



Dubai International
Financial Centre

DIFC employers' meeting: Proposals for reforming the minimum end of service gratuity

25 April 2019





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Today's speakers



Jacques Visser – Chief Legal Officer

- Jacques is the head of the Legal Affairs division of the DIFC Authority.
- In addition, he holds the position of Secretary to the DIFC Higher Board and the Boards of the DIFC Authority and DIFC Investments LLC.
- Mr. Visser also currently serves as DIFC's Security Registrar and Commissioner of Data Protection.
- Jacques has overseen the DIFC's review of its end of service gratuity system since the outset.



Christopher Payne – DIFC Group Strategy

- Christopher Payne currently works in Group Strategy at Dubai International Financial Centre.
- He holds a Ph.D from the London School of Economics, a Bachelors degree from Cambridge University, England and has published books and new articles on economics.
- He acted as main DIFC liaison with the working group and the latest reform phase of the end of service gratuity system.



Philip Wheeler – Ernst & Young Pensions Advisory

- Philip is a Senior Manager & qualified pensions actuary working in Ernst & Young's (EY) Pensions Advisory practice.
- He has over 25 years of pensions industry experience.
- Philip has been a member of the DIFC's working group since September 2016, advising the DIFC on the options for reforming the existing end of service gratuity system.



DIFC's Objectives

The DIFC is constantly assessing how best to achieve its vision of becoming a global financial hub, aligning to its overall mission approach and through the application of its core values.

	DIFC approach	Key questions
1 Vision	To drive the future of finance	How does the existing gratuity system compare to other global financial hubs?
2 Mission	To develop the world’s most advanced financial centre	Is the existing gratuity system fit for purpose?
3 Values	<div>1. Integrity. 2. Transparency. 3. Efficiency.</div>	Does the existing gratuity system promote DIFC core values?

