Solvency II could kill many British DB plans, officials say

By Editor Test *Wed, Nov 21, 2012*

British pension officials and executives are afraid the cure for their problems, as prescribed by Solvency II, would be worse than the disease.

Britain's pensions minister said that Solvency II measures in the revised IORP (Institutions for Occupational Retirement Provision) Directive will end any prospect of "risk sharing" among UK companies, and estimated that the total cost to the local pensions industry could reach as high as £400bn (€498bn), IPE.com reported.

The UK government has for months been pushing back against European Union plans to harmonize the Solvency II capital rules for insurance companies with the rules governing pensions across Europe.

If pension funds aren't given a partial exemption from Solvency II requirements, they would have to shift out of riskier assets, which would drive down their expected returns, hurt their funded status, and force plan sponsors to increase contributions. British pension officials and executives are afraid the cure for pension problems would be worse than the disease.

Addressing a PensionEurope conference in Frankfurt, Steve Webb he pointed out that it was currently illegal for companies in the UK to offer employees pension promises unless they were inflation-protected.

"We are currently looking at ways to encourage firms to offer what you might call 'Defined benefit light,' where pensions are essentially like the old DB style, but with more flexibility for the firm, or 'Defined contribution plus,' which aims at getting more money in but also looks at [plan] quality, scale, charges and governance," he said.

He said he wanted to avoid a stark and sudden shift from "high-quality, final-salary, index-linked pensions that are so expensive that firms won't want to provide them" to "minimalist DC" plans with "minimalist contributions."

UK companies wanted risk sharing but were "terrified" about Solvency II, and that Brussels would make those promises "very" expensive, Webb said. "The risk is that Solvency II will not only have a devastating effect on the European industry but destroy the prospect of risk sharing."

Webb also referred to an analysis, published today, on an initial impact assessment he commissioned showing that the cost for the UK pension industry would be as much as £150bn if Solvency II rules for pension schemes were implemented, adding that "if the full Solvency II capital requirements came through, we would be talking about £400bn in the UK."

"When we discussed the final points of the QIS (Quantitative Impact Statement) methodology, there was a huge elephant in the room – why are we doing this at all?" he said. "What is the question we are trying to answer that could possibly be in that territory?"

Webb finally argued that, in terms of plan closures, his research showed that, over the coming decade, only one in 20 DB plans would remain open to new members in the UK if Solvency II rules were introduced. “This would kill DB,” he said.