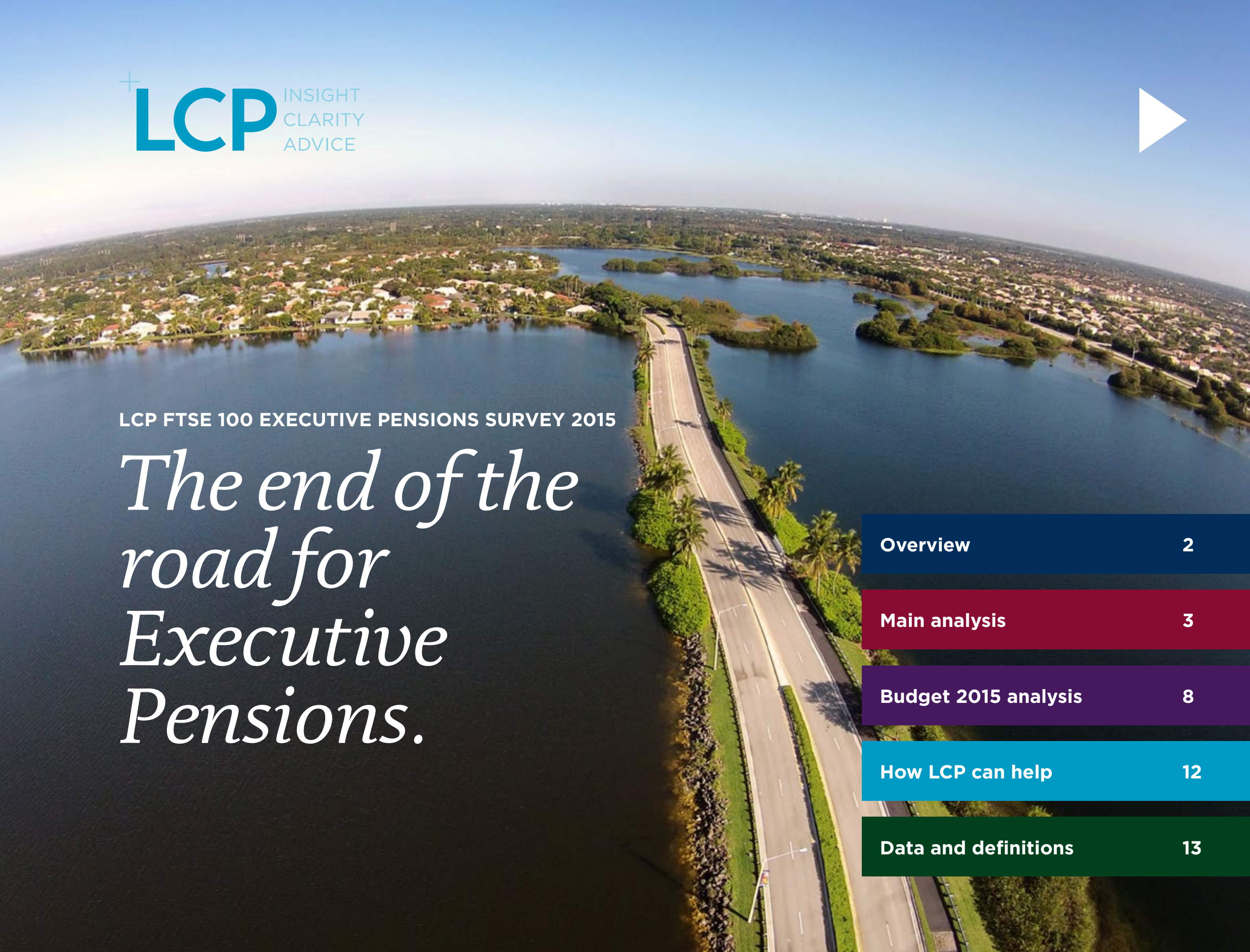


LCP INSIGHT CLARITY ADVICE

LCP FTSE 100 EXECUTIVE PENSIONS SURVEY 2015

The end of the road for Executive Pensions.

OVERVIEW

Mark Jackson
Partner
LCP

Our survey alternates between FTSE 100 and FTSE 250 companies and this year our attention is on executives in the FTSE 100.

30%
The benchmark for cash in lieu of pension.

