LCP INSIGHT CLARITY ADVICE

The changing world of pensions: Current pension developments across the world.

Retirement systems around the world are going through major changes in 2015.

Government changes are driving companies to reconsider their retirement strategies.

General increases in life expectancy (highlighted by the latest mortality tables in Canada and the US), and a need to tighten financial budgets has led to governments looking at a range of options including:

- Many countries are seeing an increase in state retirement ages – how do your company plans fit in with these changes? And is your company prepared for employees working longer?
- Some countries are reducing the tax effectiveness of retirement savings including France, Ireland, Netherlands and Mexico; whilst
- Other countries are trying to encourage greater retirement savings by offering additional tax efficiencies including Greece and Russia.

Greater public awareness also means that employees are taking more of an active interest in retirement benefits.

European legislation through IORP II is driving a shift in attitudes to governance. Sweden and the UK are already looking at additional measures to increase awareness on the pension risks companies are exposed to. This is likely to lead to further de-risking.

Elsewhere around the world, changes to pensions systems are causing companies to review their options with a view to finding better risk sharing, sustainable solutions for the future.

LCP is part of an international network of independent actuarial and employee benefit consultancies. LCP's international network specialises in giving high quality joined up advice to multinational companies on all aspects of employee benefit and retirement provision.

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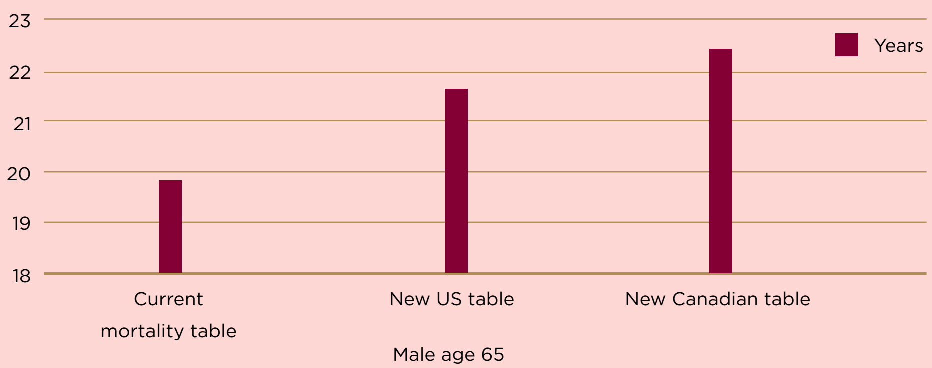
Americas

New North American mortality studies show increases in life expectancy of around 2 years.

Large increases in life expectancy at age 65



The impact of these new tables will be seen by companies in a number of ways.

- LOWER balance sheet funded status
- LOWER profit and loss
- HIGHER contribution requirements
- PRICIER lump-sum payouts
- HIGHER Pension Benefits Guarantee Corporation premiums in the US

Some of these impacts are immediate while others are delayed, leading to some short-term windows of opportunity for corporate sponsors.

Brazil

The private pension market in Brazil has been strengthened. The discount rates used in actuarial valuations will continue to reduce gradually from 5.5% pa in 2014 to 4.5% pa in 2018. Access to global assets from Brazil continues to grow.

Mexico

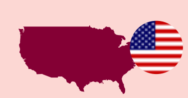
A universal state pension has been established of 115USD per month. Also, a fiscal reform has come into force which reduces the amount of deductible contributions to pension funds from 100% to 53%. This has led to some companies closing their pension schemes. A reform in social security law has been proposed which would increase the amount of earnings subject to contribution rates.

Latin America

Most countries in Latin America have made (or are looking to make) significant revisions in their benefit systems, mainly to increase coverage and efficiency. These include changes to fees, competition, foreign investment, financial education, additional contributions, investment choices, life-cycling and benefit payouts. Some countries, such as Chile, are reintroducing some form of minimum non-contributory public pension.

