

Work and Pensions Committee

Oral evidence: Defined benefit pension schemes, HC 144

Wednesday 8 November 2023

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Members present: Sir Stephen Timms (Chair); Shaun Bailey; Siobhan Baillie; David Linden; Nigel Mills; Selaine Saxby; Sir Desmond Swayne.

Questions 153-213

Witnesses

I: Terry Monk, Member, Executive Committee, Pensions Action Group, Richard Nicholl, Member, Executive Committee, Pensions Action Group, Roger Sainsbury, Founding Member, Deprived Pensioners' Association and Neil Walsh, Pensions Policy Officer, Prospect.

II: Barry Kenneth, Chief Investment Officer, Pension Protection Fund, Oliver Morley, Chief Executive, Pension Protection Fund, and Sara Protheroe, Chief Customer Officer, Pension Protection Fund.

Written evidence from witnesses:

DBP0015 [Terry Monk](#)

DBP0031 [Terry Monk](#)

DBP0087 [Richard Nicholl](#)

DBP0016 [Pension Action Group](#)

DBP0036 [Prospect](#)

DBP0053 [Deprived Pensioners' Association](#)

DBP0088 [Deprived Pensioners Association](#)

DBP0050 [Pension Protection Fund](#)

Examination of witnesses

Witnesses: Terry Monk, Richard Nicholl, Roger Sainsbury and Neil Walsh.

Q153 **Chair:** Welcome, everybody, to this meeting of the Work and Pensions Committee for our inquiry on defined benefit pensions. A warm welcome to our first panel of witnesses this morning. May I begin by making a declaration that I was the Minister for Pensions when the Pension Protection Fund and the financial assistance scheme were being set up? I think that gives me a declarable interest in the topic we are talking about. The other point I should make is that the last time Mr Sainsbury and I were sitting across a table from each other was when we were negotiating the planning conditions for London City airport, which was 37 years ago, so it is very nice to see you here again this morning. Can I ask each of you to tell us who you are?

Richard Nicholl: I am Richard Nicholl. I am from just south of Stoke—between Stoke and Shrewsbury—and I was a member of the Frederick H. Burgess pension scheme.

Terry Monk: I am Terry Monk. I have spent most of my working life in financial services, including as a member of the Bradstock scheme, which was the first compromise prior to the FAS and the PPF. Like you, Sir Stephen, I have been involved in this for 20 years, from the formation of FAS and the campaigning for FAS with Baroness Altmann right through to where we are today, so thank you for your support and your interest.

Roger Sainsbury: I am a founding member of the Deprived Pensioners Association, which originated from some former colleagues at my own company. We wanted to try to do something for our former staff, and I have ended up with something much bigger.

Neil Walsh: I am Neil Walsh. I am the pensions officer for the trade union Prospect.

Chair: Welcome to all of you. The first question is from Sir Desmond Swayne.

Q154 **Sir Desmond Swayne:** With respect to PPF and FAS, should indexation be available only to those members who were entitled to it under the original scheme rules?

Terry Monk: Yes. My overriding statement is that people should get what they paid for—end of story. If people paid for it, they should get it. If they did not pay for it, there is a strong argument as to why our money, if it can help us, should be used elsewhere when they were not paying for it.

Roger Sainsbury: I agree with that entirely, and so does the DPA. We have never been looking for general handouts; we have only been looking for fairness and the meeting of commitments made. I would consider it quite wrong if payments were started to be made to people whose original firm scheme did not have indexation in it.

Richard Nicholl: I support those comments. People paid extra, effectively, for full indexation and some schemes paid less because they were not paying for it. It is only fair that it goes to those who have paid for it and it should go to those who have paid for it.

Neil Walsh: Prospect does not have a position on that in particular, but I would just note that everybody in the PPF and the FAS is suffering greatly at this time of cost of living pressures. Whether their original rules provided for some minimal indexation or not, they are still suffering and I think there is a strong case to be made for doing something for them. A lot of people who were in schemes that have now fallen into the FAS or the PPF were contracted out and are only getting the basic state pension, and they are suffering from that as well. We do not have a position, but I would not say it is clear cut that there is no case at all not to give indexation to members of schemes where it was not provided for pre-1997, in the small minority of cases where that was the situation.

Q155 **Sir Desmond Swayne:** Do we know how many members of either FAS or PPF are without indexation?

Neil Walsh: I believe at the time the Bill was originally discussed—I remember some statistics from the *Hansard* of the debate in the Grand Committee of the House of Lords—the Minister at the time was quoted as saying that perhaps 90% of schemes provided indexation pre-1997 and therefore maybe 10% did not. By number of members, I imagine that fewer still did not have indexation because the ones that did not provide that were smaller. The PPF may have better numbers in the next session, but I cannot imagine that it would be a huge extra burden to provide that protection to everybody in the PPF and FAS.