£6bn
Annual savings to public finances due to reductions in annual and lifetime allowances[1]

Welcome to our annual survey of executive pension provision. This year's report follows the Chancellor's Summer 2015 Budget that announced yet more significant change for pensions.

In response to progressive reductions in the annual and lifetime allowances, our analysis confirms that companies continue their move toward flexible forms of pension compensation. Seven out of ten executives in our survey receive a flexible combination of defined contribution ("DC") and salary supplement ("cash"), or cash alone. Only one out of ten still earns a defined benefit ("DB") pension.

The Summer 2015 Budget confirmed a new tapered annual allowance with effect from April 2016. For the executives in our survey this means a reduction in the annual allowance to £10k and signals the end of the road as we know it for DB and DC executive pensions. As a consequence, we expect the move to cash will accelerate further over the next year. Thereafter, the whole pensions tax regime may be turned upside down, and we consider what the future holds in our report.

The impact of the Budget will be felt well beyond the executives studied in this report. Employers are facing the challenge of communicating the tapered annual allowance, and its many moving parts, to employees who have income of £110k or more - otherwise surprise tax charges will become common. To understand the impact see our case studies in Budget 2015 analysis.

We hope you enjoy the insight and analysis in this our 2015 survey.

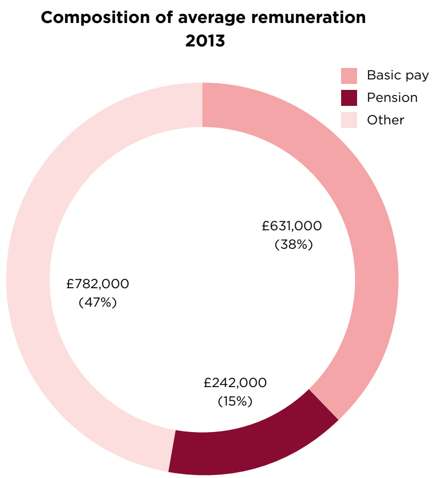
[1]Source: HM Treasury green paper "Strengthening the incentive to save: a consulation on pensions tax relief."

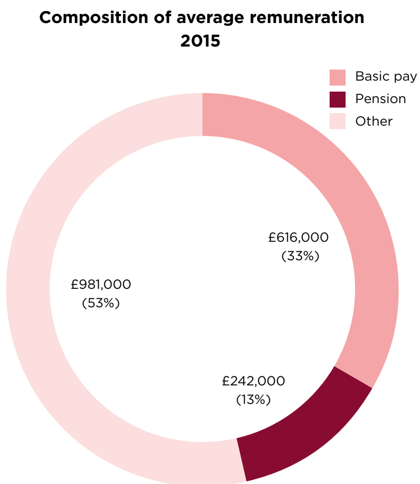
Main analysis

This section sets out our analysis of pension compensation provided to FTSE 100 executives - covering cost, type and comparison with previous years.

Pension compensation as a percentage of total remuneration

Pension benefits remain an important part of executive remuneration, with an average value of £242,000 in 2015. As a percentage of annual remuneration, pension has fallen from 15% in 2013 to 13% in 2015.

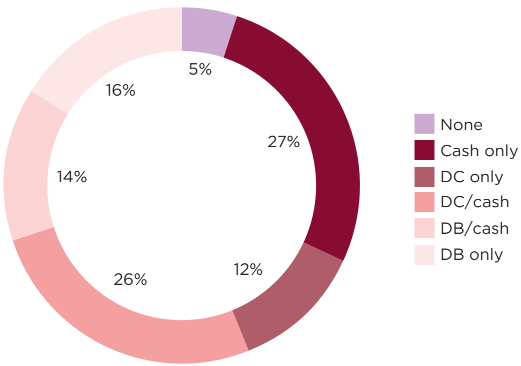




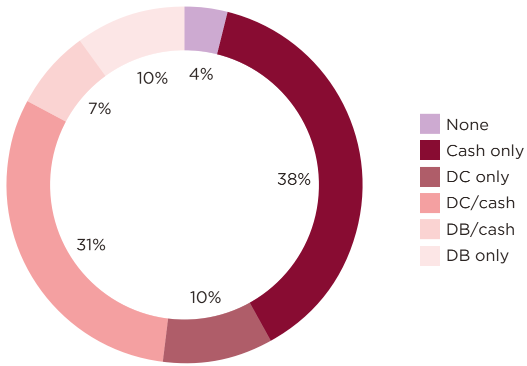
See the Data and Definitions section for further details on what's included above.

