

Check against delivery

CBI Pensions Conference - how to balance defined benefit liabilities with corporate health?

Tuesday 23 June, Hallam Conference Centre, 44 Hallam Street, London

It is my pleasure to join today's panel at this CBI conference.

I look forward to the discussion and your questions but for now let me say a few short words.

In normal times, the relationship between regulators and business is an important balance to strike – affordability and prudence, between innovation and protection.

At all times, we need to deliver a consistent and coherent regulatory approach for the long-term.

And communicate and interact with UK Plc, with CBI members, in the best possible way.

Today, that relationship is critical. No one expected:

- interest rates of 0.5%
- multi-billion pound Bank of England asset purchases
- and Budget forecasts of negative growth of 3.5%

As we consider the affect of the economic cycle, we can consider the IMF view, *“The policy interventions in the UK, together with actions taken by other national authorities, have helped restore systemic stability in the financial sector.*

They look ahead..... *“Inter-bank term lending conditions have eased and some large institutions have been able to issue unsecured debt and fresh equity, suggesting improving confidence.”*

I hope that is right...I'm sure we all do.

In pensions we have set out to secure stability...critical to the economy, your members, to UK pensions...and running right to the heart of our approach.

Because the best security for a pension scheme is a viable employer, the best long-term security for a pension scheme is the enablement of that employer to play their part in the recovery.

That's the right choice for the pension scheme and for British Business.

And that has been my priority in recent months, and you'll have seen that reflected in the Regulator's activities.

So in February, we said more about flexibility and longer recovery plans and back-end loading.

And today, we issued a statement about valuations and the employer covenant as we return to London following a nationwide series of workshops....I have just come from a workshop where a couple of hundred people – over a thousand registered – are engaging directly with my front-line operational staff on exactly how we regulate; and our approach in these difficult times.

This is something the CBI was looking to see, and I want to thank you for your support.

Because, as we recognise, what started as a global credit crisis has caused severe detrimental affects for occupational pensions, with more uncertainty and cash constraint; our workshops, and the statement we will publish today which consolidates those messages into one place, are designed to help.

Now, let me preempt some questions....I want to touch on the issue of triggers.

I understand the rationale for the 8 point action plan....and I agree with John [Cridland] when he said, "longer recovery periods will help firms keep their commitment to pensions."

But the trigger is not a target – and however much I say it - it is a trigger and not a target.

Let me explain my position.

The regulatory system allows for flexibility in the structure and length of deficit recovery plans, where there are genuine issues of affordability.

So be assured, all recovery plans that come to us are looked at on a case-by-case basis.

And I know the CBI supports that specific approach and we also agree on this being fundamental to the UK – a real strength we must preserve if we are to get right that affordability question – because in Europe there are those who look to Solvency II for the answers and again we are united with the CBI against this.

So the affordability question is what trustees and sponsors must get right – which is why we have been going around the country and saying clearly – we expect trustees to engage in positive and open dialogue with their sponsor, using the principle of reasonable affordability to set payment schedules.

We stress the importance of setting strong technical provisions as a basis for the creation of a reasonable and viable recovery plan.

And we stress that liabilities are not flexible and trustees should not allow the current economic conditions to disguise the true cost of their scheme's liabilities.

So to date we have seen, and considered appropriate, recovery plans ranging in length from less than 1 year to over 20 years.

In each of these instances the particular plan length appeared sensible for the circumstances of the scheme and sponsoring employer concerned.

So the trigger is a trigger for scrutiny – and I accept that following my argument, as affordability challenges tighten, this means more scrutiny.

That's why, this year, we've preserved our commitment to doing more for less.

We have responsibilities to trustees, their members and to business....the UK economy and UK PLC needs long-term stability and sensible scrutiny – and that means effective regulation.

So I agree flexibility where appropriate and sensible; but I disagree that in the biggest economic crisis I've seen in my lifetime it would be responsible to move the trigger for scrutiny of recovery plans.

To do this would be to make the trigger a target, a moveable benchmark, a function of the economic cycle – that is simply not what it is for; and I don't think in the long-term this is the right choice for CBI members.

We should accept more scrutiny in a downturn and do so whilst managing our burdens on business down, looking to a counter-cyclical approach which utilises flexibility in the scheme funding system.

Today we have clarified in our statement – that builds both on our workshop experience and our messages in February on exactly how that can be done.

- We have emphasised the importance of prudence in setting technical provisions
- But we have also explained that the scheme specific funding regime is driven by the principles of reasonable affordability and flexibility - which means that the overall level of technical provisions should reflect the ability of the employer to support the scheme in the future. This is what we refer to as the employer covenant.

On top of this we note that

- Any recovery plan needs to take account of the ability of the employer to meet contribution commitments
- And where sufficient prudence and reasonable affordability has been established, a sensible consideration about the length of the recovery plan and schedule of annual payments can occur...that's the balance we need to strike.

Now let's touch just briefly on the issue of marked to market valuations.

Whilst the CBI has made calls for accounting valuations to be adapted to allow like-for-like comparison of scheme positions, we remain convinced that the marked to market approach has helped encourage transparency in valuations of assets and there is no robust case for moving from the current system.

We fully understand that the extreme volatility in market valuations causes difficulties for schemes, but also see that the other approaches have potentially profound drawbacks.

Finally, contingent assets...in the workshops we have heard questions around contingent assets and increased deficit reduction payments being made conditional on the future profitability of the

company, and we have said these can be considered - they may provide greater security and greater flexibility for the length and structure of a recovery plan.

So, I hope I have answered the difficult questions before they are asked.

But more importantly, I have tried to explain how we will continue to apply the flexibilities in the scheme funding system pragmatically...

...and will continue to provide ongoing support to all those managing occupational pension schemes in the UK.

Let me just add...in the spirit of openness, following on from our workshops we will be holding a web-cast in which Bill Galvin and June Mulroy will join me in discussing funding issues...I hope you can take a look on our website.

We will also publish a series of case studies later today which illustrate some common examples of funding issues, alongside the statement I referred to.

And very finally, our ongoing work on trustee knowledge and understanding continues and we are launching a new trustee toolkit module on 'buy outs and buy-ins on June 29' – which we hope you find useful.

In all of this, our aim remains to look for outcomes that are in the best interests of the scheme and sponsor...we hope to continue to do so with your support.

Let me put on record my thanks to the CBI, and appreciation for the challenge and effort of all trustees, employers, and members here today...thank you.