Institute and Faculty of Actuaries

Collective DC (CDC) Design Principles

CDC Working Party

Keith McInally
James Franklin-Adams

5 November 2024

Introduction

Presenters

Keith McInally
Pensions and Investment Actuary
Abrdn Investments

James Franklin-Adams
Pensions Actuary
Aon

Paper

"The route to effective scheme design"

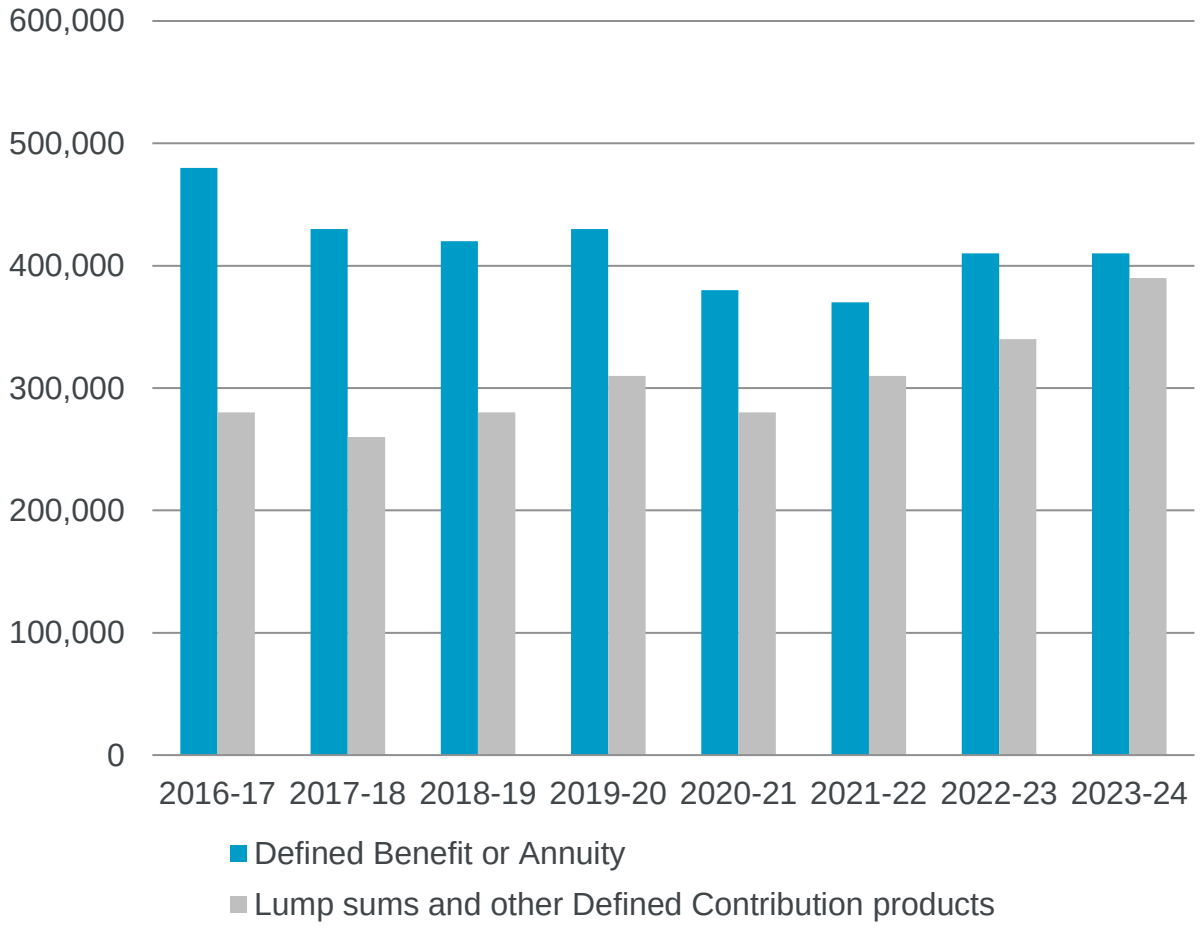
IFoA's Virtual Learning Environment – see link in the chat

