**Supplementary evidence from Aon (APS0066)**

The primary issue for savers is that the future is uncertain and so, however well thought-through the predictions of the future are, the future will be what it will be. Guaranteed pensions are underwritten by the employer (defined benefit (DB) pensions) or the insurer (annuities). In either case, it is that entity that bears the risk of worse than expected performance, and because of this the price is high for guaranteed pensions. Through the behaviour of employers and individuals actively selecting to close DB pension schemes or not to buy annuities at retirement (respectively), we can be confident that the (large) majority consider guaranteed pensions to be more expensive than they are prepared to pay for. Consequently, forms of pension scheme that are not guaranteed have to be the way forward to meet the needs of the majority.

Additionally, as I referenced in my evidence, the personal longevity risk each of us bears is very material. What I mean by this is that although *average* life expectancies can be assessed reasonably accurately for large groups of people, the uncertainty around that average for an *individual* is large. For example, there is approximately a 50% chance of a 65 year-old dying sometime between seven years earlier and seven years later than their average life expectancy. And yet individuals understandably wish to ensure their pension income meets their *actual* lifespan, so they do not underspend if they die early, nor exhaust their savings if they die at a greater age.

CDC is the only pension design I am aware of that addresses both of these issues. It does this through pooling risk, a familiar technique that underpins insurance.

CDC does not rule out the possibility that pensions must be reduced if experience does not meet expectations. This represents a clear communications challenge, although it is one I believe is over-emphasised because the same risk exists with income drawdown products but without attracting much attention.

One witness referenced the negative Dutch experience with their form of CDC. UK CDC was designed in the knowledge of the experiences of similar pension plan designs in other countries, so I do not believe the Dutch experience is relevant to the UK. One example of this is that under the draft UK CDC regulations currently under consultation, it will not be possible to react to unexpectedly poor experience by increasing the contribution rates of active members. However, this was the case for many Dutch CDC schemes following the financial crisis as a consequence of the Dutch CDC solvency rules. This meant that restoration of the funding level was met by rises in the contribution rate paid by the active members, who by definition were the younger members. But restoring the funding level benefited all members, young and old. Inevitably, younger members found this inequitable.

In summary, there is great demand from savers for an affordable pension for life and CDC has the prospect of meeting that demand. Commercial CDC vehicles (ie for-profit Mastertrusts) would ensure access to CDC for all savers, including the self-employed. But as one witness noted, specific checks and balances on commercial CDC vehicles would be required to ensure the interests of the commercial entity are aligned with the interests of savers.

The Government has taken a big step to introduce significant new legislation to enable CDC pension schemes. These types of schemes are new to the UK and will remain so for some time before a significant track record is built up. However, they represent a milestone of much-needed innovation in UK pensions, and, in my view, it is important that the Government presses on to introduce the

regulations required to extend the reach of these new schemes to commercial CDC schemes, in order that access to this type of pension benefit can be enabled for all savers.

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