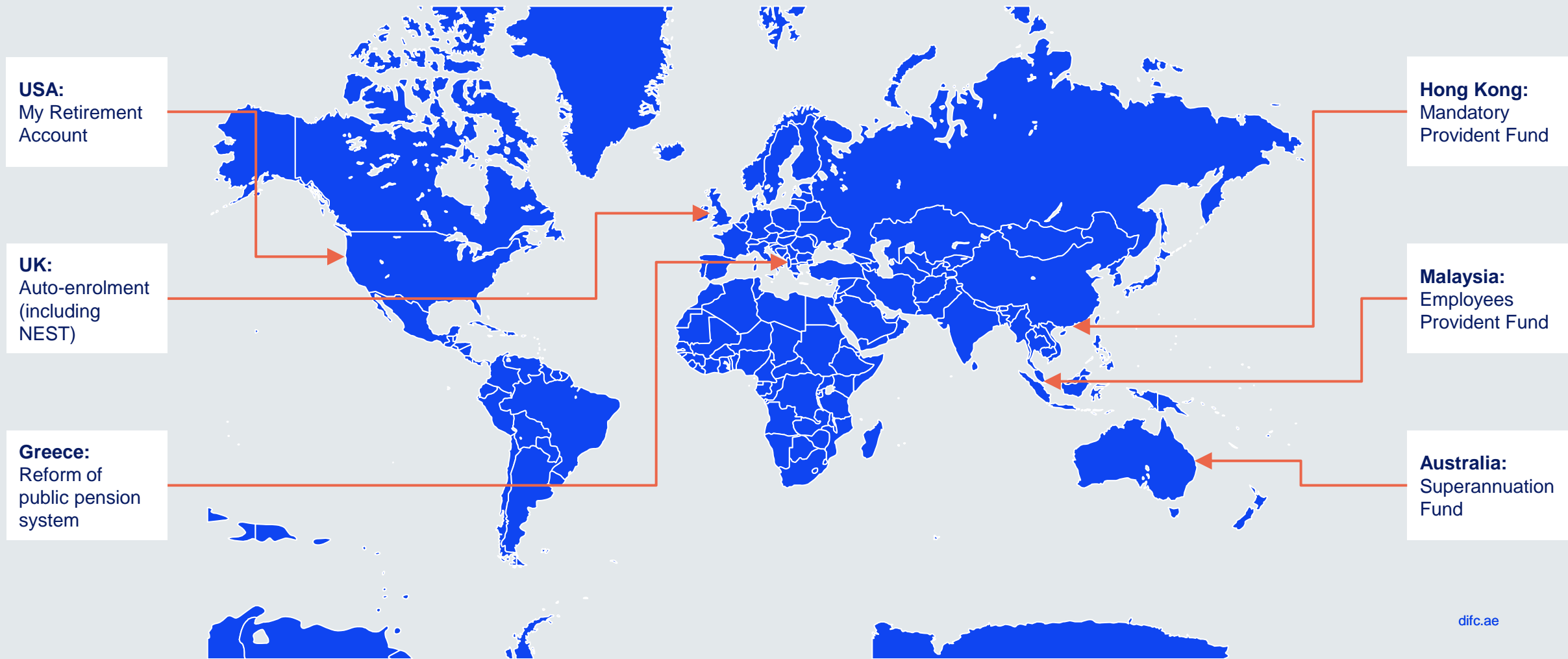


Global trends & best practice – An EY view

The existing end of service gratuity system has been reassessed by considering changing demographics and global trends.



Notable government retirement savings plans that have been established as or are being reformed as a defined contribution basis.





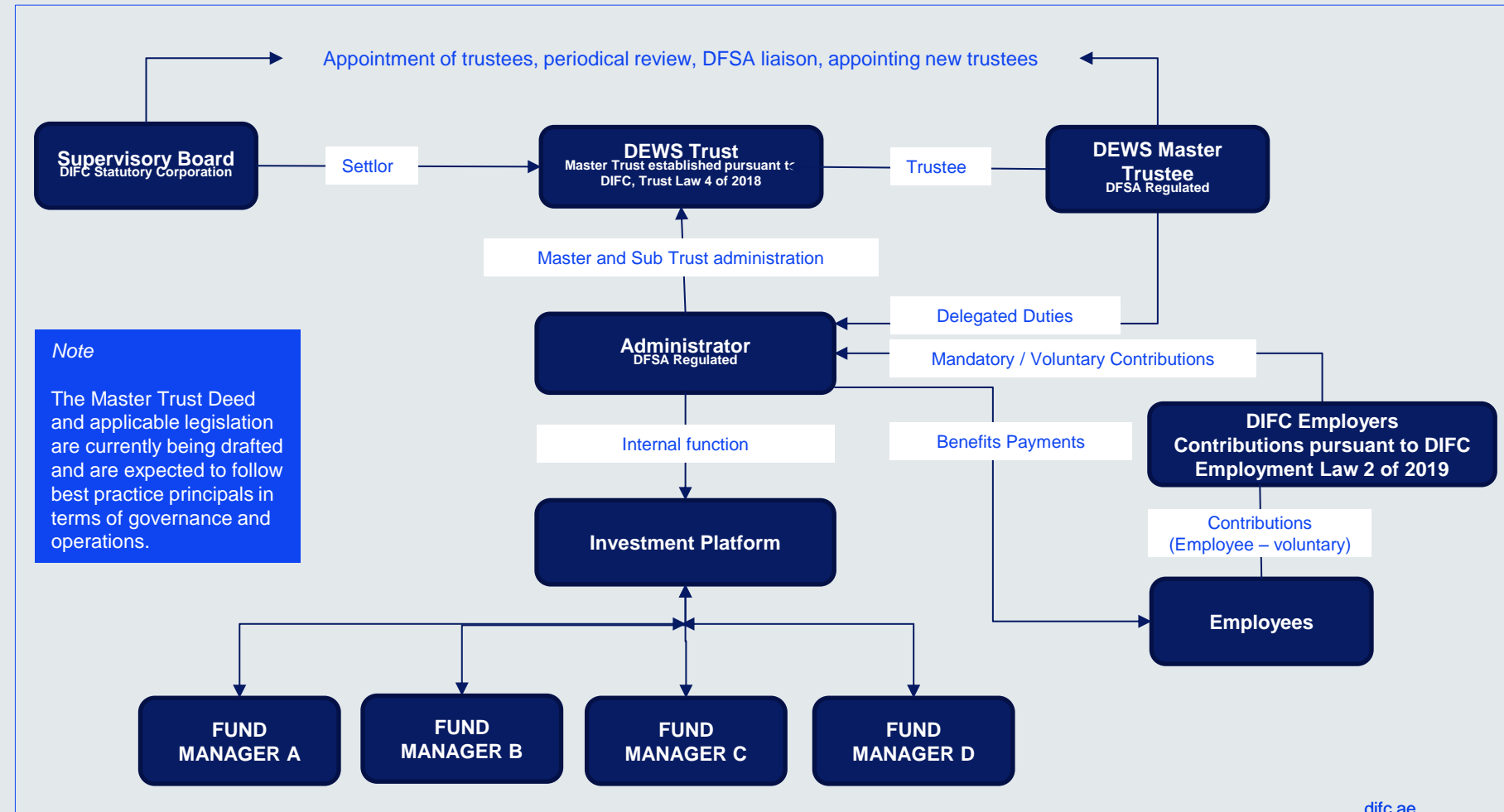
DIFC's conclusions from the working group phase