IFoA Pensions CDC and Collective Benefits Working Party

Simon Eagle (Chair)
Mark Foster
Paul Wales
Peter Williams
Derek Benstead
Helen Draper
Shriti Jadav
Catherine Donnelly
Yushuo Liu
Alec Findlater
Alan Newton
Keith McInally
James Franklin-Adams

Institute and Faculty of Actuaries

UK Retirement Landscape

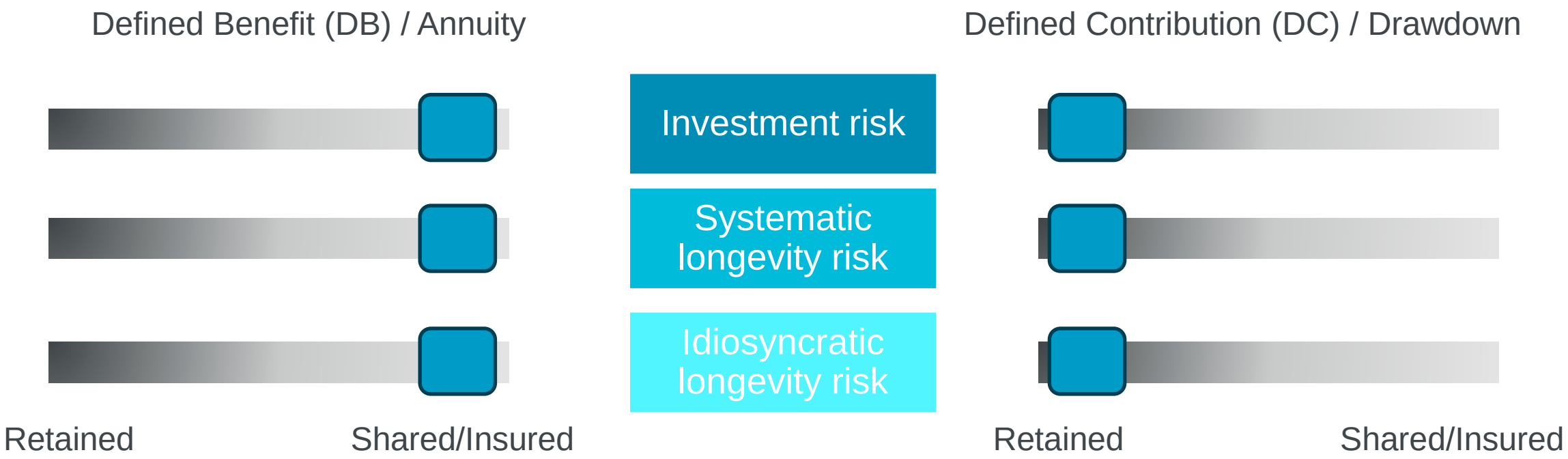


- Number of Defined Contribution (DC) retirements has been steadily growing as a share of the market
- With open Defined Benefit (DB) schemes becoming rare in the private sector, DC funds will soon overtake DB as the main source of new private individual retirement funds in the UK

Data source: DWP Workplace pension participation and savings trends: 2009 to 2023

Institute and Faculty of Actuaries

Current Retirement Solutions



Institute and Faculty of Actuaries

What is Collective DC (CDC)?

Employers' and employees' contributions are fixed giving cost stability. There is no ability to seek more contributions from members or employer (defined contribution in nature).

In exchange for contributions, members accrue target pension benefits payable from retirement age until death. However, benefits are not guaranteed and will be adjusted over time based on scheme experience.

By default, income is paid from the scheme to members in their retirement until death. Spouses' pensions and other death benefits may also be provided.

