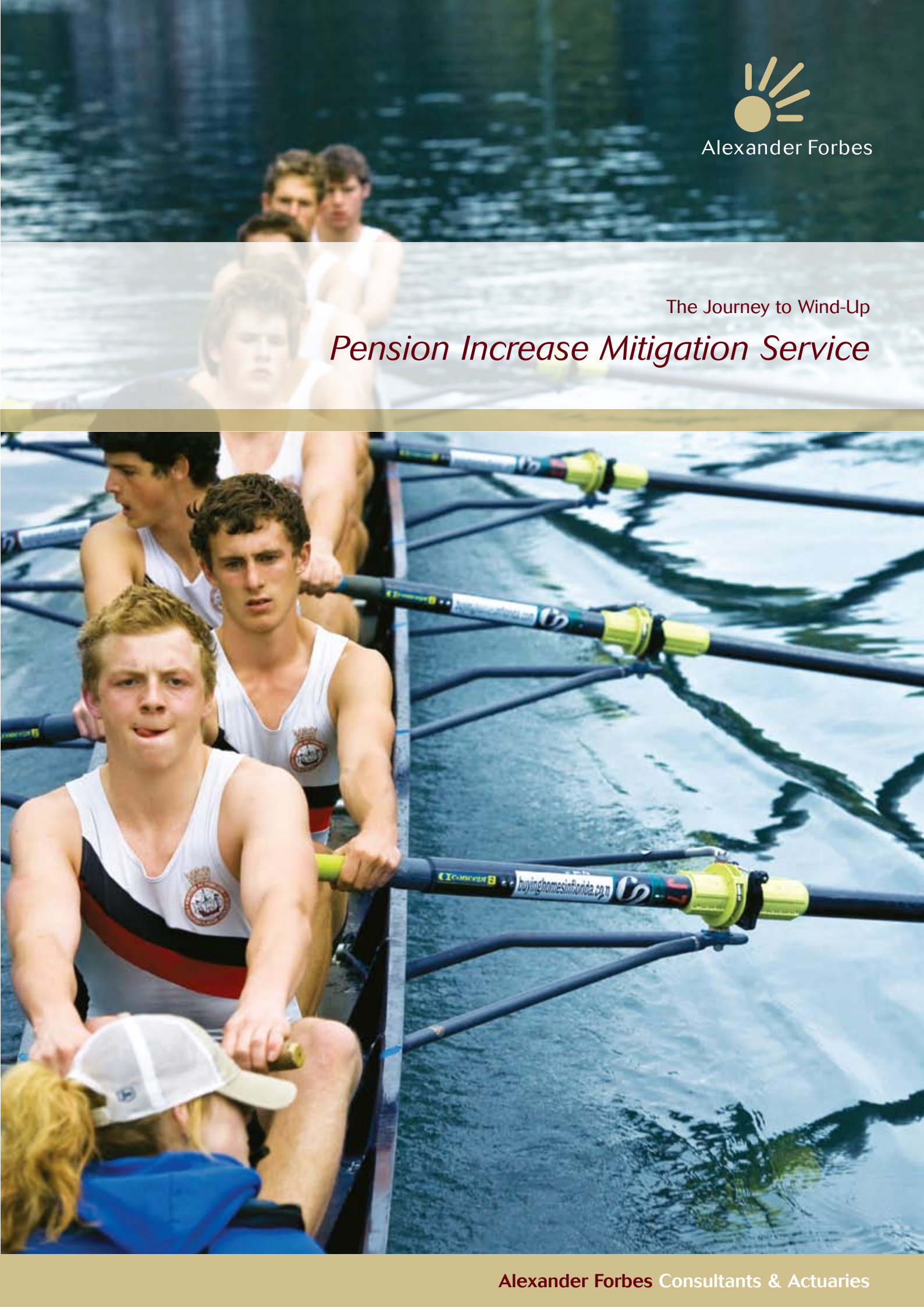




Alexander Forbes

The Journey to Wind-Up  
*Pension Increase Mitigation Service*





# Pension Increase Mitigation Service

Typically, pensions in a defined benefit scheme will increase in future in line with inflation, or by a fixed percentage, throughout an individual pensioner's lifetime. These increases often impose uncertainty on the scheme, while members themselves have no choice in how their pension is paid.

Whether winding-up your scheme is in sight or not, the uncertainty of these increases is a burden that can be eased.

Our Pension Increase Mitigation Service (PIMS) enables members to be offered a higher but level pension for some of their pension instead of the promise of a future increase.

This aims to:

- *improve the funding level*
- *reduce the uncertainty of future pension payments*
- *improve cash flow*

PIMS has the additional bonus of giving your scheme's current and future pensioners a choice in how they receive their pension.

