

CHAIRMAN'S MESSAGE FROM PATRICK BURKE

MARKETS AND THE FUNDING STANDARD



Patrick Burke

As the mid-way point of 2008 approaches the immediate challenges facing many of our members include the funding and accounting standard implications of the dramatic fall in equity markets experienced over the last 12 months. While equity markets may have stabilised somewhat in April and May the credit crunch, as evidenced by the widened spread on corporate bonds, has not gone away and the concern remains that a sustained recession may be pending and that earnings may disappoint in this event.

It is in precisely these circumstances that the strengths and weaknesses of the current Funding Standard mechanisms become most apparent. IAPF supports a strong and robust funding standard which assists trustees in the discharge of their duty to balance and safeguard the interests of scheme members. IAPF recognises that the Funding Standard enhances member confidence, can improve the technical framework for ensuring adequate contributions and can enhance overall funding and investment governance.

The interests and security of member benefits are put at risk by the mechanics of the Funding Standard which require that Funding Proposals be re-visited on an annual basis. Such requirements only serve to cause uncertainty and frustration on the part of sponsoring employers and multi-national parents and will undermine the sustainability of member benefits and the commitment of those employers to defined benefit strategies. IAPF understand the benefits of summary assessments and the arguments for disclosure of solvency levels on an annual basis and can accept annual oversight of this nature.

However, we call on Minister Mary Hanafin to immediately amend the mechanics of the Funding Standard which require the re-negotiation of Funding Proposals from one year to the next and we propose that

a triennial framework should be sufficient. The uncertainties and frustrations brought about by annual negotiations on such matters will only result in a reduction in the overall benefit levels of private sector employees.

Minister Hanafin comes to the Department for Social and Family Affairs with a strong record for resolving multi-faceted issues and we look forward to working with the Minister in promoting a sustainable regime for second pillar pensions, including these essential revisions.

In addition, we call upon the Minister to urgently review the requirement to mark solvency levels against the annuity rates of insurers operating under distinct regulatory and commercial regimes. Our view - supported by the OECD in its recent review of the Irish pensions system - is set out in our response to the governments Green Paper on Pensions where we propose that actuarial guidance should dictate the valuation basis for pensioner liabilities having regard to the cost to the scheme of the continuation of benefits.

Failure (or a political inability) to revise the fundamental mechanics of the Funding Standard valuation basis in this fashion will, in our view, necessitate other changes (e.g. the removal of future pension increases for future generations of pensioners from the Funding Standard) in order to introduce the flexibility necessary to ensure the continuation of defined benefit in the private sector.

ONGOING SUPPORT FOR MEMBERS

There is some comfort that recent liability valuations will have reduced in line with increased corporate bond yields and the IAPF Asset Allocation Survey 2008 clearly shows that many trustees had already implemented enhanced asset/liability matching and LDI strategies during the course of last year.

These difficult times highlight the importance

of our recent work in support of IAPF members through our general and specialist investment training courses, through our work with the Pensions Board towards the publication in March of our Investment Guidelines and through the high standard of our Investment Conference in April.

SOLVENCY II CONCERNS

Recent success on the policy agenda includes a significant improvement of the European Commissions position on the application of very onerous Solvency II funding requirements for funded pension arrangements. We remain grateful to Commissioner McCreevy and his Cabinet members for the time and attention which they have given to us in this regard. The broader proposal for a harmonised quantitative Solvency regime is unlikely to go away and IAPF continue to represent the interests of our members in the debate at European level.

GREEN PAPER

I am pleased to report the completion of our responses to the governments Green Paper on Pensions. The full text of our submission, as with all our research and publications, are available on www.iapf.ie.

RESEARCH

Our research commitments have been very significant over the past year including the Services Sector Survey 2007, the Benefits and Pensions Trends Survey 2007, the Asset Allocation Survey 2008 and the Defined Contribution Survey 2008.

TAX INCENTIVISATION - LIFE STRATEGIES REPORT

In addition, IAPF commissioned independent research on the costs and benefits of tax incentives and allowances within public and private sector pensions in order to improve the quality of public debate on how improvements to the State pension might be achieved.

For many years the IAPF has been concerned that simplistic modelling of historic data

and current cost accounting has failed to provide our policy makers with a clear view of the economic consequences of the various public policy options which might exist to enhance the State pension as our population ages.

Some work on these models was already completed as part of the National Pensions Review and the report presented to the IAPF by Life Strategies now confirms a number of key points in this debate:

1. The report quantifies the risk of comparing the relativities of proposed State Pension enhancements and the costs of tax incentivisation on a current cost basis; to do so grossly offends the principle of sustainability within the first pillar. In addition, the report establishes that the current cost of incentivisation is not directly transferable to the funding of first pillar pensions.
2. The net effective rate of tax relief granted through the incentivisation of private sector pensions is significantly lower for higher earners (and those high earners who contribute in higher proportions) while the greatest beneficiaries of the current taxation system are those in the public sector and those in low to medium pay grades (circa €40,000 p.a.) of the private sector.

3. The implementation difficulties for such proposals seem insurmountable given the BIK implications for the public service and the European direction for a harmonised pensions framework (EET).

4. There are serious issues arising for the sustainability of our State pensions. These issues are dominated by the increasing costs of State and public service pensions whereas the costs of private sector pensions (through tax incentivisation) remain static over the medium to long term and represent a reducing proportion of the total pensions cost base over this time.

A copy of the report has been submitted to the Commission on Taxation and included in our Green Paper submission and can be downloaded from the IAPF website at www.iapf.ie.

FOCUSING ON DC

Our increased focus on the needs of Defined Contribution sponsors and trustees continued during the first half of 2008 culminating in the publication of our Defined Contribution Survey, our Guidelines for DC Trustees & Members and our hugely successful first Annual Defined Contribution Conference.

IAPF welcome the appointment of Minister Brian Lenihan to the Department of Finance and will continue to call for the expansion of the ARF regime to Defined Contribution scheme members in all of our consultations with the Department of Finance.

Our continued promotion of DC adequacy continues as contribution and participation rates seem to be slowly rising and we are scheduled to publish an update to our DC Adequacy Booklet in the Autumn.

OUR PEOPLE

As you can tell just from this brief message (not to mention the Annual Dinner, our Annual Golf Outing, the Benefits Conference, our IT development, events, research, office and accounts management) the volume of work which has been undertaken over the last 12 months has been enormous. I remain hugely indebted to our office staff, our Council and our Committee members for their continued commitment and drive and look forward to completing our work programme for the year.

As ever, your feedback and suggestions remain hugely important to me and I invite you to contact me directly if there is any way you feel IAPF can enhance the quality and relevance of our services.