Basic Design Principles

- Whole-life or decumulation only
- Pooling of longevity risk
- Defined contribution
- **Variable** retirement benefits
- Benefits expressed as income

Institute and Faculty of Actuaries

10 Key Areas of Scheme Design

- Pricing accrual
- Setting assumptions
- Investment pooling
- Longevity pooling
- Pension increases
- No risk buffers
- Wind-up
- Member options
- Leaving service benefits
- Insurance

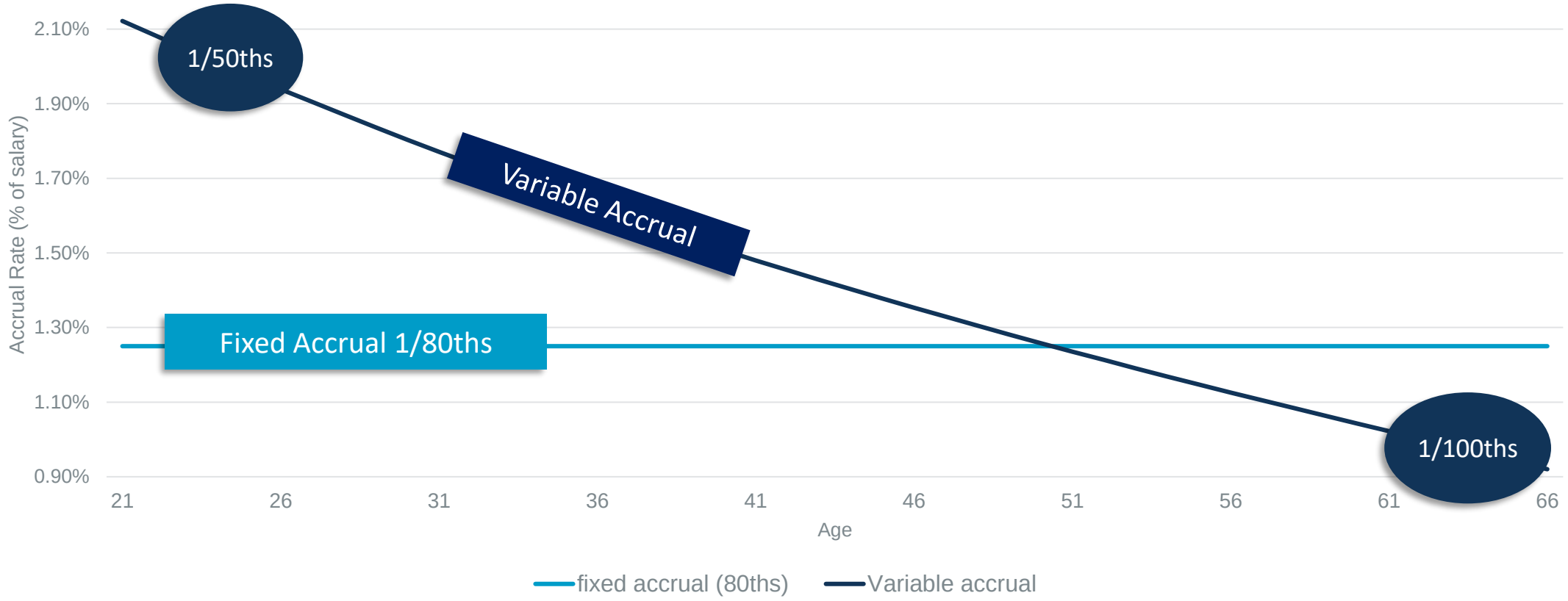
Institute and Faculty of Actuaries

7 Design Principles

1. Ensure there are clear design objectives from the start
2. Keep it simple
3. Compare the design with existing pension options
4. You will have to make compromises
5. Be deliberate when ‘designing in’ cross-subsidies
6. Analyse the reaction of benefits under the design to changes in circumstances
7. Consider sustainability of the design

