DESIGN OF PENSION ARRANGEMENTS TO MITIGATE LONGEVITY RISK

Working Party on Private Pensions

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OECD

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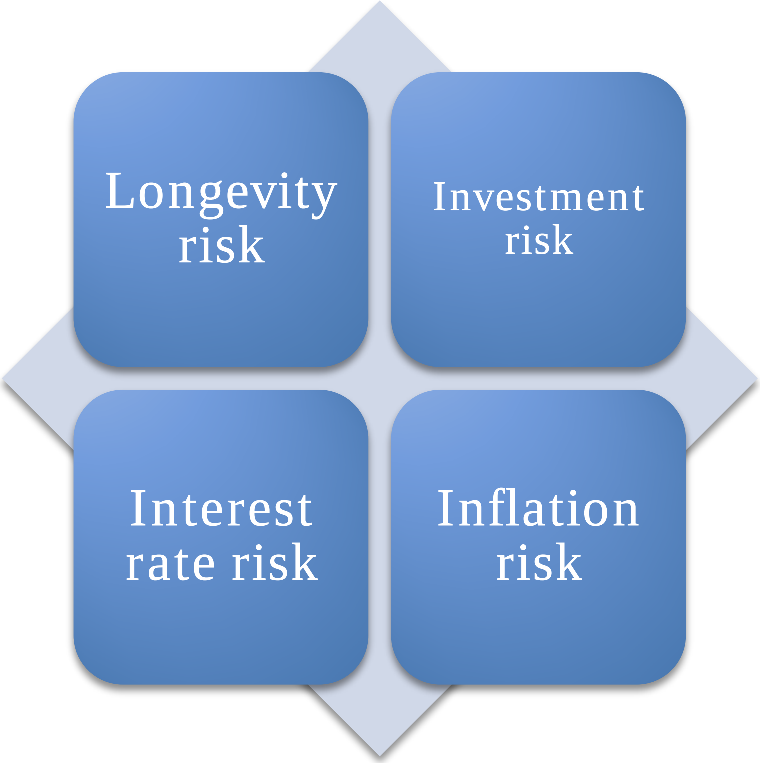
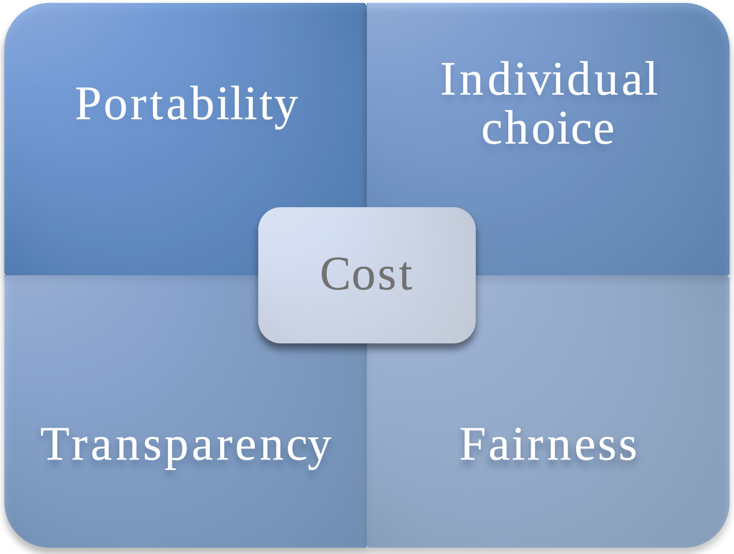
Project on designing pension arrangements to address longevity risk

- Structures to manage longevity risk
  - Classification and design features
- Regulatory requirements
  - Reserving and solvency, discount rates
- Understanding the transition to payout
  - Communication of options, process, entities involved
- Assessment of structures
  - Cost of implementation, consumer benefit
- Policy implications

Risk-sharing of different types of pension arrangements and features

Risks fully transferred to provider → Risks shared between members and provider → Risks shared collectively among members → Risks borne individually by members





Taxonomy

- **Risks fully transferred to provider**
  - Traditional DB
  - Traditional annuity products
  - Longevity insurance
- **Risks shared between members and provider**
  - Annuities with minimum guarantee
  - Hybrid DB
- **Risks shared collectively among members**
  - Target benefit schemes
  - Collective individual DC schemes
  - Tontine-type schemes
- **Risks borne individually by members**
  - Individual DC

Key differences between types of schemes that share risks between sponsors and members

- Annuities with minimum guarantee
  - Insurance regulatory framework
  - Benefits framed as minimum income plus expected bonus payments
  - Liabilities are hard guarantees
- Hybrid DB plans
  - Pension regulatory framework
  - Benefits communicated assuming all conditional benefits will be paid
  - Liabilities valued based on expected payment

Key differences among types of schemes that share risks among individual members

- Target benefit schemes
  - Covers accumulation and pay-out
  - No de-risking of investment
  - No individual choice in investment or speed of drawdown
  - Investment risks sharing across time/generations
- Collective individual defined contribution
  - Collective investment in pay-out only
  - Flexibility around investment strategy and speed of drawdown
  - Intergenerational risk sharing limited
- Tontine-type schemes
  - Focus on pay-out
  - Low-risk investment
  - No individual choice around drawdown speed

Main observations

- Trade-off between cost and certainty of benefits
  - Risk-sharing can result in higher pensions, but pension levels are not guaranteed
- Increased risk sharing tends to reduce flexibility…
  - Collective management of assets can lead to higher pensions, but at the cost of individual choice
  - Portability must be restricted in pay-out to effectively mitigate longevity risk
- …and may present challenges for individuals
  - Tends to decrease transparency
  - May be seen as inequitable across generations

Next steps

- Regulatory requirements
- Transition from accumulation to payout

➢ Would a survey be feasible to collect information on these aspects?

THANK YOU!

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