High level recommendations	Defined contribution design	Centralised administration	Mandatory contributions
Feature	Detailed recommendations		
Legal structure	<ul style="list-style-type: none"> Global best practice for preserving benefit security means the DIFC Employees Workplace Savings (DEWS) should be established using a master trust structure, governed by an independent trustee, domiciled in the DIFC and regulated by the DFSA. 		
Benefits & contributions	<ul style="list-style-type: none"> For simplicity, the existing end of service gratuity structure for eligibility, Basic Wage definition, and timing of payments should be retained under the DEWS. For cost neutrality and simplicity purposes, minimum employer contribution rates under DEWS should broadly match minimum accrual rates under the existing end of service gratuity system. 		
Transition	<ul style="list-style-type: none"> There should be no change to benefits accrued under the existing end of service gratuity structure such that they remain linked to Basic Wage at eventual termination date. All DIFC-based companies and employees should be subject to the changeover from the existing regime to the DEWS. Employers that have an end of service arrangement that provides benefits no less than DEWS and that is funded via a third party fiduciary should be exempt from joining DEWS. 		
Administration	<ul style="list-style-type: none"> There is a range of third party service providers who would be able to administer the DEWS for all DIFC-based companies and their employees. These would be solicited by RFP to select a suitable service provider. They would be able to provide the range of services that employees, employers and the DIFC could reasonably expect. 		
Investment	<ul style="list-style-type: none"> To minimise plan charges, contributions should be invested (where reasonably possible) in passive, index-tracking funds. Employees should be able to select from a range of pre-selected managed funds, based on the employee's risk appetite. A default investment option should apply where employees do not make a selection. Consultation may be required to gain views on the acceptability for a proportion of contributions to be invested in UAE-based assets. 		
Charges	<ul style="list-style-type: none"> The operating costs of the DEWS should be recovered, where possible, through an annual management charge (AMC) that would apply to employees' investment accounts. Subject to economies of scale and market rates, it is expected the AMC for the DEWS would not be dissimilar to charges applied to best practice occupational savings regimes around the world. 		

The DEWS trust document is expected to follow international best practice within the DIFC legislative framework.

Key points to note

1. A DIFC Supervisory Board will oversee the establishment of the DEWS Master Trust, and the appointment of its trustee and operational service provider.
2. The DFSA will regulate the trustee and administrator.
3. The trustee will oversee the governance of the trust. The administrator will perform the operations of the trust.
4. A new system of regulation and compliance will facilitate the set up and running of the DEWS Trust.
5. Employer contributions will be mandatory, employees can contribute if they wish.
6. The DEWS Trust will operate on a funded, defined contribution basis, investing contributions on behalf of employees and paying benefits on leaving service or later, if requested.





