Global Pension Risk Survey 2019

UK Survey Findings

Hot topics: cyber risk and GMP equalisation

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Introduction

Welcome to the 2019 Global Pension Risk Survey findings concerning hot topics. These findings form part of our overall 2019 survey of UK defined benefit (DB) pension schemes.

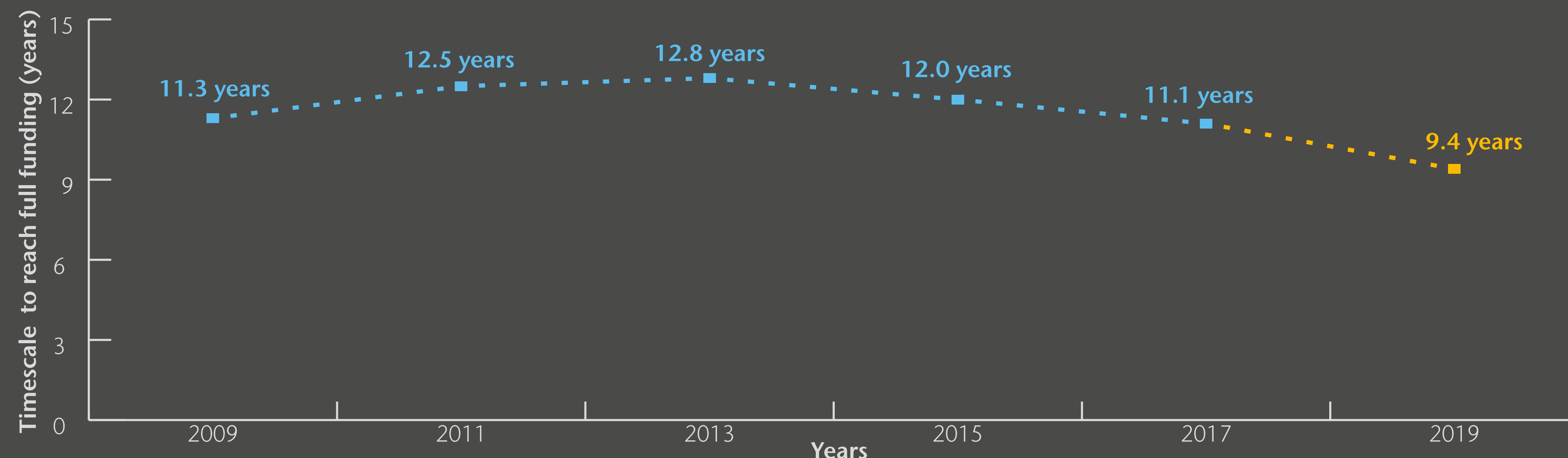
We carry out the Global Pension Risk Survey every two years, and looking back over the last decade, we can see how the pensions landscape has developed. Ten years ago, schemes were dealing with the fallout from the global financial crisis, and over the following years, increasing numbers of schemes closed to accrual in response to rising costs.

As a result, schemes began to set their sights on long-term, lower-risk destinations, but market conditions and, initially, rising longevity seemed to conspire against making progress. The ultimate low risk target forever seemed just out of reach. However, in recent years, schemes' long-term objectives have grown closer than they have ever been (see chart), as schemes mature.

Maturity is a key theme of this survey, as it is of many of The Pensions Regulator (TPR)'s recent statements, including the 2019 Annual Funding Statement. As many schemes see significant amounts of liabilities transferring out, they are maturing rapidly, and decisions around long-term targets, management of liabilities, investment strategy and approaches to hedging longevity risk have come more sharply into focus. Even open and less mature schemes will be affected by these changes as well as by the pressure from TPR to have a long-term target. There are also new issues for schemes to confront in 2019, including cyber risk and (finally) dealing with GMP equalisation after 2018's Lloyds Bank court case ruling.

In this set of findings, we look in detail at how schemes have wrestled with cyber risk and GMP equalisation. The survey findings relating to the other subject areas in the survey are available separately.

