

## News Alert 2011/01

3 March 2011

### *ECJ bans sex discrimination in insurance pricing*

#### *At a glance*

On 1 March 2011 the European Court of Justice (ECJ) delivered its [judgment](#) in the Test-Achats case. Gender discrimination in the pricing of insurance is outlawed as from 21 December 2012. This will have a knock-on effect to pension schemes, but the extent and the timing of some of this is uncertain.

#### *Key Actions*

---

##### **Trustees**

Get legal advice on how the ruling may impact your scheme and whether any current practices need urgent review. It is currently unclear whether the ruling will extend from the insurance field to benefits provided within occupational pension schemes and, if it does, the timing of the extension. However, trustees will want to understand the legal risks and how to manage them.

---

##### **Employers**

Consider taking advice on the effect of the ruling on the costs of your pension scheme and other relevant insurances. Employers with de-risking strategies in train will want to understand whether or not the ruling will impact them.

---

##### **Pensions manager**

Develop, with advice, an understanding about how the routine management of the scheme may be affected and whether it would be appropriate to pre-empt any future compulsion by moving to unisex bases sooner rather than later.

---

#### *The Detail*

##### **The ruling**

The ECJ has ruled that from 21 December 2012, taking the gender of an insured individual into account as a risk factor in insurance contracts constitutes unlawful sex discrimination.

[EU Directive 2004/113](#) prohibits sex from being taken into account as a factor in calculating insurance premiums and benefits in respect of insurance contracts which are

concluded after 21 December 2007. However, that Directive makes provision, in Article 5(2), for Member States to permit sex-specific differences in insurance premiums and benefits insofar as sex is a determining risk factor that can be substantiated by relevant and accurate actuarial and statistical data. This aspect of the Directive is subject to reassessment by 21 December 2012, but as currently expressed, appears to permit the above “opt-out” to continue indefinitely.

The UK took advantage of this opt-out and the current domestic provisions are set out in the Equality Act 2010.

The ECJ has now ruled that Article 5(2) is counter to higher-ranking EU law, particularly the [Charter of Fundamental Rights of the European Union](#). It has held that Article 5(2) is invalid as from 21 December 2012.

#### Nature of the transition

Although from 21 December 2012 it will not be lawful to use gender-based factors in calculating insurance rates, it is not clear whether this also means that contracts in force at this date with continuing premiums are affected, and if so how.

#### Impact on annuities and pension benefits via the insurance market

The ruling has some implications within the pensions field from 21 December 2012, although insurers may start to price for the new legal reality now.

- There will be a direct and possibly immediate effect upon individual annuity pricing. An individual seeking to purchase a single life annuity is likely to be affected; men may lose and women may gain. As the effect is likely to be less marked with joint life annuities, men may be incentivised to buy such benefits. There is also the possibility that, in aggregate, all individuals lose, as insurers seek to mitigate selection risk and re-balance cross-subsidies in their annuity book. Certainly, over the coming months the current logic for annuity shopping becomes even more compelling, with insurers likely to react differently and at different speeds.
- It is possible that the revised income drawdown limits, effective from 6 April 2011, that were settled last month, will need to be revisited; otherwise men will be able to continue to take a greater maximum income from drawdown products than women. They may need to be revised anyway if annuity pricing moves to unisex ahead of 21 December 2012.
- Although premiums for life assurance cover may now move in favour of men and against women, it is thought that the movements will be slight given the ages and short durations over which such contracts are typically taken out. The same may be true for other insured “risk benefits”.
- For defined benefit schemes considering de-risking, because the grantee of an annuity policy will often be a trustee body, not a legal person having gender (and in

any case members' benefits should be unaffected), it is not currently thought that the ruling will materially affect bulk annuity products. We therefore currently anticipate that there should be little immediate impact on annuity buy-in and longevity swap products. However, there may be an impact where policies are purchased in the names of members, and there may also be impacts where policies for deferred pensioners include allowance for the cost of "options" such as cash commutation at retirement and transfer values.

- If bulk annuity products are little affected this will mean that there will be little impact on associated occupational scheme calculations, such as employer debt payments and solvency estimates. An early indication of the validity of this premise may be the outcome of the Pension Protection Fund's review of assumptions for PPF entry and levy calculations, where a clear marker has been put down within the proposals issued last month that they may have to be adjusted in the light of the judgment.

#### Impact on benefits inside occupational pension schemes

The impact of the judgment may extend beyond the gender-based pricing of insurance contracts and apply directly to the use of gender-based factors in occupational pension schemes insofar as they impact individual benefits. For example, this might include cash commutation factors and transfer value factors. This is because the logic that the ECJ has applied in the Test-Achats case would seem to be equally applicable to other areas where sex discrimination is currently permitted.

Quite when "within scheme" pension benefits may be affected is uncertain, with early indications being that legal opinion is currently somewhat divided. But it does seem that the judgment makes it more difficult to defend existing sex-based practices on an ongoing basis.