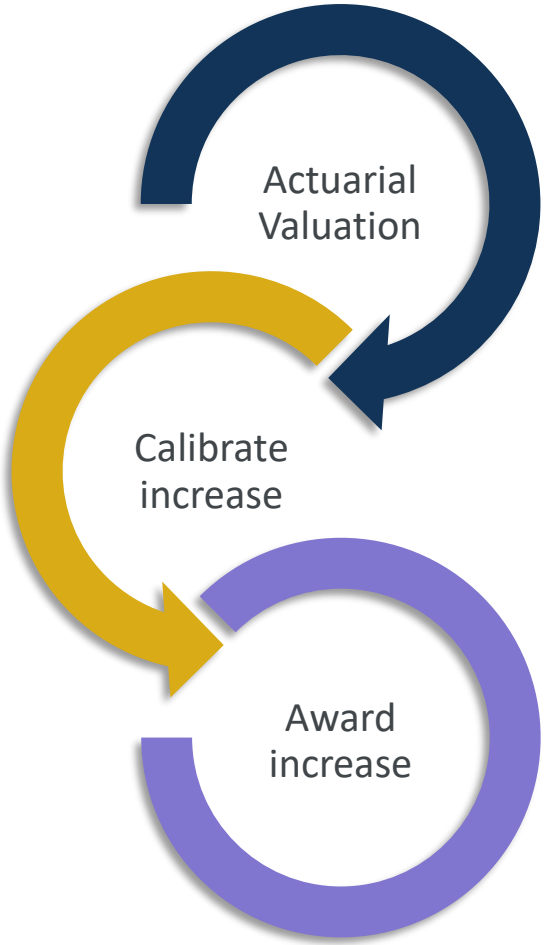
Institute and Faculty of Actuaries

Case Study 1 – Pricing Accrual



Institute and Faculty of Actuaries

Case Study 2 – Pension Increase Calculation



Each year the appointed Scheme Actuary performs a valuation with assets taken at market value

The present value of all accrued benefits is calculated using best estimate assumptions

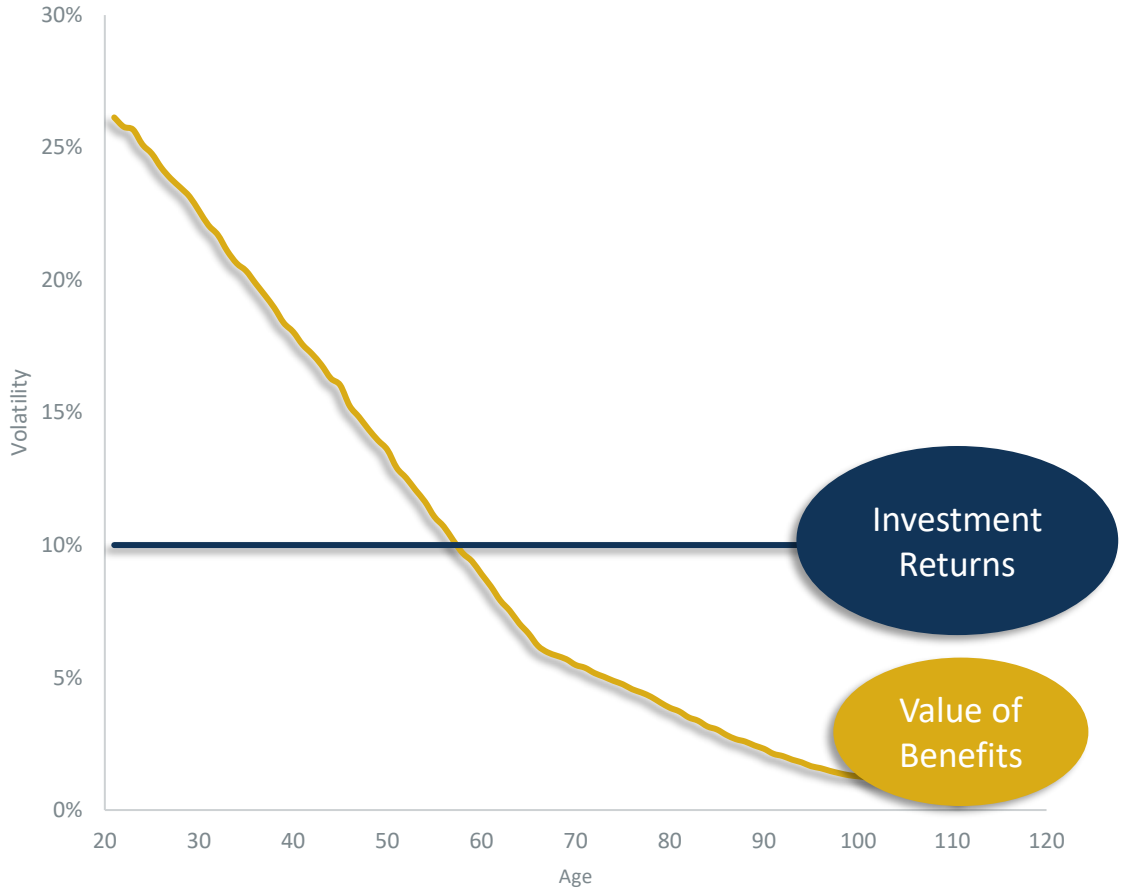
The future annual pension increase assumption is calibrated such that the assets = liabilities