Timescale to reach long-term target as reported in previous Global Pension Risk Surveys

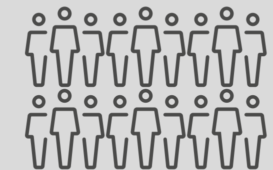


Unless otherwise indicated, all sources are the Global Pension Risk Survey 2019.

Survey demographics at a glance

170 UK respondents to the 2019 survey

15% of respondent schemes had fewer than **500 members**



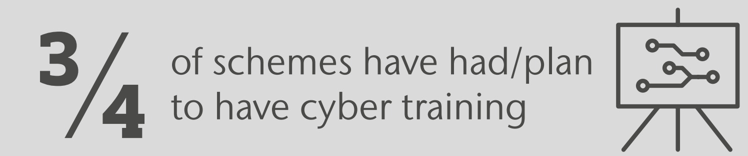
28% of respondent schemes had over **10,000 members**

Wide range of asset sizes covered.
From sub-£100m to over £1bn of assets

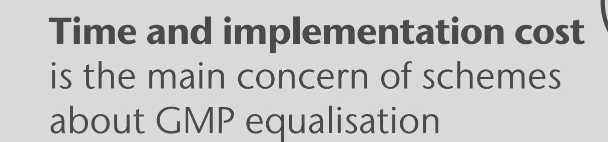
Nearly 2/3 of responses came from trustees

