Pension Schemes Bill 2019-21: Collective Defined Contribution (CDC) Schemes
October 2020

- **Royal Mail Group (RMG) and the Communication Workers Union (CWU) are committed to implementing a Collective Defined Contribution (CDC) pension scheme** (called Collective Money Purchase (CMP) Schemes in the Pension Schemes Bill) for Royal Mail's c.141,500 UK employees.
- Royal Mail and CWU agreed to introduce a CDC pension scheme, combined with a guaranteed lump sum at the point of retirement, following the decision to close Royal Mail's Defined Benefit (DB) scheme in March 2018.
- **We believe this will provide the best possible pension arrangement for our people.** It will provide members with greater certainty about the retirement outcomes they will achieve than would be possible in a Defined Contribution (DC) scheme, while providing greater certainty about costs for employers than a DB scheme.
- **We welcome the opportunity to provide further evidence to the Public Bill Committee on CDC's merits.** We will continue to work closely with Government and parliamentarians across the House to ensure that the legislation inspires confidence in CDC schemes. We look to avoid anything which could deter other employers from launching similar schemes.

What is a CDC scheme?

CDC schemes, covered in Parts 1 and 2 of the legislation, pool the investment and longevity risks between members. Contribution rates for both the employer and the employee are fixed in advance. The scheme provides members with an income in retirement, on which the rate of increase varies. Each year there is an estimate of future pension increase levels but these are not guaranteed and pension reductions are possible in extremis. CDC schemes provide members with greater certainty about the retirement outcomes they will achieve than would be possible in a DC scheme, while providing greater certainty about costs for employers than a DB scheme.

RMG's proposed CDC scheme

Royal Mail and CWU agreed to introduce a CDC scheme, combined with a guaranteed lump sum at the point of retirement, following the decision to close Royal Mail's DB scheme in March 2018:

- Our scheme will follow similar auto-enrolment requirements to those in place for DB and DC schemes to ensure that no-one is left out from CDC's benefits in the future.
- Members will contribute 6% of pensionable pay and Royal Mail has committed to contributing 13.6% of pensionable pay.
- Ensuring intergenerational fairness is a priority for Royal Mail and CWU. Learning lessons from CDC schemes in other countries, our design features a funding and investment design which is robust to changes in circumstances, as well as benefit adjustment rules which treat each member in the same way.
- We will ensure that the nature of the benefit is communicated clearly to employees.
- The Bill is drafted to ensure CDC schemes are governed within a strict regulatory structure and only implemented once a clear governance and disclosure framework is put in place.

What are the benefits of CDC schemes?

- Due to the pooling of risk, they can take a less conservative investment strategy in members' later years, allowing for higher potential returns.
- Unlike DC schemes, they do not require members to purchase an annuity to receive an income for life in retirement and they can benefit from an overall reduction in costs through economies of scale.

- They can be simpler for members who are not faced with making decisions about investments or what to do with their benefits at retirement. Further, CDC schemes give employers a third option thus increasing choice.

Ensuring fairness in the provision of CDC schemes

We welcome discussions on how to ensure the fairness of future CDC schemes. Royal Mail's scheme is designed to address the possibility of intergenerational unfairness by not using capital buffers and explicitly preventing the trustees from favouring one group over another. The DWP acknowledged this in its 2019 consultation response. When it comes to Lord Sharkey's amendment, we agree with Government that we should give careful consideration to how reporting on fairness might work in practice and share their concerns with the additional reporting requirements the amendment introduces. We therefore support the Government amendment which removes Lord Sharkey's amendment from the Bill.

Covid-19 modelling

Modelling conducted by Willis Towers Watson and Aon shows that Royal Mail's CDC scheme would have provided better outcomes for savers through the current market conditions than traditional DC schemes. As such, Royal Mail and CWU remain committed to the introduction of a CDC pension scheme for employees at the earliest opportunity.

Support for CDC

As Government[1] notes, there is significant support for CDC schemes in the UK:

- **Confederation of British Industry (CBI):** "The CBI supports the creation of a third option to offer employers greater freedom to provide workplace pensions."[2]
- **Trade Union Congress (TUC):** "They [CDC schemes] should provide more security and predictability; they provide a straightforward way of generating an income in retirement, and they are likely to be cost effective and could offer better returns to savers".[3]
- **Royal Society of the Arts (RSA):** "These schemes benefit from economies of scale and can make longer term, mixed-risk investments. Studies by RSA and Aon Hewitt show that for the same contributions, CDCs can deliver 30% higher pension payments."[4]
- **Pensions Policy Institute (PPI):** "In the long-term, CDC produces better outcomes than DC. The PPI modelled CDC scheme also requires a relatively low contribution rate to maintain these outcomes."[5]
- **Institute and Faculty of Actuaries (IFA):** "The enablement of CDC would be a positive development for the provision of UK pensions, which would be in the public interest".[6]
- **Resolution Foundation (RF):** "We call for larger schemes that are better able to share risk among savers, and for the same reason support the government's promotion of 'collective defined contribution' (CDC) schemes."[7]

Next steps Royal Mail and CWU hope to see a swift Parliamentary passage so we can offer a CDC scheme to employees at the earliest opportunity. If you would like to discuss this further, please contact Fiona Hamilton, Head of Public Affairs, on fiona.hamilton@royalmail.com.

[1] Gov.uk press release on the introduction of CDC schemes in the UK: https://www.gov.uk/government/news/new-pension-scheme-could-deliver-improved-returns-for-millions
[2] CBI evidence to the Work and Pensions Select Committee: http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/workand-pensions-committee/collective-defined-contribution-pension-schemes/written/77625.pdf
[3] TUC, 'Three reasons why CDC pensions could mean a better retirement for workers': https://www.tuc.org.uk/blogs/three-reasons-why-cdc-pensions-could-mean-better-retirement-workers
[4] RSA, 'The case for CDC pensions': https://www.thersa.org/discover/publications-and-articles/rsa-blogs/2018/10/the-case-for-cdc-pensions--past-present-and-future
[5] PPI, 'Modelling Collective Defined Contribution Schemes': http://www.pensionspolicyinstitute.org.uk/publications/reports/modellingcollective-defined-contribution-schemes
[6] IFoA response to the Department for Work and Pensions: https://www.actuaries.org.uk/system/files/field/document/IFoA%20response%20to%20DWP%20consultation%20-%20Delivering%20CDC%20schemes%20-%20FINAL.pdf
[7] Resolution Foundation, 'More ambition, less risk – building on the success of auto-enrolment': https://www.resolutionfoundation.org/comment/more-ambition-less-risk-building-on-the-success-of-auto-enrolment/