Proposed next steps

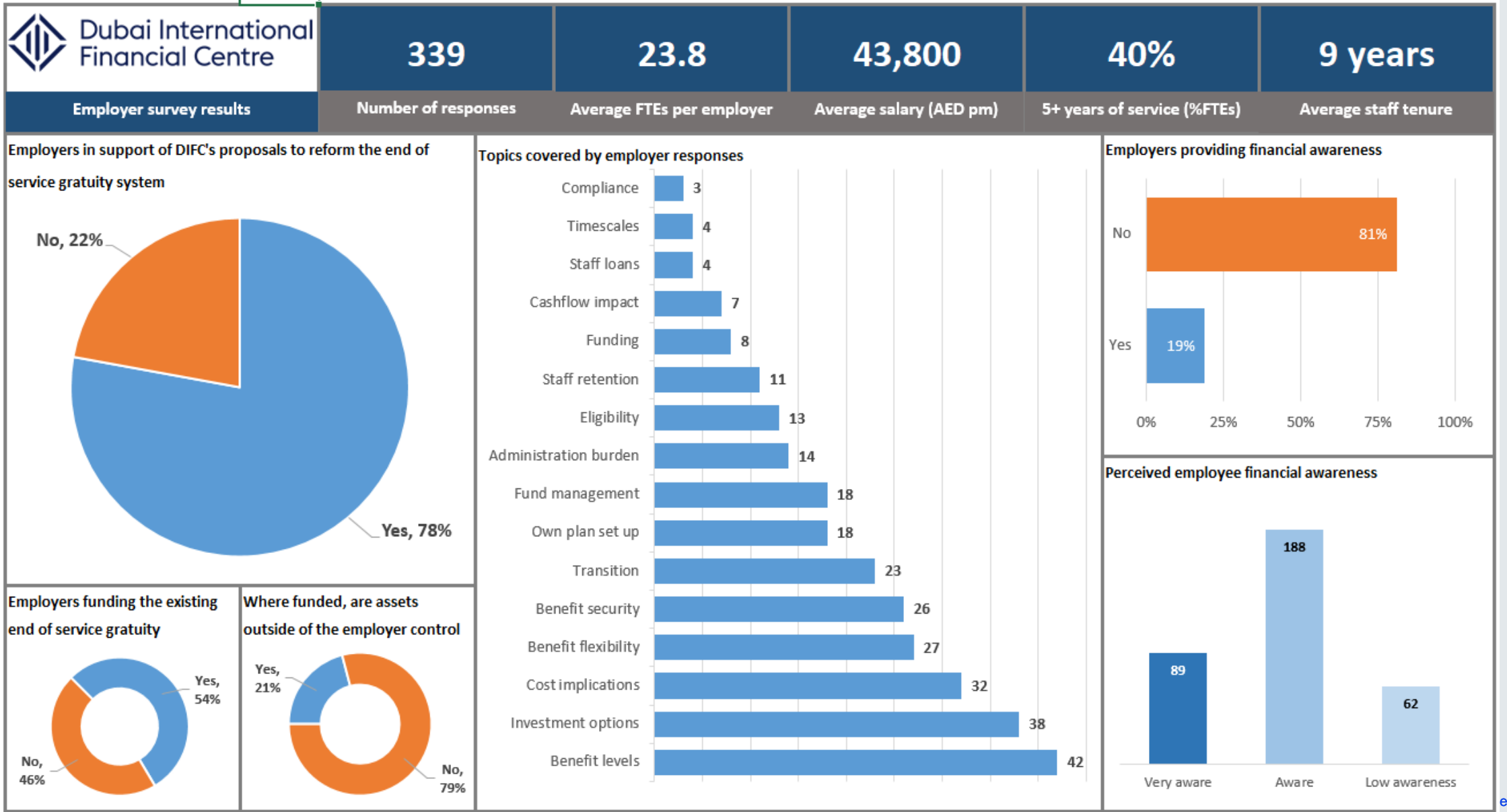
DIFC anticipates the next high level steps to be as follows.

Item	Details	Expected timescale
Review employer survey feedback	DIFC to issue a summary of survey responses and employer feedback.	May 2019
DEWS legislation	DIFC to finalise the legal framework for establishing DEWS and the trust documentation.	June 2019
Appointments	DIFC to appoint the DEWS trustee and administrator following an RFP process.	July 2019
DEWS engage with employers	The trustee and administrator contact employers around the process to transition to DEWS.	August 2019
DEWS go live date	DEWS goes live on 1 January 2020 with contributions commencing to the trust, and service stopping for the existing defined benefit arrangement.	January 2020