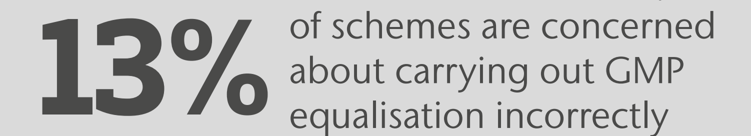
Hot topics

Key findings



2/3
have no documentation of cyber risks, mitigations and procedures





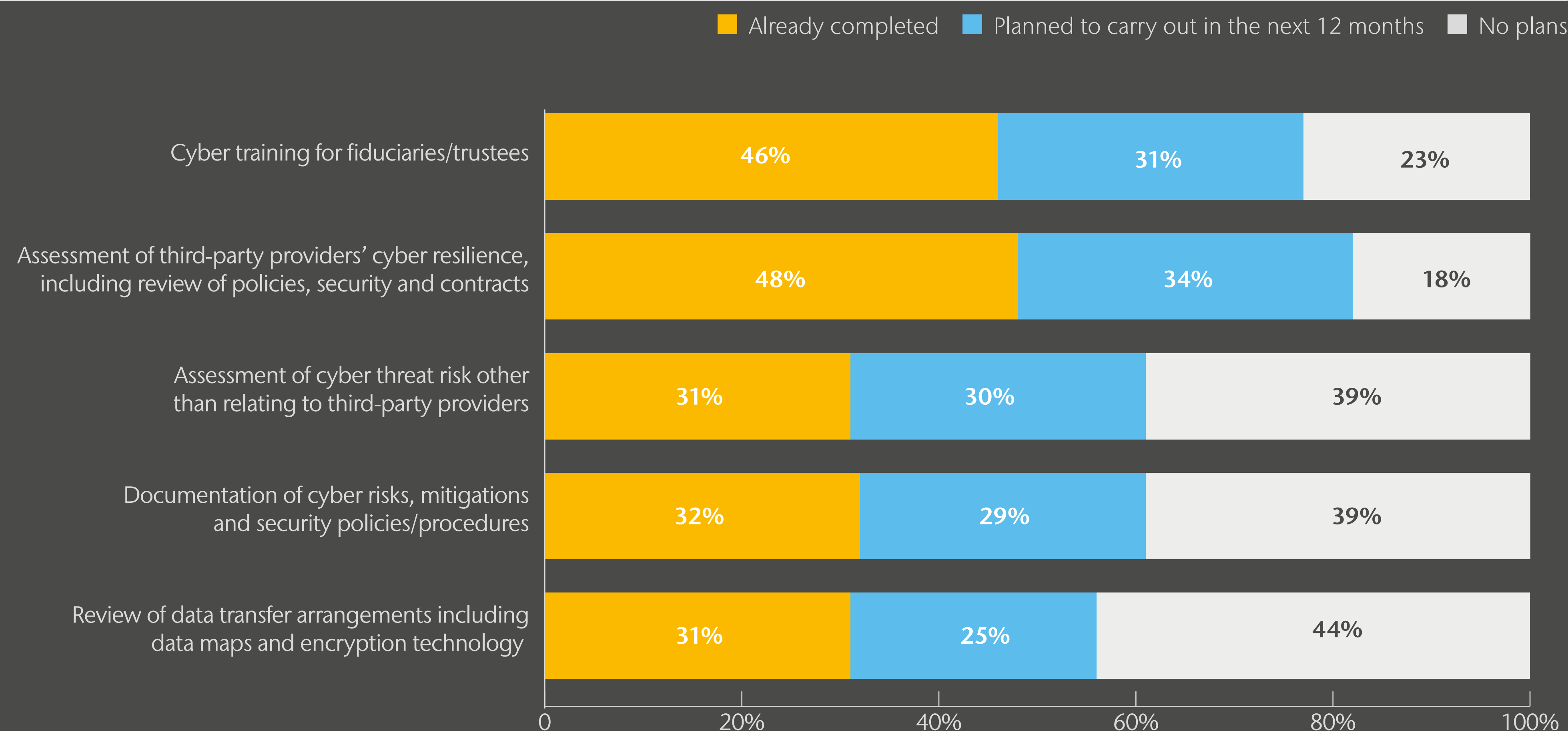
Hot topics | Cyber risk

Cyber risk is an increasing threat to modern businesses, and something that pension schemes are not exempt from. Thankfully, over 95% of respondents said that their scheme had not been affected by cybercrime, but a handful of respondents confirmed that they had been affected and, unfortunately, we expect that this figure is only likely to increase.

It was encouraging to see that three in four schemes have had cyber training or plan to have it in the next 12 months. We also see that almost half of schemes have already carried out an assessment of third-party providers' cyber resilience, with more on the way. However, that leaves a significant proportion of schemes (almost one in five) with no plans to act on this risk.

Two-thirds of schemes currently have no documentation of cyber risks, mitigations, and security policies and procedures. Broadly half of respondents have not carried out and do not plan to carry out a review of data transfer agreements. This seems especially high given recent GDPR requirements.

Actions to prevent a cyber incident



It was encouraging to see that schemes have been taking actions to prevent a cyber incident. As with the respondents to our 2018 Global Benefits Governance Survey, cyber security is clearly a priority. As a first step in understanding cyber threats to schemes, schemes should be carrying out an assessment of both themselves and third-party providers. Even this can be a challenging task as there are many processes to consider and most schemes have many providers.

An updated code of practice on internal controls is also due from TPR later this year, which we expect to include explicit references to cyber risks. This should be a call to action for schemes that have not taken any action to date, and we expect that these statistics will change when we come to the next Global Pension Risk Survey in 2021.

In more depth

We asked schemes questions to understand the plans they have in place to respond to a cyber incident.

To supplement training, within the next 12 months, half of schemes expect to have completed a 'war game' exercise where the participants discuss what actions they would take in the event of a cyber incident. Such exercises bring cyber risks to life as they help participants focus on the issues that matter to their scheme.