Canada

The Canadian Institute of Actuaries has issued the first ever mortality tables and mortality improvement scales based on Canadian mortality experience. Canadian longevity has improved significantly faster than projected by the commonly used US standard tables. A Federal Legislative proposal would permit the establishment of Target Benefit Pension Plans as a means of better managing longevity risk. Other Federal proposals include changes in permitted pension fund investments that will impact federally registered plan sponsors.



USA

Decent investment performance and extended relief under a new federal act, continue to improve the financial position of private sector DB plans funded status. The prospect of P&L volatility, and the ever increasing size of DB plans keeps the prospect of de-risking and eventual wind-up of DB plans a perpetual board room discussion.

The shift to DC retirement plans among the younger population, together with a move towards DC style healthcare, is altering the conversation about shutting down DB plans, from whether, to when.

Measures continue to be reviewed on how to sustain solvency of the federal government retirement programme, which is expected to run out of money in the next 15-20 years. Removing the cap on payroll taxes and extending the ultimate retirement age to 69 or 70, up from 67, are some of the considerations.

Europe

Particular changes that companies may need to take action on

2015

1 JANUARY 2015

Netherlands

Accrual rate limited to 1.875% for average pay plans and 1.657% for final salary plans, and pensionable salaries limited to €100,000

1 JANUARY 2015

Germany

Guaranteed interest rate for life insurances decreases, resulting in lower guaranteed benefits for new members of DC plans

1 JANUARY 2015

Italy

Tax roll up of TFR increased from 11% to 17%

6 APRIL 2015

UK

New freedom and flexibilities come into force

2016

1 JANUARY 2016

France

Mandatory health insurance introduced for all employers

1 JANUARY 2016

Sweden

The new Occupational Business Act expected to take effect

Belgium

A number of insurers have lowered the guaranteed rate of return in group insured corporate pension plans to a level below the legal guaranteed minimum. Employers are considering the consequences of this; in particular with their obligation to fund to this legal minimum. Employers that have previously decided not to value their defined contribution plans under IAS19 should reconsider their decision.

Cyprus

Occupational pension funds in Cyprus face ongoing challenges as a result of the measures taken to support the banking system in Cyprus. The controls are prohibiting local pension funds from implementing globally diversified investment strategies. Around 700 occupational pension funds have dissolved since March 2013.

France

Taxes continue to increase on medical and pension plans. The discrimination rules under which an employer can offer different benefits to employees by category have now been clarified: it is now very difficult to set up a scheme for too specific a population without avoiding significant taxes. As a result, many companies are looking for alternative arrangements for their Company executives. Mandatory health insurance will be introduced for all employers from 1 January 2016.

Netherlands

Pension plan retirement ages have increased to 67 in 2014 for future service, in combination with a lower limit for future pension accrual. The government has also agreed to further limit the accrual rate to 1.875% for average pay plans (1.657% for final pay plans) and limit pensionable salaries to €100,000 from 2015. Other legislation changes are also affecting DC plans. As a result, almost all pension plans in the Netherlands should have been amended in 2014. A national pension debate has started, where everyone can give their views regarding the best pension system for the future.

Russia

The Government has proposed to increase the retirement age. From 2014, new contribution rates apply and a new pension formula for future pensioners was implemented. Currently, the government is discussing a set of laws to stimulate additional pension contributions through tax incentives and other methods.

Germany

Concerns continue over the low interest rates. Revised test methods must be used to prove the adequacy of the actuarial interest rate. From 2015 onwards, the guaranteed interest rate for life insurances decreases from 1.75% down to 1.25%, resulting in lower guaranteed benefits for new members of DC plans. Internal marketing for corporate pensions is more of a key focus for plan sponsors.

