

Using best estimate life expectancies: why it matters for employers

At a glance

The latest industry life expectancy model (CMI 2024) has recently been released. Employers usually update their pensions liability figures used for accounting purposes for the latest model each year.

Within CMI 2024, the impact of the COVID-19 pandemic has now been fully integrated into future life expectancy projections. Despite this, CMI 2024 shows an increase in life expectancies for the average scheme, with older members expected to live longer than previously expected.

Adopting this model without tailoring the inputs may add unnecessary prudence to a scheme's liabilities, as life expectancies across the membership will vary depending on a variety of factors, such as household income and age.

Modern analyses allow easier assessment of best estimate life expectancy for schemes, helping to mitigate risks of overfunding, gain a better understanding of the cost of insurance and better hedge scheme cashflows.

Benefits of using best estimate life expectancy

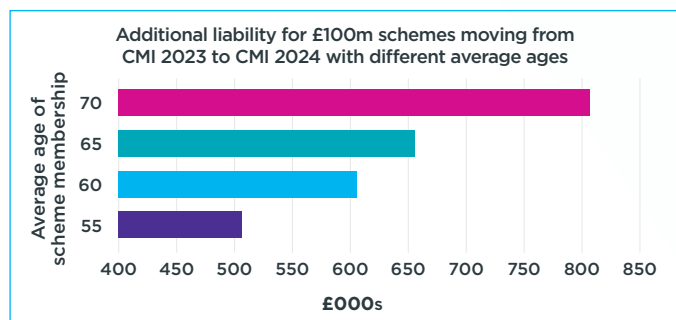
By understanding the best estimate life expectancy of your scheme's membership, employers can apply this insight across a number of areas.

Use	Benefit
Accounting	More accurate reporting of pension costs and provides justification of assumptions for auditors
Cash funding	Improved ability to assess cash contributions needed and reduce the risk of overfunding
Insurance transaction	Greater understanding of cost of securing member benefits and timeframe to securing a transaction
Run-on	Greater understanding of future cashflows to help plan for run-on
Asset hedging	Help tailor cashflow models to more accurately remove interest and inflation risk



Impact of CMI 2024

Overall, life expectancies have increased between the CMI 2023 and 2024 models.



Adopting CMI 2024 increases liabilities, especially for schemes with an older membership. This emphasises the importance of reviewing your scheme's membership to ensure the model is adopted with the appropriate inputs.



Actions employers should take

1. Assess the impact of adopting the CMI 2024 model on your scheme.
2. Obtain an up-to-date best estimate of your members' future life expectancies.
3. Use a best estimate of your scheme membership's life expectancy to review your liabilities on both an accounting and funding basis, and check if it has been incorporated into the investment hedging strategy.
4. Assess the impact of updating your scheme's best estimate life expectancy on your long-term strategy, whether this is through securing benefits with an insurer or running on for surplus.

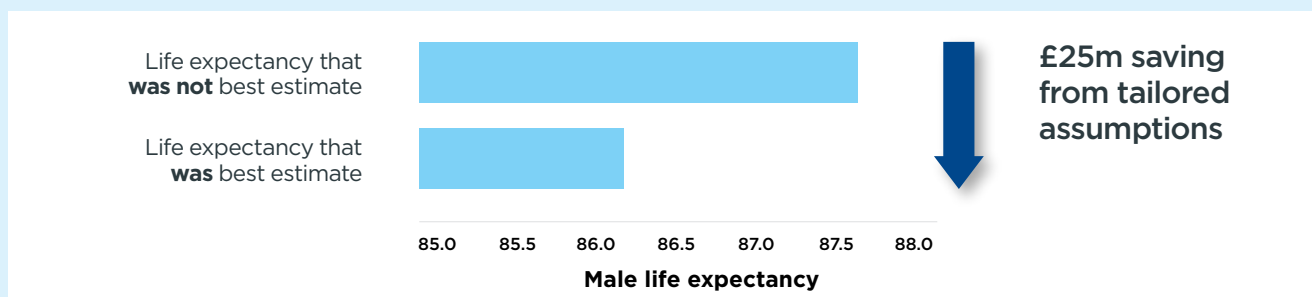
Factors that affect best estimate life expectancy

The CMI model estimates life expectancy for an average scheme if the inputs are not tailored. To determine the best estimate life expectancy for your specific scheme using the model, a number of characteristics of your scheme's membership will need to be considered.

Factor	Impact on life expectancy	Impact on liabilities
 Pension amount	Higher pension income implies higher life expectancy	Higher life expectancy will increase pension liability
 Socioeconomic profile	More affluent individuals (usually identified via postcode analysis) will have a higher life expectancy	Higher life expectancy will increase pension liability
 Health profile	Healthier individuals (identified via postcode analysis) will have a higher life expectancy	Higher life expectancy will increase pension liability
 Level of deprivation	More deprived individuals will have a lower life expectancy	Lower life expectancy will decrease pension liability

Case study: What difference can best estimate assumptions make?

XPS recently supported an employer with a £600m scheme facing a £125m shortfall on a solvency basis. The employer was keen to secure benefits with an insurer but believed this was unaffordable in the short term.



A detailed analysis to find out the scheme's best estimate life expectancy revealed that the shortfall was £25m lower than initially expected. With this improved insight, the employer was able to commit cash contributions to cover the lower deficit, enabling an insurance transaction to proceed.

Find out more

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