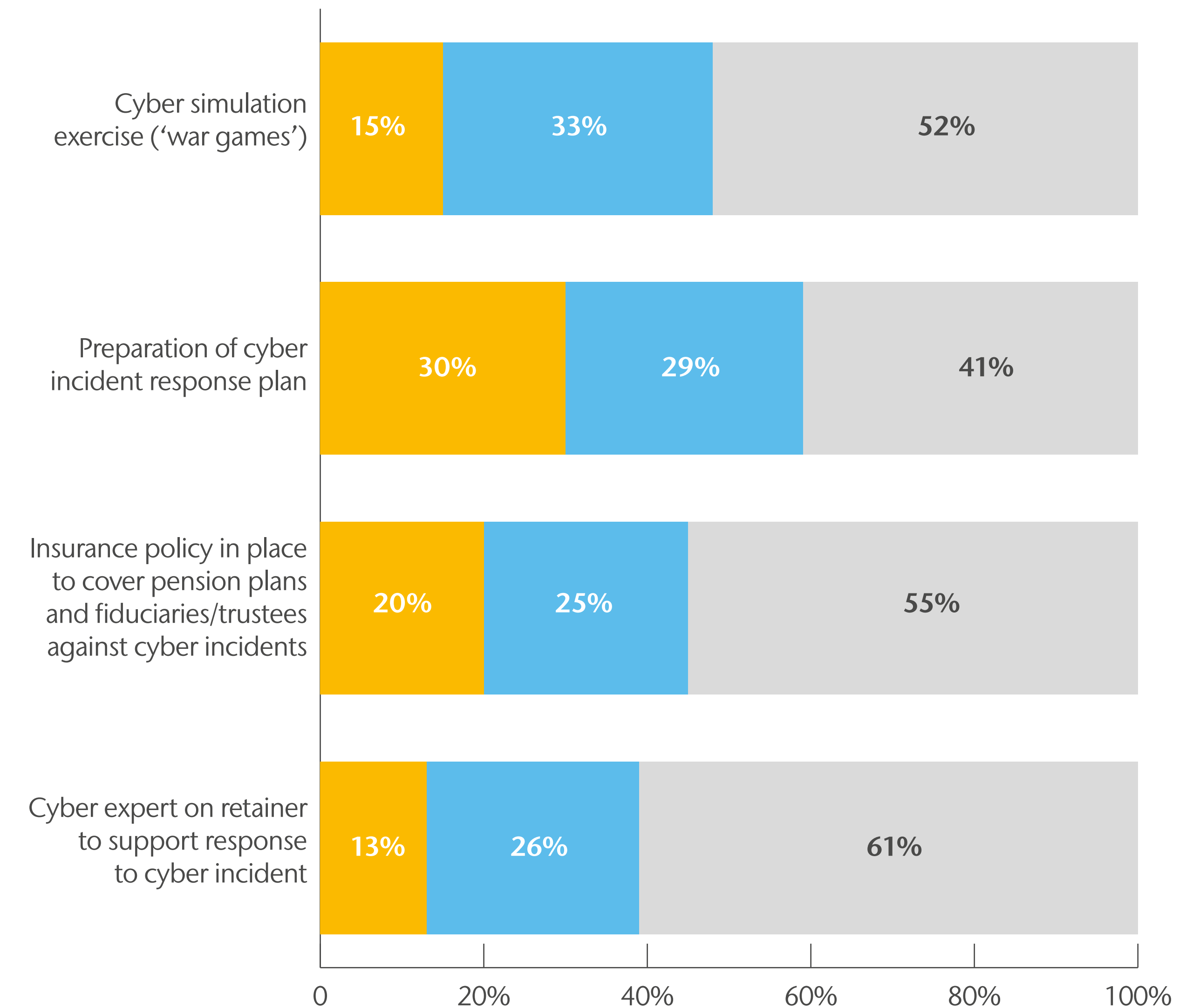
Surprisingly, over 40% of respondents have no intention of having a cyber incident response plan, despite TPR explicitly saying that schemes should have one.

When looking in more detail at the cyber risk results, we see that many schemes are yet to take action. We expect this is because cyber risk has only recently had more coverage in relation to pension schemes.

The lack of cyber insurance is not surprising. In fact, given the lack of cyber insurance in the market we are surprised that 20% of schemes believe they already have cover. With corporate policies usually not extending to trustees, and trustee liability policies only effective if there is a claim against the trustees, we suspect that actual levels of insurance are much lower than this survey suggests.

One of the most popular aspects of cyber insurance is access to an expert in the event of a cyber incident. It is encouraging to see some schemes putting this in place.