Pension types offered to a FTSE 100 executive

% of executives with each type of provision 2013



% of executives with each type of provision 2015

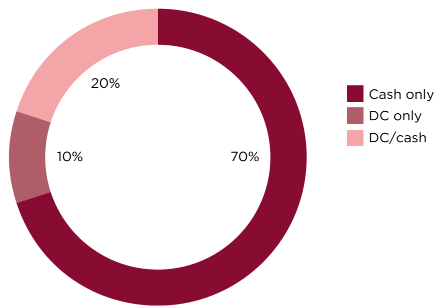


Salary supplement ("cash only") in lieu of any pension provision continues to grow and is now in place for 38% of executives (up from 27% in 2013).

Flexible pension compensation, giving executives the choice of tax efficient pension savings in a DC arrangement and/or cash ("DC/Cash"), has also grown; to 31% of executives (up from 26% in 2013).

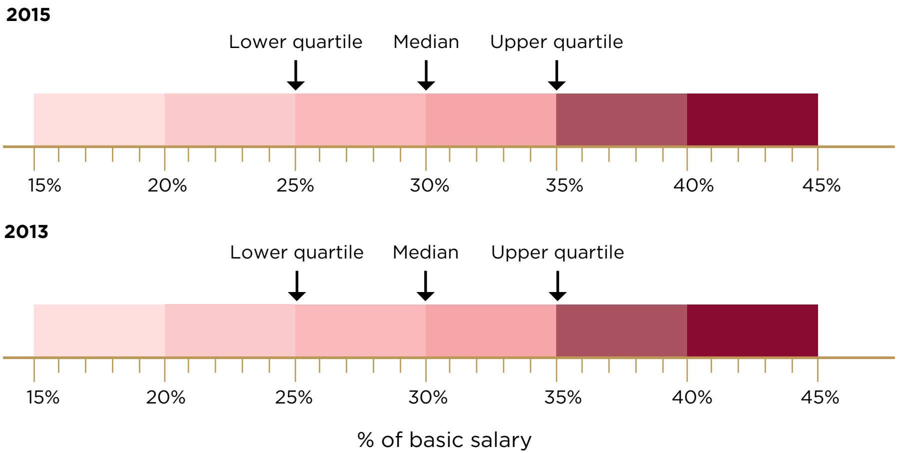
Taking these together, 7 out of 10 executives have the flexibility of cash in lieu of pension. This is supported by the fact that 70% of executives recruited during the year received a salary supplement as the only form of pension compensation.

% of executives with each type of pension provision
External appointments (in 2015)



Cash in lieu of pension

Below we set out the lower quartile, median and upper quartile to show the range of provision for the 38% of FTSE100 executives who received this benefit as their only form of pension provision.



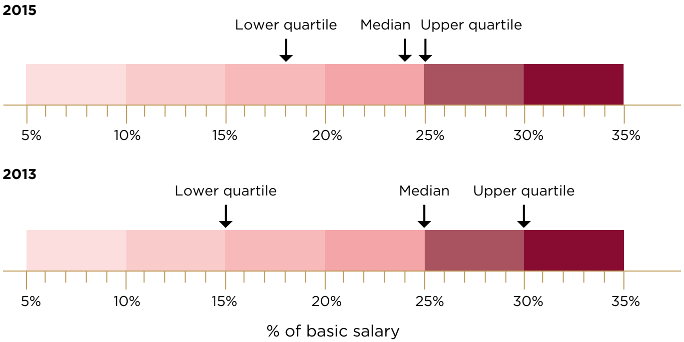
There has been no change in the cash benchmark in the past two years. We expect remuneration committees will continue to set compensation amounts at these levels in the near future.

Companies with cash in lieu of pension for all executives

- AstraZeneca
- Barclays
- Barratt Developments
- BG Group
- BT Group
- Compass Group
- G4S
- HSBC
- ITV
- Johnson Matthey
- Land Securities Group
- Marks & Spencer
- Meggitt
- Morrisons
- Old Mutual
- RBS
- Smith & Nephew
- Smiths Group
- Standard Life
- United Utilities
- Vodafone
- Weir Group

Defined Contribution and cash

The spread of compensation where executives receive a combination of DC and cash compensation has narrowed since 2013.