Results from the employer survey

Results from the employer survey





Common queries raised by employers

Common queries raised by employers

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#	Query	DIFC observation
1	Why change the existing system?	The existing system suffers from several key problems: (1) benefit payments are not secure (2) employers are exposed to open-ended liabilities (3) globally, the developed world is moving towards funded DC benefits.
2	Why use a master trust?	Globally, best practice is to use a trust arrangement as this provides benefit security and a robust governance and operational framework.
3	Is the scheme voluntary?	All DIFC employers and employees will be required to participate in DEWS unless an employer operates a qualifying system of their own.
4	Can employers use their own system?	Employers can use their own end of service system as long as its contributions / benefits exceed DEWS and it is fully funded via a third party fiduciary arrangement.
5	Who will pay for the cost of the new system?	DEWS' costs will be met using an annual management charge levelled on invested assets, in line with global best practice.
6	Can employers still provide a defined-benefit gratuity on leaving service?	DEWS sets out the minimum benefit basis. Similar to the existing system, employers can choose to top up DEWS benefits to equal a defined benefit amount.
7	What are the investment options?	Employees will be given the option to set a high level asset allocation or use the trustee's default investment option (set according to the employee's risk appetite). A Shari'ah investment option will also be available. A proportion of assets may also be invested in local investment markets.
8	What happens to existing benefits?	At the changeover date, benefits earned under the existing formula would stop earning new service, but would continue to be linked to future increases in Basic Salary. DIFC labour law requires that basic salary can be no less than 50% of regular earnings.
9	How and when will benefits be paid under the new system?	Similar to the existing system, benefits will be paid when an employee leaves service. Under the new system, benefits will be paid directly to the employee in order to preserve benefit security.
10	Can employees contribute to DEWS?	Employee will be able to make voluntary contributions to DEWS. Employer contributions will be mandatory.
11	What will be the employer contributions to DEWS?	Contributions are expected to be cost neutral compared to the existing gratuity system. These have yet to be finalized but are expected to be around 5.83% of basic salary for where service is below 5 years and around 8.33 above 5 years of service.
12	What happens when an employee leaves service?	For benefits earned under the existing end of service arrangement, the employer will continue to pay this part of the overall benefit. The employee can choose either to take their DEWS benefit at leaving service or defer divesting until a later date.
13	When will DEWS be implemented?	DIFC intends for DEWS to commence from 1 January 2020.



Q&A



Q&A

Gratuity Investment Governance DC Attraction Platform
Trustee Retention Contributions Costs Trust Cashflow Awareness
Demographics Expectations Funded
Benefits DB Security Trends Administration
Allocations Charges Global



Appendix

Minimum benefits emerging from DEWS might be higher or lower than the minimum provided under the existing end of service gratuity regime.