Actions in response to a cyber incident

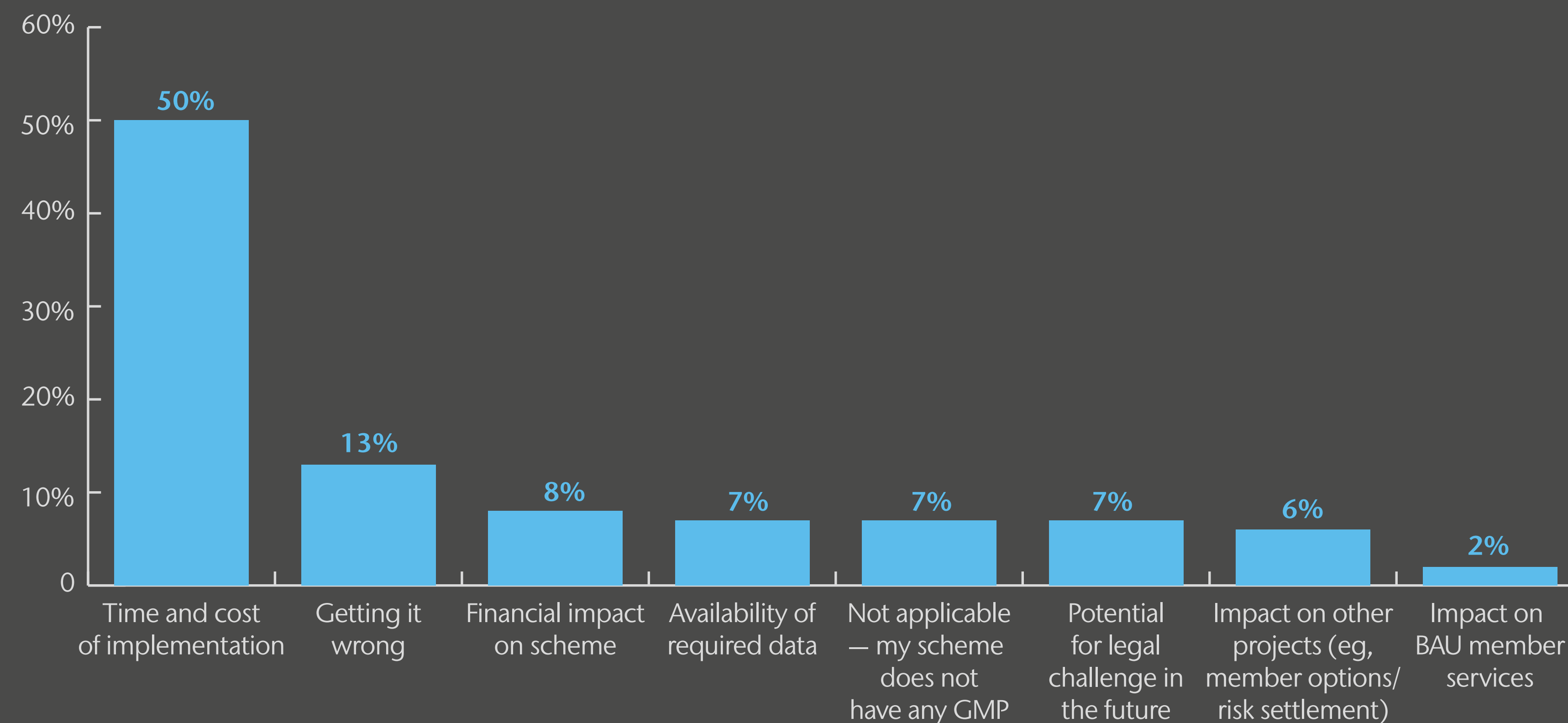


Hot topics | GMP equalisation

In October 2018, the High Court finally confirmed that Guaranteed Minimum Pensions (GMPs) accrued in private sector pension plans between 17 May 1990 and 5 April 1997 must be equalised between men and women. This will be a big project for schemes over the coming years because it involves looking back over such a significant period in the history of pension schemes.

As part of the survey, we asked respondents what their top three concerns were in relation to GMP equalisation.

