reconciliation Service, with HMRC ceasing to respond to scheme queries by October 2018. Members who hold contracted-out benefits will be written to in December 2018 informing them of their GMP entitlement.

Whilst trustees are waking up to the issues that they and their advisers face, it has been estimated that between April 2014 and 2018, there are 17,000 members each day that need to be addressed. With such large numbers it is surprising that many have left it until now.

One of the reasons why trustees need to act before the deadline is to protect themselves from claims made by members whose GMP benefits were overlooked. If GMP issues are not sorted in time HMRC will assume its own data is correct, which may increase schemes' liabilities. This will be particularly difficult for trustees who will need to go back to scheme sponsors, cap in hand. Another reason, particularly for those looking to buy-out, is that the insurance market will offer less advantageous buy-out terms or refuse to quote where the GMPs remain unconfirmed.

If you have yet to start the GMP reconciliation process, we would urge you to discuss this with your advisers as soon as possible - it is far better to do so when HMRC is available to assist. Coupled with that is the importance of shopping around to ensure that you are paying a fair price for the work involved.

i Annual Allowance charges

The reductions in the Annual Allowance over the past few years now mean that more people will incur tax charges than ever before.

In most cases the responsibility to pay the charges falls upon the member and as such, they need to supply details via their self-assessment tax return. HMRC has asked schemes to remind members of this issue as in some cases the individuals were not aware of the potential charge and may not be notifying HMRC.

Whilst trustees have no legal obligation to notify their membership they do have a moral obligation. In particular if the tax charge is large (more than £2,000 in today's terms) then they are obliged to offer a "scheme pays" facility which allows the scheme to settle the tax due on behalf of the member and reclaim it from them via, normally, a reduction in their benefits.

If the member is only in one scheme then the situation is relatively simple. Things start to get complicated if a member is part of more than one scheme or has taken flexible access within a scheme, meaning their Annual Allowance reduces to £10,000 per annum. The further tapering of the Annual Allowance from next year will also add further complications and it will be difficult for trustees and members to be 100% certain that they have complied with the various criteria correctly.

Having been involved in many calculations for members, we see that it is not only the wealthy members who are getting caught in this net. Your advisers should be able to assist with the calculations necessary to determine the extent of the "problem".

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The Pensions Regulator... ten years on

6 April 2015 marked the ten year anniversary of the Pensions Regulator (tPR) coming into power and the establishment of the Pension Protection Fund. The last ten years have seen dramatic changes in the pensions landscape – some good, some not so good, and some where I am still sitting firmly on the fence. The following represent my views and mine alone!

Hits

- **The Pension Protection Fund (PPF) and the Financial Assistance Scheme (FAS)** – Since 6 April 2005, the PPF has taken on responsibility for the pensions of 200,000 members – starting with the 6,000 employees of MG Rover who went bust on 8 April 2005.
- **Trustee Knowledge and Understanding (TKU) and Trustee Governance** – Appreciation of internal controls, conflicts of interest and pensions liberation fraud were pretty much non-existent 10 years ago. tPR's focus has recently shifted towards Defined Contribution (DC) schemes and I expect this to continue to have a positive effect.
- **Automatic enrolment** – Are more people saving for their retirement, or at least behaving proactively towards their pensions? Overwhelmingly so.
  The Department for Work and Pensions (DWP) has forecasted that nine million people will start saving (or save more) for their retirement purely due to automatic enrolment.

Misses

- **Decline of Defined Benefit (DB) provision** – The proportion of private sector DB schemes that are accepting new members has reduced from 36% (2007) to 13% (2014). For the first time, active membership of DC schemes exceeds that of DB schemes. Was it ever genuinely sustainable? Perhaps not, but it will be missed.
- **Guaranteed Minimum Pension (GMP) equalisation** – Despite the monumental impact of the original Barber sex-equalisation judgement, the cloud of GMP equalisation still looms and the DWP have done nothing to suggest that it will be allowed to disappear without a trace. A lot of advisers have their fingers firmly crossed.
- **Tax simplification** – The original concept was indeed simple, but subsequent changes (primarily due to the steady reduction in the Annual and Lifetime Allowance limits) have arguably made the current tax regime even more complex than the old HMRC limits that existed up to 6 April 2006.

Jury's out

- **Flexibility for DC schemes** – At the time of going to press, we are nearly six months into the new regime. Its success will be judged in 20-30 years' time ...
- **Pensions indexation** – The reduction in the cap from 5% to 2.5% p.a., and the emergence of the Consumer Prices Index as an alternative to the Retail Prices Index have helped ease the burden of mandatory indexation. Is it now time to remove it completely and embrace flexibility?
- **Defined Ambition** – A halfway house between DB and DC. The best of both worlds or a fall between two stools? There doesn't seem to be much appetite to embrace Steve Webb's first radical concept.

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Actuary in the Corner
How much is it worth, Guv?

DB As Scheme Actuary to a number of Defined Benefit (DB) pension schemes, we are aware of a significant increase in interest from members regarding the value of their pension.

