XPS Corporate

XPS Insights for Employers

February 2021

Pandemic drives new wave of benefit change

What you **need to know**

- With the onset of the COVID-19 pandemic in 2020, a number of employers sought to manage costs and risks to protect businesses and employment. A number of industries saw revenue fall and needed to manage costs.
- The Government's Coronavirus Job Retention Scheme has certainly helped with meeting employment costs, but the scheme only covered auto-enrolment minimum pension contributions and even then only until July 2020.
- At the same time, the cost of defined benefit pensions was set to increase when next calculated by the pension scheme. The costs typically reflect long term interest rates which had fallen significantly during the pandemic.

Against this backdrop we carried out a survey to understand actions employers were taking on managing pension cost for their current employees. This survey of 450 clients has indicated a sharp increase in employers looking to close their DB pension schemes to future accrual.

The **results of our survey** show that 2020 has seen significant upturn in benefit change reviews:

23% of schemes remain open to benefit accrual

20% of open schemes have commissioned benefit change advice since the arrival of COVID-19

71% of schemes currently looking at benefit change cited either cost or risk management as a reason for review

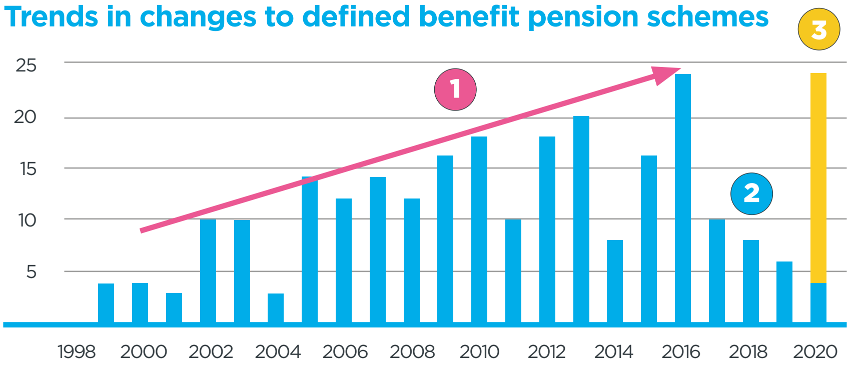
74% of schemes open to accrual are paying more than 20% of pensionable salaries for future accrual

76% of schemes closed to accrual are paying less than 9% of pensionable salaries to new arrangements

Actions you can take

- **Assess** expected costs and associated risk given your current benefit design.
- **Decide** if contingency plans are needed to manage benefit cost.
- If change is needed, **consider** your alternative benefit options.
- **Measure** the cost of your preferred benefit structure on your long term funding target.
- If making a change, **plan** how to effectively communicate in the current environment.

Trends in changes to defined benefit pension schemes



Source: XPS Pensions Group

1. Clear upwards trend of scheme closures from 2000 as defined contribution becomes more popular.
2. By 2016 many schemes had considered pension arrangements alongside auto-enrolment requirements and the ending of contracting-out. Benefit change considerations started to tail off.
3. We expect to see a surge, of up to 300%, of employers closing their schemes following 2020 benefit change reviews brought about by economic uncertainties due to COVID-19.

The finer detail: trends and best practice on benefit change

Reasons employers consider benefit change

Past reasons for changes to DB benefits

- Cost and risk management have always been primary reasons for employers to conduct benefit reviews of their DB scheme
- Historically such benefit reviews did not necessarily lead to closure.
- Almost a third of schemes in our survey also cited alignment of benefits across their employees as an additional reason for benefit review.

What does the future hold?

- COVID-19 continues to make economic conditions challenging and we expect to see more activity in this area in the coming years.
- In today's uncertain economic world, cost and risk management has become even more prevalent and the majority of our 2020 reviews are actively considering closure.
- The Coronavirus Job Retention Scheme has been extended to the end of April 2021 but this does not cover pension contributions, and as a result has meant employers have had to consider how to manage pension costs.
- The Pensions Regulator's 2020 funding consultation, and the consultation expected later this year may result in further reviews down the line, but currently COVID-19 is the prime reason for review.

Key steps to carrying out an effective benefit change

1
Reason for change
Understand the need for change and be able to explain it clearly

2
Design options
Thorough discussions and analysis around options available

3
Strategy
Identify and engage with all stakeholders effectively

4
Consult
Member experience is key. Enhance through **video calls**, **modellers** and **live monitoring of feedback**

The Pensions Regulator's funding consultations could result in further benefit review in coming years, but for now COVID-19 has undoubtedly brought benefit change back on the agenda for many corporates.

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