GMP equalisation — main concerns



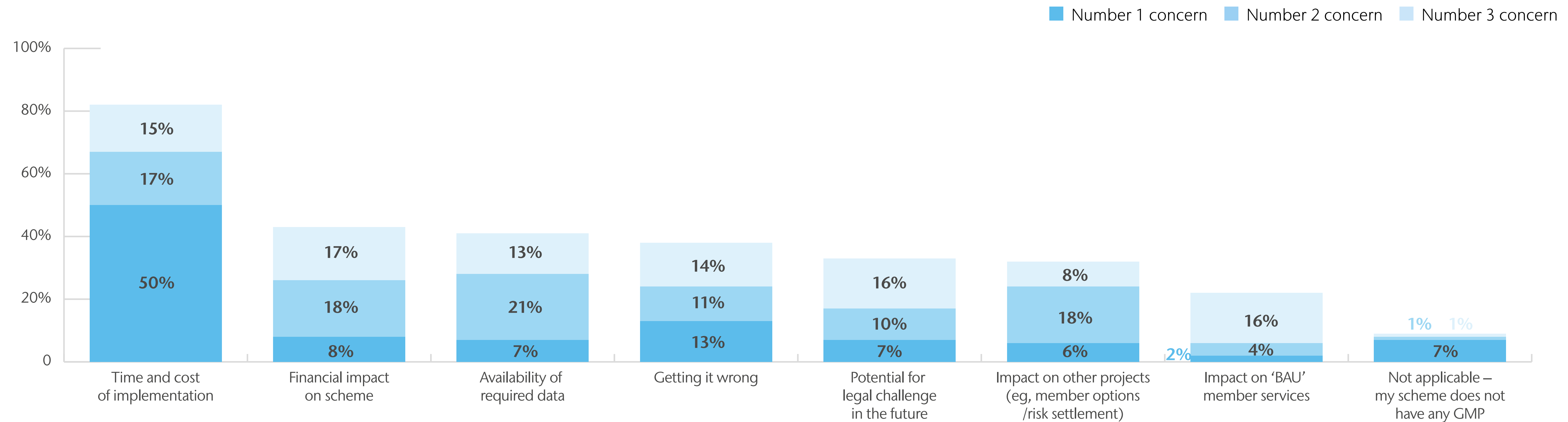
The time and cost of implementation was significantly ahead of other concerns, with 50% of schemes having it as their main concern. This was the main concern for small, medium and large schemes. The second most commonly-selected main concern was that the equalisation process would not itself be carried out correctly (13%).

The concerns over the time and cost of GMP equalisation are not surprising given the scale of the project; particularly as this is, in general, an unwelcome exercise for pension schemes. Key to managing costs will be effective project planning and management, and in July 2019 The Pensions Administration Standards Association (PASA) released a checklist that schemes can use to prepare for the project. Schemes that have not yet taken action can learn from the first movers in order to manage time and costs effectively.

It will be equally important to ensure that the equalisation process is carried out accurately, so no repeat work is needed. This risk can be managed by having experienced advisers who are close to industry developments.

