Editorial: Pensions into perspective

If you are reading this, you are probably a pensions professional and, like me, have probably spent most of your adult life working in pensions. Indeed, pensions have been an important element of most employees' working life and an even more important part of their post-retirement life even since the 1834 Superannuation Act brought occupational pension schemes, as we know them today, into being in the UK. But are they really as important to employees as we like to think? Is it time to start thinking about pensions in a different way?

Thinking about pensions in the context of the total remuneration package, for example, would perhaps give us a more realistic perspective. Rather than looking at pay and benefits in the traditional, and somewhat piecemeal way, the total remuneration approach addresses the total investment made around employees. It can include short- and long-term incentives, vacations, car schemes, ill-health and medical benefits, pensions, life and accidental death cover, as well as basic pay.

Towers Perrin has undertaken a number of client projects throughout Europe, designed to benchmark given positions against those in peer companies. Sample results, illustrating the financial weight of individual remuneration elements expressed as a percentage of total remuneration, are shown in Table 1.

Clearly, these will vary significantly by industry, as well as by profile of the individual positions. However, as you can see, the results clearly indicate that pensions rarely account for more than

10 per cent of total remuneration. This begs the question: 'Why do we place so much emphasis on pensions?'

Part of the answer, of course, stems from the fact that pensions have been institutionalised, not only by governments as part of their social security programmes, but also by employers as part of their employment package. And another part of the answer stems from the fact that funded pension plans account for vast amounts of money. Indeed, in some cases, these funds can be greater than the value of the sponsoring company. However, the fact that pensions have become an accepted part of the remuneration landscape does not necessarily mean that they are either a valued or a valuable part of an employee's package. Indeed, Towers Perrin research¹ seems to indicate the opposite. In spite of all the time, effort and money that employers spend on providing and communicating retirement benefits, the following prevails:

- only 54 per cent of employees understand what their financial needs in retirement will be
- only 42 per cent are confident that they will have enough income in retirement to meet their needs
- only 29 per cent would be willing to accept lower pay increases to get more retirement benefits
- only 46 per cent of managers and 38 per cent of employees take the view that benefit programmes influence why people join a company and then stay with it. Indeed, only half of employees underestimate the value of their benefits.

Table 1: Financial weight of individual remuneration elements (expressed as % of total remuneration)

	UK %	the Netherlands %	France %
Basic salary	63	56	52
Short-term incentive	7	8	11
Long-term incentive	3	7	22
Stock purchase plan	1	1	1
Retirement plan	6	3	2
Vacation	6	7	5
Car policy	12	16	6
Other (medical, life etc)	2	2	1

Moreover, there are a number of economic, cultural and demographic changes around the world which pose significant challenges to the traditional approach of pensions as an isolated benefit in an employee's package. These are:

- governments around the globe are modifying their traditional social security programmes. Some have moved away from defined benefit-style arrangements and adopted defined contribution instead. Others have maintained and modified their defined benefit systems, either by reducing the social security benefit levels and/or delaying the age at which workers can receive benefits. The end result of such changes is, of course, a movement towards greater reliance on private employer-sponsored retirement plans and individual savings.
- the ratio of retirees to the overall population continues to escalate in most of the industrialised nations and many developing countries. This puts pressure on state retirement benefit systems, as well as on the arrangements of individual employers.
- a worldwide shortage of executive talent, skilled managers and technology-based professionals is motivating companies to be ever more creative when building reward

packages to attract and retain these highly sought-after individuals.

- increasing diversity in the workforce, in terms of both lifestyle and aspirations, is encouraging employers to offer more flexibility and self-selection options in their remuneration packages. There is a growing realisation that one size does not fit all.
- multinational companies in Europe must address the effect of a common currency on their pay programmes and human resource management strategies.
- severe economic and currency crises in Asia are forcing companies to reassess their approach to remuneration.
- the gradual relaxing of restrictive local laws and customs in Latin America is allowing employers to improve their pay and other reward programmes.

It seems there has never been a better time for both national and multinational companies to adopt a more holistic approach to pay and benefits or total remuneration.

Like many other things, total remuneration started in the USA. It is now prevalent there, and is becoming increasingly so in the UK. However, the concept is still relatively new in Europe. One of the reasons for this may be that employers feel restricted

by a perceived lack of flexibility. Total remuneration aims to appeal to different employee needs, thereby maximising the perceived value, and the return on the employer's investment in the employee. However, this requires a flexible approach to the design and management of reward components. In Europe, there is often more flexibility than companies think. Indeed, we have found that in most European countries, companies can have and have implemented a fairly extensive flexible benefits programme.

Although I would urge all employers to look at their pension plans in the context of total remuneration, I believe that this applies especially to European employers. Indeed, there are factors that apply specifically to this geographic group; factors that will influence their human resource (HR) strategies going forward. These are in particular:

- the looming of a common European currency
- the movement of the European Commission (however slowly) towards the harmonisation of supplementary pension provision
- the free movement of workers.

These are all compelling arguments in

favour of employers adopting one European HR strategy, rather than a string of country-specific ones. Indeed, with increased mobility of employees across borders, strategy and design need to focus on 'not acting as a barrier' to mobility. Administration, operation and communication therefore become key issues. Moreover, a common strategy can only be achieved by means of transparency and consistency — two qualities that can only be facilitated by total remuneration.

Pensions are important for all sorts of reasons: historical, financial and security. They are also clearly a 'needed to play' element of the total remuneration package. My contention is not that they are not important; simply, that as pensions professionals, we should stand back and view them from a broader perspective: that of total remuneration.

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Reference

- 1 Towers Perrin's Benefit Effectiveness Index polled random samples of managers and employees in large organisations across seven countries: Brazil, Canada, France, Germany, the Netherlands, the UK and the USA. The research was conducted in 1997 and 1998.