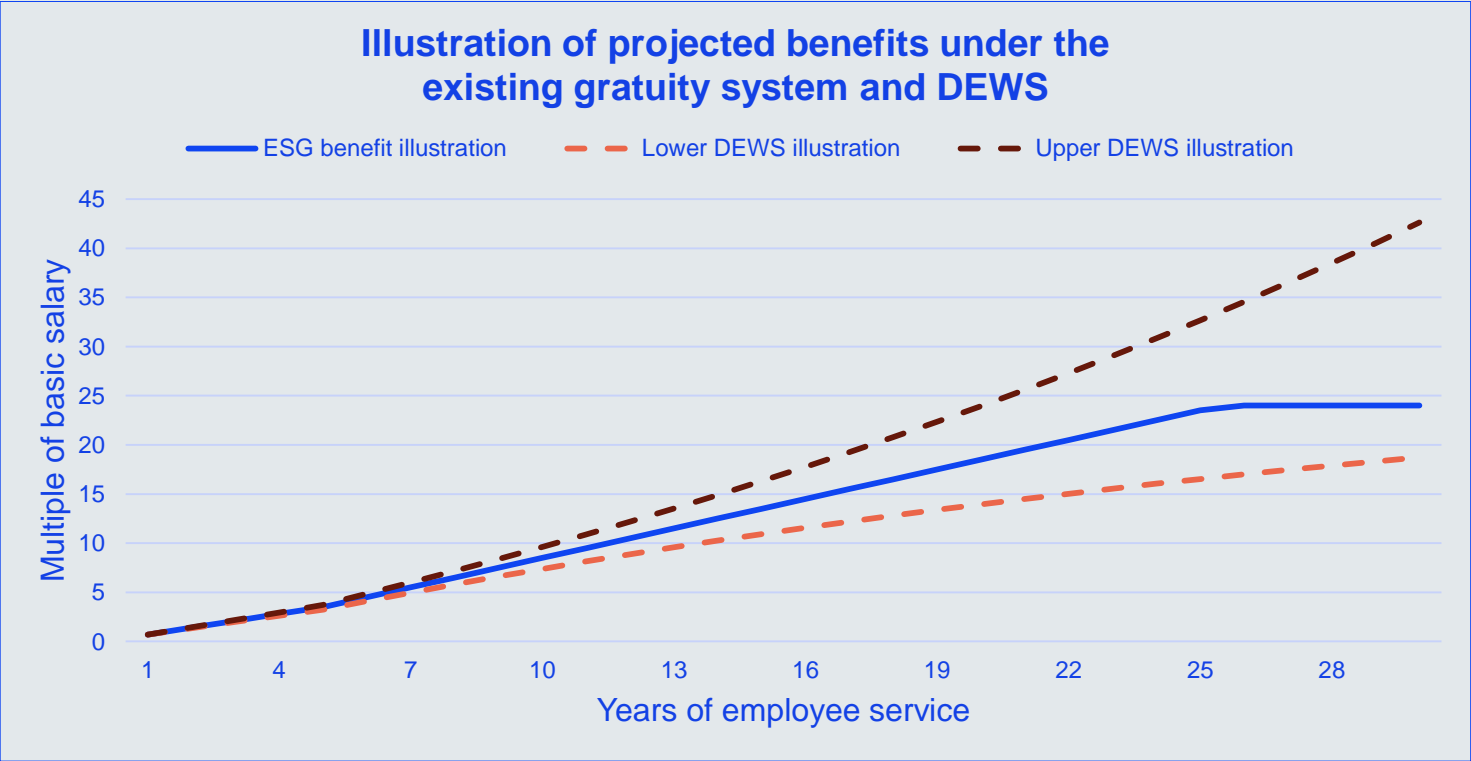
Projected benefit comparison

Benefits under DEWS would depend on future increases in basic salary and on investment returns achieved on contributions paid into DEWS on behalf of the employees

The benefit projections below illustrate the potential level of benefits that could emerge under DEWS under two different sets of assumptions. These are compared to the level of benefits that would emerge under the existing end of service gratuity (ESG) arrangement.

The table values show multiples of Basic Wage at termination date under the ESG and DEWS for different periods of service.