In more depth

GMP equalisation — top three concerns



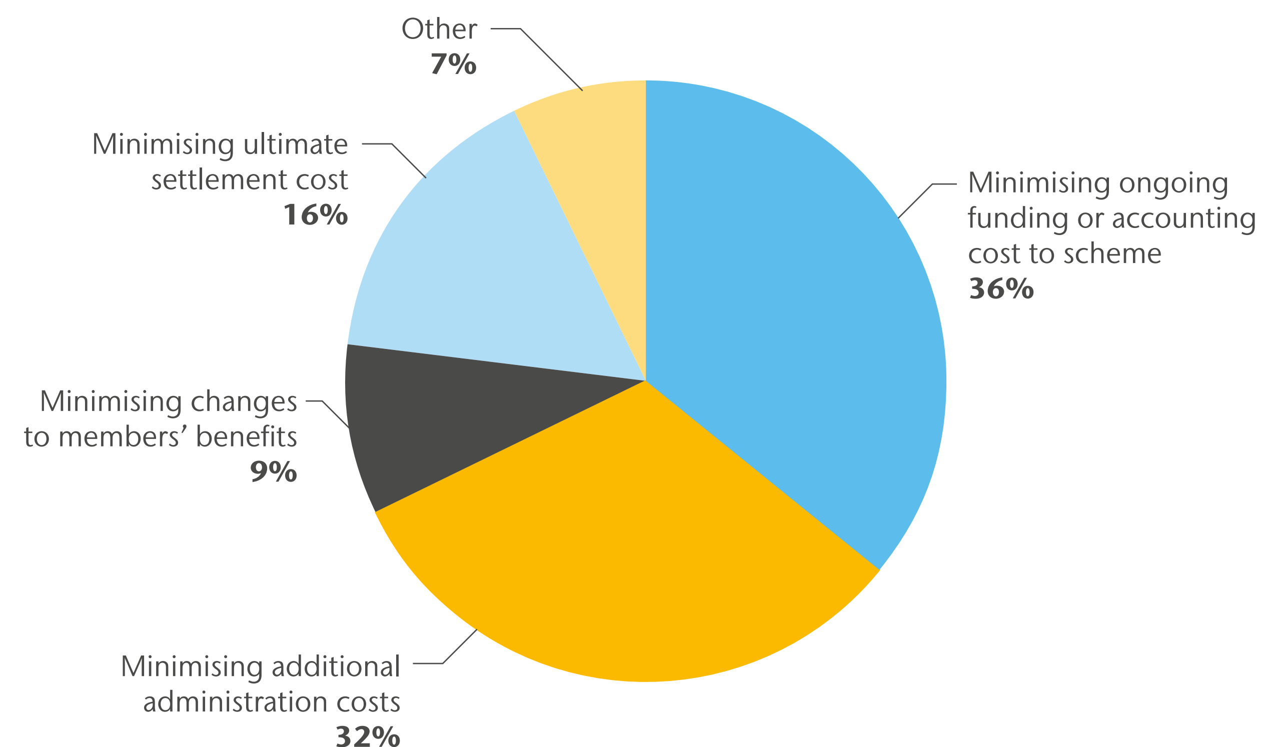
Looking in more detail to see what concerns respondents included in their top three, we still see that time and cost of implementation was significantly ahead of other concerns and was in the top three concerns for 82% of respondents. The next three biggest were the financial impact on the scheme, the availability of required data and the risk of getting the equalisation wrong, each being selected by around four in 10 respondents.

The financial impact has typically been a concern because sponsors need to include the additional liability in their profit and loss account. It can be material in that context, even if it is more modest in the context of additional scheme liability as a whole.

Data is a challenge for many schemes as the data needed is from many years ago. PASA is looking at guidance on how difficult-to-acquire or lost data can be managed.

As noted in the high-level results section, it will be essential that the equalisation is done accurately first time.

GMP equalisation — key considerations



The judge on the Lloyds case allowed a number of different methods to be used for GMP equalisation that used either a dual records approach or GMP conversion to deliver the newly-equalised benefit. Dual records is an administration solution that continues to compare the member and the equivalent member of the opposite sex over time, whereas GMP conversion converts the benefit into a new form to deliver the value of an equalised benefit.

Sponsors will have the right to decide whether GMP conversion is right for their scheme, but trustees have significant powers in setting any conversion terms, so in practice sponsors and trustees need to work together on setting the objectives for GMP equalisation projects.

In deciding which method to use, respondents' most important considerations were the ongoing funding or accounting cost to the scheme (36%) and the additional administration costs (32%).

These results echo the finding that the costs of GMP equalisation are a key concern. However, comparing the costs of the different methodologies will involve not just the accounting and funding costs, but also long-term administration cost impact compared to implementation cost. These are not easy comparisons to make.

It is interesting to note that despite buyout increasing in popularity as a long-term funding target, minimising the ultimate settlement cost was the most important consideration for only 16% of respondents, although it could be an important secondary consideration for many more.

We believe that action can and should be taken now to consider the information that can be gathered about data and benefits, even if it is more cost efficient not to rush too fast to implementation.

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