Greece

There is continued pressure on the benefit levels and financing of social security pensions. From 1 January 2014 the taxation of contributions and benefits from group pension plans has changed. Employer contributions on behalf of the employee are not taxed as income. Benefits paid in the form of annuity payments are taxed at 15%. Benefits paid in the form of lump sums are taxed at 10% up to €40,000 and 20% thereafter.

There is also uncertainty due to the parliamentary elections due in 2015.

Spain

The state retirement age is increasing from 65 to 67, with some exceptions for those with long contribution histories. In addition, a "sustainability factor" has been approved from 2019 and the indexation of the pensions to CPI is no longer guaranteed.

Sweden

A proposal for new regulation of occupational pension plans in Sweden was presented in September 2014. The proposal justifies the need for a strengthened solvency regulation, and enhanced regulation on corporate governance and risk management, based on the application of certain parts of the IORP II Directive. Above all, the motive for the new regulation is that the present regulation is not sufficiently risk-sensitive. The lack of risk sensitivity is particularly true for investment risks and risk matching between assets and liabilities. Occupational pension plans that bear risk will have two choices; either seek to transform itself into an institution operating under a new proposed law, the Occupational Business Act, or apply for a permit under the Insurance Business Act. The proposal suggests that the new Occupational Business Act will take effect from 1 January 2016.

Ireland

The 2014 Irish Budget capped pension pots at €2.0m. Benefits in excess of this are effectively double taxed. The result is that DB Pensions will be capped at between €65,000 and €100,000 depending on when members retire. Funding challenges continue as euro bond yields remain low. The challenge is exacerbated by the requirement for pension schemes to hold risk reserves from 2016. Schemes can get relief under the statutory solvency standard by using Euro Sovereign bonds (or other qualifying assets) to back pensioner liabilities. The government's Pension Levy for 2014 is 0.75% of pension fund assets, and the levy will be at least 0.15% for 2015. The position after this is currently unclear. The practice of closing retirement plans, with members receiving a fraction of the benefits they thought they had, continues. The state pension age is increasing gradually to 68 for those retiring after 2028.

Italy

From 1 January 2015, the tax on roll-up of TFR (termination indemnity) plans has increased from 11% to 17%. This will result in a reduction in liabilities for affected TFR plans and significant P&L impact under IAS19. Tax on pension fund investment returns has increased from 11.5% to 20%, reducing their attractiveness. Finally, the TFR can now optionally be received as part of ongoing salary, for an experimental 3 year period.

Switzerland

Current topics of discussion include increasing life expectancy and potentially unsustainable pension conversion rates. As companies are looking to reduce these risks, the performance of a risk assessment has grown in importance. The Federal Counsel has started a comprehensive reform of pension provision in Switzerland (Pensions 2020).

UK

The March 2014 Budget introduced major changes to UK pension plans. DC benefits will have full flexibility in how they can be taken at retirement, and private sector DB plan members will also be able to access these flexibilities through transferring to a DC plan. Companies need to consider their pension strategy for both DB and DC plans to ensure de-risking opportunities are not missed and members are given appropriate options. The key action is for companies to review their benefit communications to ensure that they remain compliant as well as ensuring that they provide employees with sufficient information to make educated retirement decisions.

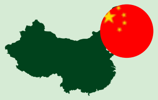
Africa, Asia and Middle East

Indonesia

Since January 2014 the National Social Security System (NSSS) has implemented a mandatory health programme for all Indonesian citizens. Employers and employees are required to pay contributions as a percentage of pay, of 4% and 1% respectively. From July 2015 the NSSS will also implement a pension programme for all Indonesian workers. Discussions on how to harmonize all the programmes are still in progress.

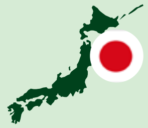
Australia

The Australian government is having difficulty in getting many of its retirement income and other budgetary measures passed. The changes to social security pensions are particularly controversial and face considerable opposition both inside and outside Parliament. The increase in the superannuation guarantee has been postponed. The reform of the financial advice laws is going ahead after a deal with the minor parliamentary parties - but on a watered down basis.