## How does it work?

Individuals with escalating pensions are offered an enhanced but flat rate pension, agreed between the company and the trustees, in lieu of future non-statutory increases.

The effect of the change in payments, is illustrated in figure 1.

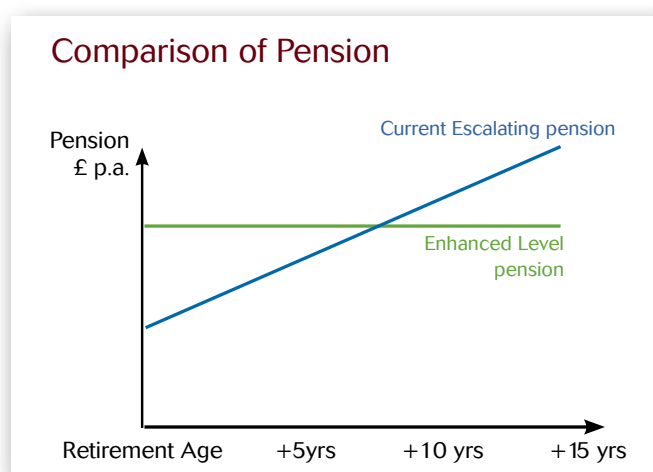


Figure 1

The accumulated pension in pure monetary terms, (i.e. total pension received), for the same example individual is shown in figure 2.

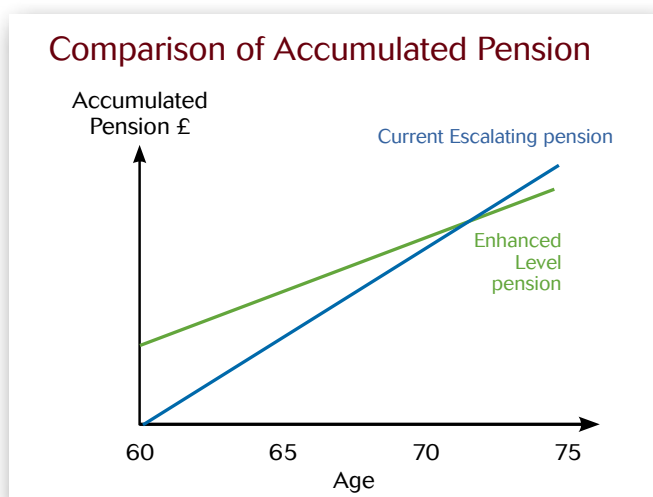


Figure 2

Importantly, it can be seen that it takes many years before the accumulated escalating pension exceeds the accumulated level pension.

Using our PIMS to offer an attractive enhanced level creates a win-win situation for the company, trustees and the members. We can help calculate this offer for each pensioner.

## Considerations

Some increases to defined benefit pensions are statutory and cannot be altered. Statutory increases are:

- Nil on the excess over the Guaranteed Minimum Pension (GMP) accrued before 6 April 1997 and on the GMP accrued before 6 April 1988;
- Inflation (capped at 3% per annum) on the GMP accrued after 6 April 1988;

- Inflation (capped at 5% per annum) on the pension accrued after 6 April 1997; and
- Inflation (capped at 2.5% per annum) on the pension accrued after 6 April 2005

Many pension schemes give increases at a rate higher than those set out above. These can be removed with the pensioner's consent, further lowering the payments.

## Why choose PIMS?

### Benefits to the pensioner

- Offered choice of a higher pension (choice that is currently not available)
- Attractive to people with lower life expectancy
- Ability to have bulk of pension income available when healthy and fit (in sixties and seventies).

### Benefits to the company

- No company funds required if higher pension offered
- Reduces buy-out, ongoing and FRS17 deficit
- Can strengthen the employer covenant
- Can improve sale price of company

### Benefits to the trustees

- Improves funding level and can reduce deficit
- Cash flow positive as liabilities reduce by more than increase in pension, depending on level of offer
- Can reduce ultimate wind-up costs (simpler pension to secure)

## Our Experience

We have found that a significant number of pensioners will accept the offer providing it is made at an appropriate level. Take-up rates can also be affected by how the offer is communicated.

Below is an example which shows the potential liability savings where the defined benefit pension

scheme provides increases in line with inflation capped at 5% per annum on the pension accrued before 6 April 1997.

In this example the company and trustees decide to pass on 75% of the value of the non statutory pension increases back to the pensioner in the form of an increase in the current pension. In this example, the company have just over 50 pensioners.

Take-up rate	Buyout Liability Reduction (£)
40%	61,420
60%	92,140
80%	122,850
100%	153,570

Offering members a choice on how their pension is paid is key to treating them fairly. However, if not carried out correctly, this can cause problems for trustees and employers in the future.

**If you would like to discuss your pension scheme with our experts please call**

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