

Why your company pension might not be so safe

*From David Stevenson, across the river from the City
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Company pensions are in big trouble.

UK company pension funds are now in the red to the tune of over £240bn - the biggest shortfall ever recorded. And here's the irony. It's partly due to QE – quantitative easing, the Bank of England's cash printing press, which is supposed to be bailing Britain out.

And there are even bigger pension problems looming. With the economy going downhill fast, more firms will go bust and the company fund deficit will just keep climbing.

OK, there's a back-up plan - the Pension Protection Fund (PPF). But will the PPF cope with the growing demands on it? And should you now transfer out of your company's final salary scheme?

QE hasn't helped pension funds at all, despite being the Bank of England's £150bn money-minting method for boosting the economy.

Here's why not. When the Bank began adding liquidity to the system by buying UK government bonds - gilts - it forced up prices, which in turn slashed yields to the lowest levels ever recorded. But rather than support big gilt-holding pension funds, it's done the opposite. Those funds now get less from their fixed-income assets than before, which means they'll need more money to meet their future liabilities.

More pension problems are looming

Mind you, QE isn't the only pension fund problem. Big share price falls have been adding to the shortfall by knocking large chunks out of the assets of company pension schemes. And while some share prices may recover, Deloitte's consultants warn that rising deficits could already require many employers to pony up higher pension contributions, which some cash-strapped companies may not be able to afford. No wonder 80% of schemes have closed their doors to new members.

But there's an even bigger problem looming. With the economy on a slippery downhill slope, more and more businesses will bite the dust. As Mehernosh Engineer at BNP Paribas puts it: "We expect a combination of further weakening in the economy leading to sharp profit declines, large and looming refinancing risk, and a further decrease in risk and bank lending appetite to lead to higher stress and defaults".

In other words, the business damage-to-date will look like a minor hiccup compared with what's in store. And this will further widen the total company pension fund deficit as 'underfunding' increases, i.e. the kitty will prove well short of what's needed to pay all the claims.

The Pension Protection Fund may not protect you

There is, of course, a backstop - the PPF (Pension Protection Fund), which is backed by levies on member pension funds. If companies go bust when their schemes are underfunded, the PPF pays out 90% of the pension you would have received, up to £28,000 a year.

But the PPF already has its hands more than full. Its losses have been stacking up, and there's a growing risk this pension lifeboat could itself be swamped, says the Guardian's Simon Bowers and Philip Inman. The government's under pressure to guarantee it, though with the public purse being stretched every which way but loose, there's not enough spare cash. "Rhetoric about guarantees has conspicuously disappeared", says Watson Wyatt's David Robbins, "with more ministerial speeches saying only that the PPF 'provides a safety net'."

In short, the PPF could be an accident waiting to happen. And rising worries about so many funds mean that it may be time to think the unthinkable. Such as transferring out of your company final salary scheme into a personal pension, known as a DC – defined contribution – plan, where you'd have much more control over your own money.

This could be a good time to go it alone

One reason this could be a good time to 'go it alone' is that some firms are now offering their employees sweeteners to ditch their company pensions, says the Sunday Times' Jennifer Hill.

And here's the rub. By forcing gilt yields down so low, QE is now opening up an unprecedented window of opportunity. Because for exactly the same reason that it's made life harder for your employer's scheme, i.e. with more money being needed to pay for your eventual pension, QE has pushed up the transfer values you'd now receive. These soared by as much as a staggering 31% in March alone, says Hill, quoting First Actuarial data.

Clearly, while transferring depends on the solvency of your employers' scheme, there are risks. The decision is final, i.e. you can't reverse it. You'd want a new personal pension to match up to what you should get by staying put. It also depends on individual circumstances, so you should consult a financial advisor before taking the plunge. And check out the useful Pensions Advisory Service. But with many company schemes, and the PPF, looking ever dodgier, it could be well worth considering...