The legal mechanism for an extension to pension scheme benefits may be a reference by a national court to the ECJ or an amendment by the EU to a Directive. One would hope that any decision would not be backdated, but there is a possibility that it might, with Test-Achats applying automatically, as from 1 March 2011 (the transitional period up to 21 December 2012 may turn out to apply narrowly to insurance).

If and when the extension happens, the following common gender-based terms of occupational pension schemes will have to move to a unisex basis:

- Cash commutation rates applicable on retirement;
- Early and late retirement factors – but many schemes operate on a unisex basis already; and
- Factors for converting transfers-in and DC additional voluntary contributions to defined benefit rights.

It may also be appropriate to adjust the actuarial basis underlying transfer values so that they become unisex. This could be on the premise that these days, to transfer benefits from a defined benefit scheme is generally also to transfer into a defined contribution arrangement where it is the pot that counts.

If legal advice points towards the risk of an immediate extension to pension scheme benefits, some individual transactions may need to be suspended whilst their calculation bases are re-assessed.

If and whenever the extension to pension scheme benefits occurs it should still be possible for pensions actuaries to use gender as one of the parameters when making assessments of the scheme's liabilities, such as when setting the technical provisions for a scheme funding valuation.



#### Comment

*The thrust of this judgement is predictable in terms of how individual private insurance contracts are priced. What is intriguing, or perhaps even disturbing, from the pensions standpoint is the potential for the ruling to directly impact occupational pension schemes from an as yet unknown date.*

*With trustees already looking nervously towards being forced to eliminate benefit inequalities arising from guaranteed minimum pension requirements it seems that sex discrimination issues will loom large through 2011.*

*There is also an exemption regarding age discrimination in the relevant European Directive upon which is built an edifice of exemptions for typical age discriminatory practices in UK pension schemes. We wonder whether the wind is blowing in such a way that a number of these exemptions will also come under judicial scrutiny.*

This News Alert should not be relied upon for detailed advice or taken as an authoritative statement of the law. If you would like any assistance or further information on the contents of this News Alert, please contact David Everett or the partner who normally advises you at LCP on +44 (0)20 7439 2266 or by email [enquiries@lcp.uk.com](mailto:enquiries@lcp.uk.com)

[www.lcp.uk.com](http://www.lcp.uk.com)

LCP is a firm of financial, actuarial and business consultants, specialising in the areas of pensions, investment, insurance and business analytics.

Lane Clark & Peacock LLP  
London, UK  
Tel: +44 (0)20 7439 2266  
[enquiries@lcp.uk.com](mailto:enquiries@lcp.uk.com)

Lane Clark & Peacock LLP  
Winchester, UK  
Tel: +44 (0)1962 870060  
[enquiries@lcp.uk.com](mailto:enquiries@lcp.uk.com)

Lane Clark & Peacock  
Belgium CVBA  
Brussels, Belgium  
Tel: +32 (0)2 761 45 61  
[info@lcpbe.com](mailto:info@lcpbe.com)

Lane Clark & Peacock  
Ireland Limited  
Dublin, Ireland  
Tel: +353 (0)1 614 43 93  
[enquiries@lcpireland.com](mailto:enquiries@lcpireland.com)

Lane Clark & Peacock LLP  
St Helier, Jersey\*  
Tel: +44 (0)1534 887600  
[enquiries@lcp.uk.com](mailto:enquiries@lcp.uk.com)

Lane Clark & Peacock  
Netherlands B.V.  
Utrecht, Netherlands  
Tel: +31 (0)30 256 76 30  
[info@nl.lcpeurope.com](mailto:info@nl.lcpeurope.com)

LCP Libera AG  
Zürich, Switzerland  
Tel: +41 (0)43 817 73 00  
[info@libera.ch](mailto:info@libera.ch)

LCP Libera AG  
Basel, Switzerland  
Tel: +41 (0)61 205 74 00  
[info@libera.ch](mailto:info@libera.ch)

LCP Asalis AG  
Zürich, Switzerland  
Tel: +41 (0)43 344 42 10  
[info@asalis.ch](mailto:info@asalis.ch)

All rights to this document are reserved to Lane Clark & Peacock LLP ("LCP"). This document may be reproduced in whole or in part, provided prominent acknowledgement of the source is given. LCP is part of the Alexander Forbes Group, a leading independent provider of financial and risk services. Lane Clark & Peacock LLP is a limited liability partnership registered in England and Wales with registered number OC301436. LCP is a registered trademark in the UK (Regd. TM No 2315442) and in the EU (Regd. TM No 002935583). All partners are members of Lane Clark & Peacock LLP. A list of members' names is available for inspection at 30 Old Burlington Street W1S 3NN, the firm's principal place of business and registered office. The firm is regulated by the Institute and Faculty of Actuaries in respect of a range of investment business activities. The firm is not authorised under the Financial Services and Markets Act 2000 but we are able in certain circumstances to offer a limited range of investment services to clients because we are members (as defined under the Act) of the Institute and Faculty of Actuaries, a Designated Professional Body. We can provide these investment services if they are an incidental part of the professional services we have been engaged to provide.

© Lane Clark & Peacock LLP. \*No regulated business is carried out from this location.