In March 2014, the Government announced new flexibilities at retirement for members of Defined Contribution (DC) pension schemes, including taking the value of their DC benefits as cash, more technically known as an Uncrystallised Funds Pension Lump Sum (UFPLS), and flexible drawdown as an alternative to compulsory annuity purchase. As a direct consequence of these new flexibilities, effective from 6 April 2015, some members of DB schemes are finding it advantageous to transfer out of their DB scheme to a DC arrangement as they approach retirement in order to make use of these new flexibilities.

Our experience however is that it's not just older members who are requesting a transfer value quotation. A wide range of members are now, generally, more interested in pensions than ever before. That must be a good thing, surely? The number of quotations provided to members is on the increase and the number of confirmed transfer out cases also appears to be increasing.

Quantum needs to be ever vigilant and continues to warn members about pension scams as well as rigorously checking the legitimacy of receiving pension arrangements. Should any concerns about pension liberation fraud arise, we may notify scheme trustees as well as Action Fraud. It has also become a requirement for trustees to check that members have received financial advice regarding their transfer if their transfer value is over £30,000.

From an actuarial perspective, the key risk for a DB scheme is that an increase in the number of transfers out could have a detrimental effect on the scheme's funding position and the security of the remaining members' benefits.

If a scheme is underfunded on the transfer value basis, the trustees should consider reducing transfer values until such time as the scheme returns to being adequately funded. Furthermore, trustees should understand the relationship between the ongoing funding reserve and the transfer value – it is a common misconception that the former is always bigger than the latter and the funding level will improve if a member transfers out! That is not always the case.

Frequent disinvestment activity, in order to pay the transfer values, may also impact on the overall level of return achieved by the scheme, which in turn impacts on the scheme's deficit recovery plan.

It is a good idea to monitor the level of activity in your scheme and, if you haven't done so already, we suggest that you discuss (the basis of) transfer values with your Scheme Actuary at the earliest opportunity.

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QuantiFI

"When the facts change, I change my mind." That was the mantra of John Maynard Keynes. The unpredictability of markets, coupled with heightened regulatory control, makes this maxim meaningful to most pension practitioners today. It is especially pertinent given another of his credited quotes: "Markets can remain irrational a lot longer than you and I can remain solvent".

It may be nearly 70 years since Keynes' death, but the sentiment still stands today. So we are excited to unveil QuantiFI, our new real-time financial management consulting tool for trustees and finance directors. QuantiFI is a complete suite of cost and risk management tools which supports the analysis of funding and investment strategies of Defined Benefit (DB) pension schemes, helping clients to meet their long-term savings goals.

QuantiFI embraces the holistic approach to financial management that is advocated and promoted by the Pensions Regulator.

This new software allows Quantum and our clients to look at their pension scheme through the past, present and future – and from all key angles i.e. funding level monitoring, recovery plan analysis, investment strategy and risk assessment.

In order to capitalise on the power of QuantiFI, clients are encouraged to place their scheme's assets on an investment company's implementation platform. This allows investment decisions to be acted upon efficiently and effectively before the chance has gone.

Quantum's Partner heading up our Investment Services, Robert Davies, has been quoted in the press recently as saying that "….much change has come about with respect to risk and regulation since the financial crisis. The unpredictability of investment markets, coupled with acute regulatory control, makes QuantiFI meaningful to most pension scheme trustees, and finance directors too. When the facts change, it alerts them to the situation and helps them change their minds. It answers those questions regularly asked by the Pensions Regulator and allows clients to make informed decisions on a timely basis."

If you would like to learn more about QuantiFI please contact us.

Quantum chronicles

New arrivals

Dylan Morgan
Amy Sutherland
Matthew Tucker
Sabrena Edmonds
Joshua Davies
Mike Watkins
Rachel O'Connor
Julia Britton
Conor Henry
Heather Harrie
Lewis Jones

Events

We have held seven events recently

- Investment Evening in conjunction with Mobius Life, Cardiff – 5 March 2015
- Investment Evening in conjunction with Standard Life, Cardiff – 11 June 2015
- Pensions & Investment Seminar, London – 25 June 2015
- Pensions for Breakfast Seminar, Cardiff – 17 September 2015
- Cardiff Business Awards Finalists – 18 September 2015
- Team Quantum Challenge – the Fan Dance
- Pensions and Investment Seminar, Birmingham – 12 November 2015

QUANTUM ADVISORY
The Actuaries and Employee Benefit Consultants

Who we are

Established in 2000, Quantum Advisory is an independent Financial Services Consultancy that provides solution based Pensions and Employee Benefits services to employers, scheme trustees and members.

We design, maintain and review pension schemes and related employee benefits so that they operate efficiently and effectively and are valued by employees. This means that you can get on with doing the things that you do best, therefore saving you time and money.

Products and services

We offer a range of services to companies and pension trustees, all designed to focus on your specific needs, including:

- Actuarial services
- Administration of defined contribution and defined benefit pension schemes
- Banking, accounting and pensioner payroll
- Company advice
- Employee benefits consultancy
- Governance
- Investment consultancy
- Pension and employee benefit communications
- Risk benefits advice
- Pension scheme wind up
- Secretarial services to trustees
- Trustee training

Getting in contact

We have offices in Amersham, Birmingham, Cardiff and London. Give us a call to see how we can help with your pension and employee benefit challenges.

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