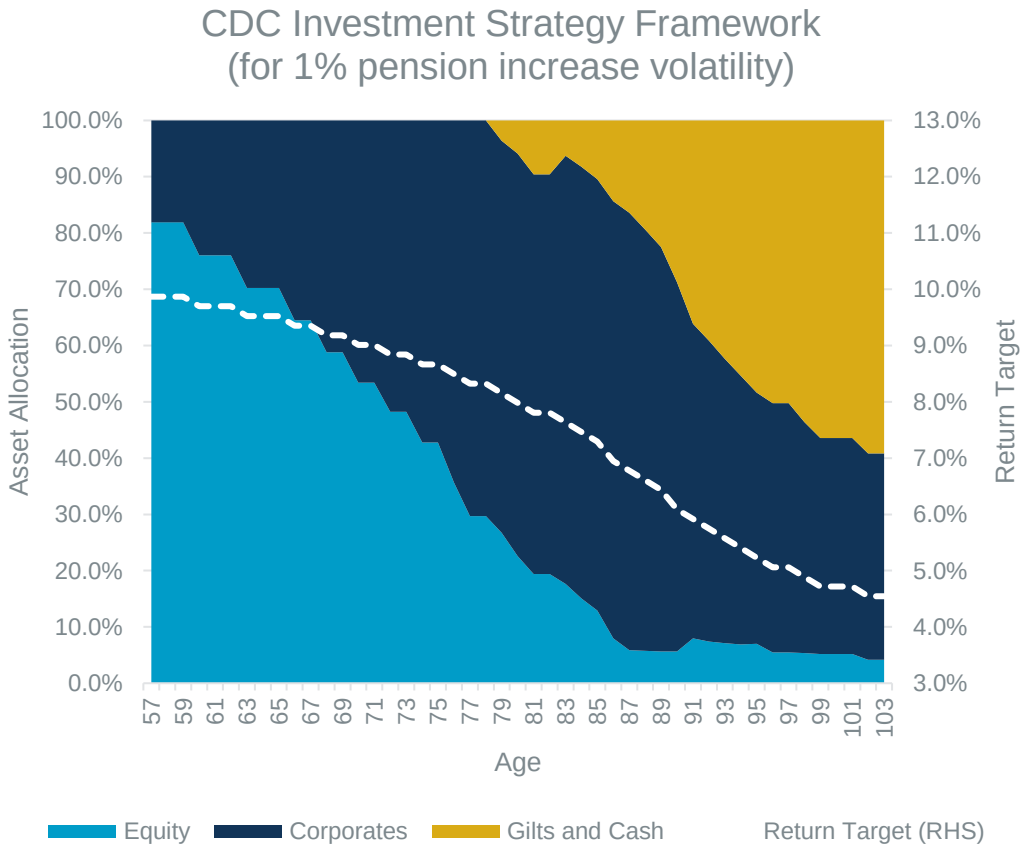
The calibrated pension increase assumption is then awarded as the actual increase for that year

All members receive the same percentage increase to accrued benefits (both non-pensioners and pensioners)

Institute and Faculty of Actuaries

Case Study 3 – Investment Pooling





Institute and Faculty of Actuaries

Next Steps

- Responding to DWP’s consultation on draft regulations for multi-employer CDC pension schemes
- Further thought leadership on CDC, including a focus on investments
- In-person session at Pension Seminar Day in May 2025

Institute and Faculty of Actuaries

Questions

Comments

Expressions of individual views by members of the Institute and Faculty of Actuaries and its staff are encouraged.

The views expressed in this presentation are those of the presenter.

Institute and Faculty of Actuaries

Institute and Faculty of Actuaries

Feedback