
RESPONSE TO HIGH LOW CONSULTATION

Draft regulations to allow the Pension Protection Fund to take account of bridging pensions: response to the public consultation on behalf of the Trustee of the British Steel Pension Scheme

I am writing on behalf of the Trustee of the British Steel Pension Scheme (the "Scheme") in response to the public consultation referred to above.

Background

By operation of a regulated apportionment arrangement the Scheme was separated from Tata Steel UK Limited ("TSUK") on 11 September 2017.

In accordance with the terms of an agreement between TSUK and the Trustee, members of the Scheme are to be given the option of transferring to the New British Steel Pension Scheme (the "New Scheme") if certain qualifying conditions are met.

Those members electing to transfer to the New Scheme would transfer to it on or before 28 March 2018 (the "Transfer"). The Scheme will enter a PPF assessment period on 29 March 2018 (the "Assessment Date") at which point any members remaining in the Scheme will, in effect, become entitled to PPF compensation.

One of the qualifying conditions for the Transfer to the New Scheme is that an initial funding test is satisfied (the "Funding Test"). The purpose of this test is to ensure that if the New Scheme goes ahead it will have an appropriate level of funding.

Under the rules of the Scheme, members retiring from active status were able to choose to receive a bridging pension. This was commonly referred to as the 'high/low' pension option. A member selecting the option would receive the 'high' pension until a specified step-down date (usually state pension age), followed by the 'low' pension from the step-down date.

The amounts of the high and low pensions were calculated by the Scheme actuary so as to be actuarially equivalent to the standard pension, with the difference between the high and low pensions being broadly equivalent to the basic state pension.

In order to choose the high/low option a member had to sign and return a form that clearly explained the effect of choosing the high/low option and made it very clear that if the option was selected the amount of pension paid to the member from the Scheme would reduce at the step-down date.

The Scheme ceased to have active members on 31 March 2017 at which point the high/low population became closed, with the number of members receiving the high pension decreasing over time as they reach their step-down dates. As at the date of this letter around 4,600 pensioner members will be in receipt of the high pension at the Assessment Date ("High Pensioners").

Any High Pensioner who transfers to the New Scheme will continue to receive the high pension until the step-down date followed by the low pension in exactly the same way as would have happened in the Scheme (but with different annual increases before and after the step-down date).

Significance of the anomaly for the Scheme and its members

The bridging pension anomaly is of particular significance to the Trustee and members of the Scheme because the method that will be used to share the Scheme's assets between the Scheme (effectively the PPF) and the New Scheme when the Transfer is made takes account of the cost of providing PPF compensation for members.

If PPF compensation continues to include the bridging pension anomaly, the Trustee would expect almost all High Pensioners to choose to remain in the Scheme. Around £600m of additional assets would then need to be left in the Scheme to meet the cost of this anomaly. Put another way, the Scheme would be meeting the cost of providing a windfall benefit worth, on average, £100,000 for each High Pensioner.

If this £600m must be included in the assets retained by the Scheme, this would make it much less likely that the New Scheme will meet the Funding Test. As explained above, if the Funding Test is not met, the Transfer will not go ahead and all of the members who have chosen to transfer to the New Scheme would end up with lower benefits in the PPF instead. Even if the Funding Test is met, the security of the transferring members' benefits in the New Scheme would be lower because the Scheme had to meet the cost of providing a windfall to High Pensioners in the PPF.

The circumstances of the Scheme are, of course, different from those of many other schemes that might enter the PPF in the future, because all members and assets of those schemes will go into the PPF. In those cases, the cost of providing any windfall benefit pensioners receiving bridging pensions would be underwritten by PPF levy payers.

Trustee support for the proposal to address the bridging pension anomaly

Without the changes to regulations proposed in the consultation, the anomaly could operate to the detriment of the majority of Scheme members for the reasons I have explained above. The Trustee therefore believes that the Government's proposal to address the anomaly is fair and reasonable.

Option 1 or 2

So far as possible the Trustee wants High Pensioners to receive a pension which as closely as possible replicates the pension to which they were entitled and were expecting to receive under the Scheme.

Because option 2 in the consultation paper (mirror existing scheme rules) means that any High Pensioner who chooses to remain in the Scheme would receive PPF compensation that more closely replicates his or her Scheme benefit entitlement than the smoothed benefit that would be provided under option 1, the Trustee considers that option 2 would on the face of it be the better way of addressing the bridging pension anomaly.

However, if the anomaly is addressed, the Trustee would expect the vast majority of High Pensioners to choose to transfer to the New Scheme, whether option 1 is adopted or option 2. In the New Scheme, they would not be affected by the 10% reduction to their pension that would be applied in the PPF or by the PPF compensation cap, and they would also benefit from the higher annual increases provided by the New Scheme. Upon the death of a High Pensioner, his or her spouse would also receive a higher spouse's pension in the New Scheme than in the PPF.

Given the very low numbers of High Pensioners that are likely to decide to remain in the Scheme and then enter the PPF, the Trustee considers that it would be reasonable for the Government to give preference to option 1, if the Government and the PPF think that this option would be more capable of being accurately administered in practice having regard to the PPF's existing administrative capabilities.



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