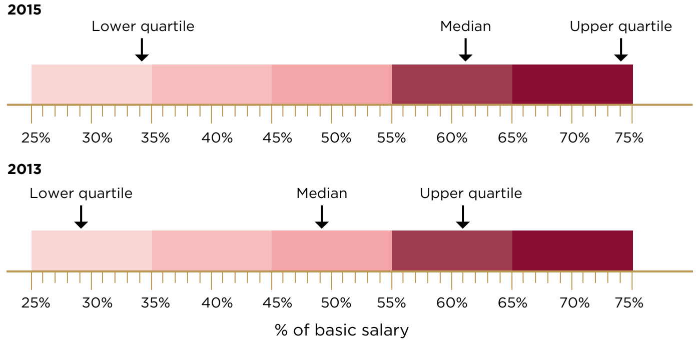


Companies that state the DC/cash split for all executives

ARM Holdings
Aviva
Dixons Carphone
IAG
Lloyds
Whitbread

Defined Benefit pensions

Few executives now earn a DB pension, but for those that do, the cost to the employer is still far higher than for any other type of pension benefit.



95% of UK-based executives earning DB pensions do so outside of the UK tax-registered regime, via Employer Financed Retirement Benefits Schemes ("EFRBS"). See page 9 for more on EFRBS.

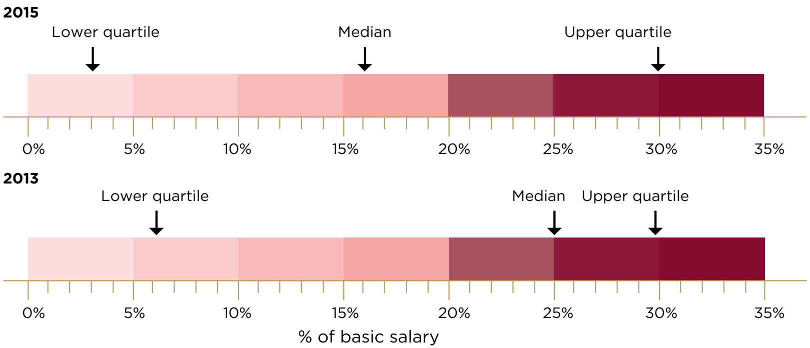
Companies with DB pensions for all executives

Associated British Foods
British American Tobacco
Diageo
SSE
Tesco

Main analysis

Defined Contribution only

Few executives received solely DC pension provision in 2015. Many of those that do are at companies that offer DC pensions to executives on exactly the same terms as other employees. For example, Admiral Group offer a contribution of 6% of pay (with an annual cap of £9,000 of contributions), while Hargreaves Lansdown and EasyJet offer a contribution of 4% and 7% respectively of basic pay to all eligible employees, including executives. The lower quartile and median are therefore much lower than for the more typical DC and cash group.



Companies with DC pensions for all executives:

Centrica
BHP Billiton
Fresnillo
Hikma Pharmaceuticals
SABMiller
Shire

No pension provision

Only 4% of executives received no explicit pension compensation.

Companies with no explicit pension compensation

Antofagasta
Randgold Resources
Sports Direct International

In the wake of Summer 2015 Budget this section looks at the impact for executive pensions

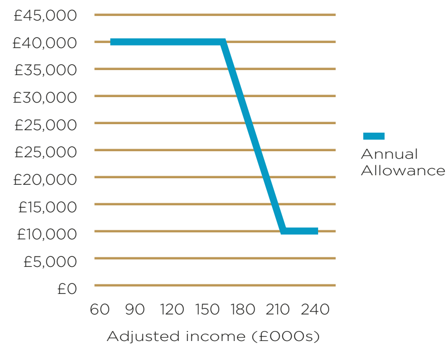
July 2015 Budget - The end of the road for executive pensions?

In his Summer Budget, the Chancellor confirmed that the lifetime allowance will reduce from £1.25m to £1m from April 2016. In addition, from April 2016 the annual allowance will reduce for those with "adjusted income" of £150k or more. "Adjusted income" is not just income used for income tax - it includes the value of pension contributions/accrual funded by the employer or individual into registered pension schemes. This includes salary sacrifice for DC schemes. Individuals could end up paying very high rates of tax if they and their employers do not start planning now.

