Big Danish pension plan switches to DC from DB

By Editor Test *Wed, Nov 30, 2011*

The new regime would be one with no investment choices for plan participants to make. "Our members… are blue-collar workers and typically don't want to make investment decisions themselves," said the plan's chief investment officer.

Industriens Pension intends transform its entire pension scheme into a life-cycle (a defined contribution plan with declining equity exposure as participant ages, but no individual control over investments) product in June, in the final stage of a move away from a traditional guaranteed pension, IPE.com reported.

On December 1, the DKK90bn (€12bn) labor-market fund will alter the basis of all member accounts to "unit-linked" from "guaranteed with-profits". The latter type of plan offers a defined benefit pension with opportunity for bonuses in retirement based on investment performance.

This change was announced in August and will be accompanied by windfall payments to members equaling around 20% of their savings as the fund shares out the DKK13bn collective savings pool, which will no longer be needed.

Jan Østergaard, chief investment officer, said: "On the first of June, we will change the scheme to a life-cycle product."

The new product will be quite simple, with no choice of risk profiles offered to members, he said.

"There will only be one level of risk, but the younger the members they are, the more risk they will have," he said. "Typically, they will have higher proportions of credit bonds and equity."

The board of trustees – made up of employee representatives – took a positive decision that the new regime would be one with no investment choices for scheme members to make.

"The board believes members wouldn't wish to have that choice," Østergaard said.

"The main argument is the profile of our members. They are blue-collar workers in the industrial sector and typically don't want to make investment decisions themselves."

Østergaard explained that, while many pension funds in Denmark running the traditional with-profits pension system – which includes a minimum yield guarantee – have run into difficulties, this has not been the case for Industriens Pension.

Such guaranteed pensions will require a high level of reserves under the upcoming Solvency II legislation, and some pension funds are unable to provide this.

"We had no problem meeting the Solvency II requirement," Østergaard said. "The main argument for moving away from guarantees was mobility in the labor market and fairness with respect to returns."

Because the industrial sector in Denmark has suffered from heavy job losses over the last few years, Industriens Pension has lost more than 35,000 of the 195,000 active members it had three years ago.

Most of the pension funds that Industriens' members are likely to move to have already changed their pension product to pure defined contribution for new members.

"If we stayed with the old system, anyone leaving us would have to leave their share of the reserves here and not gain any reserves in their new pension scheme," Østergaard said.

He said Industriens Pension had managed its guaranteed with-profits product successfully in comparison with its peers for two reasons.

"There has been a policy since the 1990s of building up reserves, and we have also opted to pursue an active investment strategy," he said.

"The other key to our success is deciding early on to hedge the guarantees 100%. You face a high level of risk from the guarantee because the liabilities fluctuate widely – due to the fact they are so long lasting."

The recent phase of very low interest rates did not dent Industriens' resources because of the hedges, he said. "It also meant we had a huge gain on the hedges, and gain corresponded to the increase in liabilities due to the guarantees."