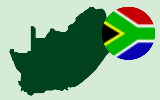
China

Flexible retirement ages are under consideration, in particular for women who currently have a normal retirement age of 50 or 55 (compared to 60 for men). Some local governments have introduced tax incentives to qualified employer sponsored plans. In these, matching contributions from employers are tax deductible up to 4% of pay. The Chinese government have announced plans to create a standardised pension system before 2020.



Japan

The Employee Pension Funds (EPFs) which have deficits in the contracted-out portion are due to be phased out in 5 years. Employers who are participating in these multi-employer EPFs should urgently consider restructuring their retirement benefit schemes. Companies are reporting based on the revised J-GAAP from the fiscal year ended 31 March 2014. The DC plan contribution cap is raised by 2,000 yen to 4,000 yen per month as of 1 October 2014.



South Africa

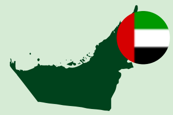
The retirement industry is in a consultation process on required reforms. Key areas of reform will include increasing preservation, coverage and annuitisation. The regulator is focussing on ways to reduce the costs of saving for retirement.

India

There have been some key changes put in place effective 1 September 2014 within Indian social security schemes. The statutory wage ceiling under the Employees' Provident Fund Scheme 1952 (EPF), the Employees' Pension Scheme 1995 (EPS) and the Employees' Deposit Linked Insurance Scheme, 1976 (EDLI) has been enhanced from INR 6,500 to INR 15,000 per month. The minimum monthly pension under the EPS has been fixed at INR 1,000. Any EPF member joining on or after 1 September 2014 shall not be allowed to become a member of EPS if his pay exceeds INR 15,000 per month at the time of joining. For such a member, his entire employer and employee contributions, amounting to 24% of wages, will be allocated to his provident fund account. The change in wage ceilings does not impact international workers since they are governed by special rules under these schemes.

Singapore

Companies are realising that the State Central Provident Fund (CPF) is inadequate and companies are reviewing the current retirement benefit provisions for their employees. Some companies are establishing tax effective company retirement schemes to include expatriates. Additionally, for tax reasons, a number of companies have established Offshore Plans with Brunei the favoured trust location since all the administration, bank account, investment and Trustees can be located in Singapore. Companies should review their expat arrangements to ensure they remain appropriate.



UAE

Some local banks are launching new corporate pension products tailored to the expatriate population of the UAE. This will help employers meet the increasing demand of the expatriate population for pension products. Additionally, an increasing number of companies value their compulsory end of service obligations under IFRS.

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Shaun Southern
Partner
shaun.southern@lcp.uk.com
+44 (0)1962 672880

Phil Cuddeford
Partner
phil.cuddeford@lcp.uk.com
+44 (0)1962 873353

Simon Coomber
Partner
simon.coomber@lcp.uk.com
+44 (0)1962 872761

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LCP is a firm of financial, actuarial and business consultants, specialising in the areas of pensions, investment, insurance and business analytics.

Lane Clark & Peacock LLP
London, UK
Tel: +44 (0)20 7439 2266
enquiries@lcp.uk.com

Lane Clark & Peacock LLP
Winchester, UK
Tel: +44 (0)1962 870060
enquiries@lcp.uk.com

Lane Clark & Peacock Belgium CVBA
Brussels, Belgium
Tel: +32 (0)2 761 45 61
info@lcpbe.com

Lane Clark & Peacock Ireland Limited
Dublin, Ireland
Tel: +353 (0)1 614 43 93
enquiries@lcpireland.com

Lane Clark & Peacock Netherlands B.V.
Utrecht, Netherlands
Tel: +31 (0)30 256 76 30
info@lcpnl.com

Lane Clark & Peacock UAE
Abu Dhabi, UAE
Tel: +971 (0)2 658 7671
info@lcpgcc.com
