COVID-19 and Impact on Retirement Plans (20 March)

The management of the impact on retirement plans is also coming to the fore (especially by companies with specialist pension managers or large DB/DC retirement plans) as we see employees asking about the impact on their own retirement income and many companies approach a quarterly reporting date.

We have identified eight key retirement-related areas which are outlined further below. There are a number of key items and risks that companies will need to consider around the world; international companies will need to decide what to prioritise, assign tasks to specific individuals, and ensure work is being done locally.

1. Managing costs and cashflows

Companies may face increased demands for extra pension contributions. The market turmoil may lead to increased funding deficits in some countries. In others, pension plan boards may put in requests for additional capital if they are concerned about the strength of the company. Companies may want to discuss use of other options depending on what is allowed locally, such as renegotiating funding plans, deferring cash commitments or using contingent assets (e.g. in the UK, Germany, Ireland, Belgium, Canada); filing for relief where contributions mandated by law (e.g. in the US); or suspending or reducing pension indexation (e.g. in the Netherlands, Germany).

Companies should also look at pension costs that may be triggered in the event employees are made redundant or offered early retirement.

As an extreme measure, we anticipate some companies may consider closure of some remaining defined benefit schemes to accrual if these are already closed to new hires, if the costs of these are significant, and the company has closed defined benefit plans in other countries. This would not be a trivial exercise, and careful employee consultation and communication would be needed.

2. Impact of unpaid leave and redundancies

Many employers may ask employees to take unpaid leave. Companies should consider the impact on retirement plans, e.g. should pension contributions and benefit accrual continue; can employees still pay voluntary calculations; how will this impact pensionable service and final pensionable pay calculations; will company matching contributions continue, etc. In some cases, plan rules may need to be amended to allow pension membership to continue for those taking unpaid leave.

Employers making redundancies should additionally consider the impact on retirement and savings plans – for example, given extreme market volatility and the knock-on effect on investments, will affected members be able to remain invested in the plan and defer drawing benefit?

3. Managing retirement assets

The large falls in assets, falls in bond yields, and increases in credit spreads have had a massive impact on retirement assets. Aon's Asset Allocation recently (17 March) ran a webinar exploring the recent market movements and how pension scheme investment portfolios should be reacting. You can listen to a replay of that webinar here.

4. Managing retirement liabilities (including IAS19 and US GAAP)

Retirement liabilities are also impacted. Liabilities calculated by reference to long-dated government bond yields (e.g. funding liabilities in many countries) will have gone up whereas some companies may find that their IAS19 and US GAAP liabilities have gone down (due to increases in corporate bond yields driven by increased credit spreads). Such increases may only be temporary if credit ratings of companies used to set the discount rates change at the end of this month, and this results in a fall in high quality corporate bond yields.

5. Regulatory intervention

Pension regulators in a number of countries, including the UK, Netherlands and Denmark, have recently issued guidance and/or new requirements to pension funds on how to navigate the current financial market turmoil. Pension funds are being asked to review their business continuity plans, and pension funds and employers will need to consider the impact on scheme funding and, in countries such as the Netherlands, conditional indexation and rights cuts. Trustees of UK plans are likely to need specific information to help assess the impact on UK deficits, and whether any additional funding may be needed – in turn, some employers may be wanting to temporarily reduce UK funding commitments if financial pressures elsewhere have increased. We expect both trustees and employers to need advice on this.

6. Crisis resilience and virtual meetings

Aon has compiled ten questions to check the resilience of your retirement plans addressing areas such as cash management, integrated risk management and contingency plans. These are available for both Defined Benefit (DB) and Defined Contribution (DC) retirement plans.

7. DC plans and financial wellbeing

Employees close to or at retirement may find their expected retirement income may be significantly lower than would have been the case a month ago. This will depend on the underlying mix of investments in DC portfolios, and how they plan to use their funds to secure an income in retirement. Some employees may find that they can no longer afford to retire, and may want to carry on working and delay their retirement. Younger employees may be concerned on large drops in values in their retirement accounts, and may make rash decisions on investment choices.

Employers will need to consider what to communicate, and how given the increase in home working, to employees in DC plans who are concerned about the market falls, especially those close to retirement.

8. De-risking, member option and buy-out/buy-in projects

The market turmoil could have a significant impact on the pricing of de-risking and liability settlement projects. Employers and trustees may need to review execution strategies and consider the impact on any transactions involving insurers.

About Aon

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