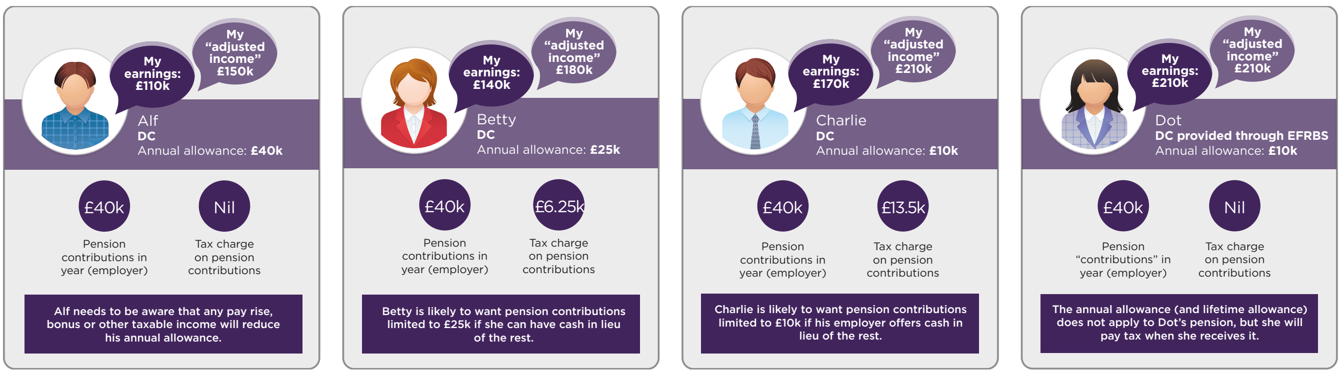
What does the tapered annual allowance look like?

These case studies look at the tax impact for individuals across DC and DB schemes who have "adjusted income" above £150k.

The higher your "adjusted income", the lower your annual allowance.

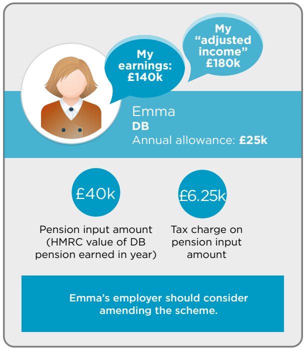


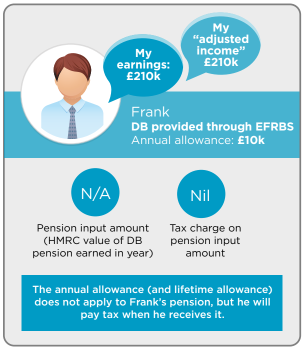
Defined Contribution Schemes



Click to view full infographic

Defined Benefit Schemes





Click to view full infographic

Unused tax relief from 3 previous years is ignored in these case studies. In all of the above, the pension drawn will be subject to tax.

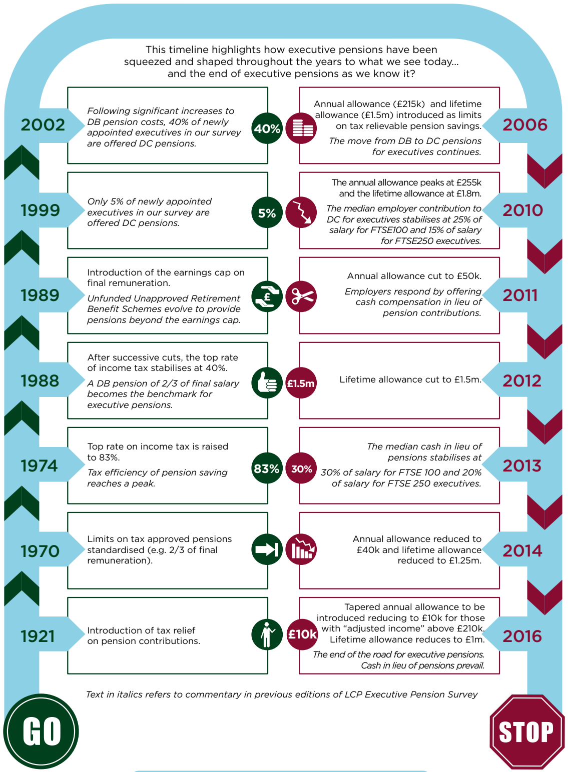
EFRBS – proceed with caution

An Employer Financed Retirement Benefit Scheme (EFRBS) is a pension scheme that is not tax-registered. If it is set up appropriately then benefits paid during retirement are subject to income tax but free of National Insurance. The annual allowance and lifetime allowance do not apply to EFRBS.