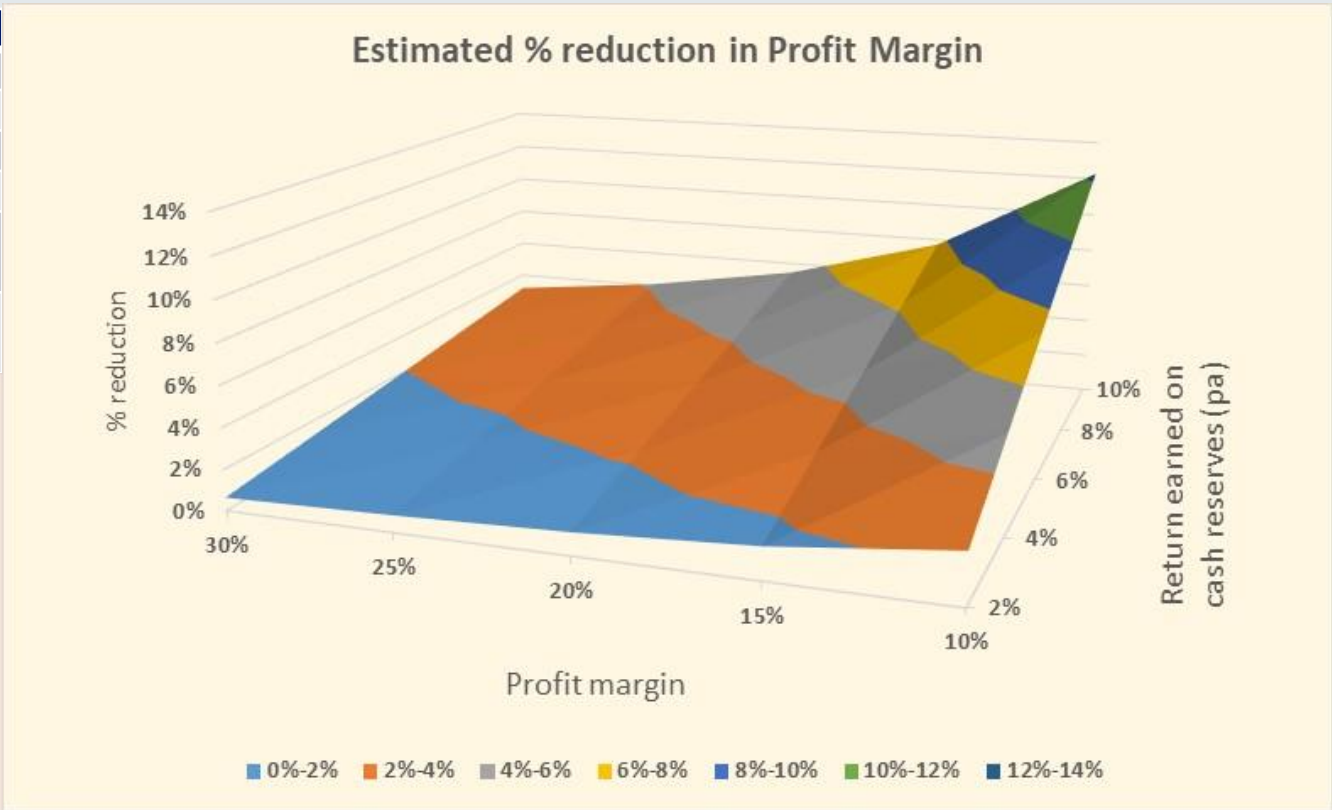
The primary assumptions underpinning the benefit projections are listed below.



DEWS assumptions	Salary increases (pa)	Investment returns (pa)	Annual management charge (pa)
Lower	5.0%	3.0%	1.25%
Upper	3.0%	7.0%	1.25%

Moving to a regularly funded savings plan from an unfunded arrangement could impact corporate profitability. The size of any potential impact depends on a range of factors. The graphs below illustrate a range of potential impacts.

Factor	Best case	Base case	Worst case
Average service (years)	6	8	10
Return on cash reserves	5%	10%	15%
Profit margin	25%	25%	25%
Average ESG accrual rate	7.1%	7.1%	7.1%
Gross salary roll (% total costs)	50%	50%	50%
Basic Wage roll (% gross salaries)	50%	50%	50%



The example below illustrates benefits being earned under the existing and new systems before and after the introduction of DEWS.

Year	Basic salary (AED pm)	Employee service at end of year	Existing end of service gratuity		DEWS system		
			Service to count	Accrued benefit (AED)	Contribution rate	Employer contribution (AED)	Accrued fund (AED)
2016	10,000	1	0.7	7,000	N/A	N/A	N/A
2017	10,400	2	1.4	14,560	N/A	N/A	N/A
2018	10,800	3	2.1	22,680	N/A	N/A	N/A
2019	11,200	4	2.8	31,360	N/A	N/A	N/A
2020	11,700	5	2.8	32,760	5.83%	8,185	8,336
2021	12,200	6	2.8	34,160	8.33%	12,195	21,063
2022	12,700	7	2.8	35,560	8.33%	12,695	34,771
2023	13,200	8	2.8	36,960	8.33%	13,195	49,496
2024	13,700	9	2.8	38,360	8.33%	13,695	65,275
2025	14,200	10	2.8	39,760	8.33%	14,194	82,147
Benefit on leaving service after 10 years			Paid by employer:	39,760		Paid by DEWS:	82,147
Total benefit payable to employee							121,907

The above illustrations rely on the following key assumptions: (1) basic salary growth of 4%pa, (2) gross investment returns of 5%pa, (3) annual management charge of 1.25%pa (4) DEWS contribution rates of 5.83% for employee service under 5 years and 8.33% for service above 5 years (not yet confirmed).



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Thank You