EFRBS are used by some of the companies in our survey to provide DC or DB to executives. As seen in our case studies, the tapered annual allowance will have an impact on employees well beyond the executives in our survey. Companies that currently use EFRBS may consider offering access to a wider group of employees, and companies that don't have EFRBS may look at introducing one.

EFRBS may prove to be a short term solution. Alongside the 2015 Budget the Government announced it "will consult on tackling the use of EFRBS to obtain tax advantage in relation to remuneration".

The Rise and Fall of Executive Pensions



Click to view full infographic

What will the future hold?

In response to progressive reductions in the annual and lifetime allowance, this report confirms that companies continue their move toward flexible forms of pension compensation, notably additional salary in lieu of pension. The summer Budget will accelerate this move. Indeed, in our opinion, it signals the end of the road for executive DB and DC pensions – see our infographic "The Rise and Fall of Executive Pensions.

Julian Lyons
Consultant
LCP

Our future surveys will be much simpler - nearly all executives at this level will have cash in lieu of pension.

A new tax regime?

A green paper *"Strengthening the incentive to save: a consultation on pensions tax relief"* was launched alongside the Summer 2015 Budget. The green paper considers a fundamental review of the taxation of pensions. Currently, the pension regime is known as EET: pension savings are exempt from tax; investment returns are exempt from tax; the pension ultimately paid is subject to tax.

The green paper considers a reversal of this regime – "TEE" – whereby pension savings are taxed; investment returns are exempt from tax; the pension ultimately paid is exempt from tax. This would bring the tax regime for pensions in line with that for individual savings accounts (ISAs). The green paper recognises that some form of additional incentive is needed if, unlike ISAs, pension savers are unable to access their savings until age 55 or later.

For executive pensions, as we've seen in this report, the current system is actually more like "TET" because a £10k annual allowance offers very little tax relief as pensions savings. A "TEE" system could represent an improvement.

£50bn

The cost to the Treasury of tax relief in 2013/14[1]

[1]Source: HM Treasury green paper "Strengthening the incentive to save: a consulation on pensions tax relief." Includes relief on income tax and National Insurance

How LCP can help

Action required

Employers need to identify the scope of employees affected by the tapered annual allowance and review current pension policy to ensure that this valuable benefit is delivered efficiently. A big challenge for employers will be warning employees of potential tax charges on their annual pension savings.

LCP can help companies and their executives:

- Review pension compensation to ensure it is in line with market practice and delivered in a practical and tax-efficient way;
- Communicate changes and explain the changing tax regime to employees;
- Provide seminars and one to one meetings; and
- Provide online tax calculators to assist employees.

Alasdair Mayes
Partner
LCP

Employers will need to find a way to communicate many moving parts in a streamlined way, otherwise surprise tax charges will be incurred unnecessarily.

Data and Definitions

- Our analysis covers the FTSE 100 constituents as at 30 April 2015.
- We have analysed published accounts with accounting years ending during 2014.
- Pension values (including for DB pensions) have been taken from each company's single figure for remuneration disclosures.
- We have considered executive directors in office at the end of each company's accounting year.
- An executive is a member of the board of directors who is also a full-time employee of the company.

Total number of executive directors in survey: 284

In order to allow comparison between all FTSE 100 executive directors the following adjustments were made to published audited information:

- Basic salary and cash allowance have been converted to full year equivalents for executives who were appointed partway through the accounting year.
- Currency conversions to sterling have been undertaken at the exchange rate stated in the accounts or, where this information is not available, at the prevailing mid-market rate at the accounting year end.
- "Other" includes items such as performance-related bonus, taxable benefits and non-cash emoluments received during the year. It does not include the value of any vesting long-term incentive awards.

Pension types offered to a FTSE 100 executive

In broad order of increasing corporate risk, the types of provision are:

- no pension compensation;
- an explicit cash allowance in lieu of pension;
- a mixture of cash and contributions to a defined contribution (DC) arrangement;
- contributions to a DC arrangement;
- a mixture of defined benefit (DB) pension and cash allowance; and
- DB pensions.

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