Roger Sainsbury: I was advised by the PPF that among the firms that had come into them, it was something like two thirds that had indexation and about one third that did not.

Q156 **Sir Desmond Swayne:** What changes would any of you make to indexation and how would that affect pre and post 1997?

Terry Monk: That is a massive subject. What time does the House sit until?

One thing I would like to add to the comments about the paid-for pre-1997 indexation is that in PPF I think, and I know in FAS, with the guaranteed minimum pension, the word is misleading. When they contracted out and had the so-called guaranteed minimum pension, that as a benefit—that is, with inflation protection for the period 1988 to 1997—does not get the increases that they would have had for that period of time. The Minister wrote to me and told me that they followed the legislation but that the legislation for that aspect does not apply to FAS. So they lost both ways: they lost what they paid, for and if they were contracted out they are not getting those increases either.

Both Richard and I are very much driven by not only our own situations but a lot of the FAS membership. In the very early days, Sir Stephen,

when you were involved in putting it together, you will remember the campaigns under John Benson, Phil Jones and the steelworkers. They have fought hard and are still fighting to get what they say—what John will say—is what we paid for.

Richard Nicholl: To answer your question, I would go with the original scheme rules. Most schemes would have an annual indexation of between 3% and 5% per annum. Some of them, like our scheme, were 3% per annum irrespective of the inflation rate and others would vary with the inflation rate with 3% as a maximum. They vary and some schemes would be 5%.

Roger Sainsbury: Our scheme at Mowlem had a 5% cap, but our campaign at DPA is focused almost entirely on this pre-1997 clause in the schedule. We think it is that clause that is causing all the trouble, and it should be extinguished.

Neil Walsh: I agree with that. In a world where choices have to be made, we would like all the promises to be honoured. If we have to start somewhere and target something, the lack of indexation in relation to compensation for benefits accrued before 1997 has to be the priority. There are about 80,000 PPF members—I don't have the figures for FAS—who have no compensation increases at all. At a time of a cost of living crisis, to have such a large element of their income frozen is terrible for them.

At the time that it was introduced, I don't think it was recognised how discriminatory that would turn out to be. We have information from a freedom of information request to the PPF that shows that the people affected by this are disproportionately older—which might be a bit obvious because, by definition, their service goes back longer—but also disproportionately female. There is a pensions gender gap, and this exacerbates it, so there is a really strong case and a fairness argument.

If you were in a scheme that did not make any distinction between pre and post 1997, you probably view the impact of that date as being fairly arbitrary. It has some meaning in statute, but there may not be any meaning to the rules of the scheme that you were in, and you might be wondering why it applies to you. When it was brought in, I think it was because of "hard choices"—that is exactly what the Minister said. There were trade-offs between increasing the levy, more taxpayer support and reducing the impact on members, but at that time, the Government was also talking about reducing future inflation protection and reducing the maximum inflation protection from inflation capped at 5% to inflation capped at 2.5%. Whether it was hubris or just a belief and overconfidence in the Bank of England, at the time they were quoting, when they were bringing in that measure, inflation capped at 5% was effectively full inflation protection.

Roger Sainsbury: It is just a thoroughly bad clause, in my view. It is definitely age discriminatory, and it is very damaging to members of the

Pension Protection Fund. I have yet to hear anybody tell me of one single merit that this clause delivers.

Neil Walsh: It is more damaging than Parliament considered when it brought it in. At the time, we were told that inflation was solved, that the great moderation was here and that we were never going to have periods of inflation spiking at 10%, 11% or 12% again, but we are having them, and some members are bearing a disproportionate burden. They are bearing a disproportionate cost when it comes to the three-way taxpayer/levy payer/members. They are bearing more of the cost than Parliament expected. Now that there is, perhaps, better performance from the PPF than we could have hoped for and the possibility of rectifying something, very first on the list of what we might consider doing is removing the arbitrary distinction, unfairness and discrimination that Roger talked about and giving some protection to pre-1997 accruals.

Richard Nicholl: We should remember that people in FAS are disproportionately affected, because FAS came in in 2004 but most schemes closed around 2000, so people would have very minimal post-1997 pensionable service which attracts a minimum amount of indexation, whereas, with PPF, somebody going in today, for instance, will have a much higher number of post-1997 pensionable years, so they have more indexation than the people in FAS. If anything does happen, we have seen before that FAS seems to be treated differently from the PPF—for “funding reasons”, in their words—so we are feeling a bit like the poor relation in terms of any uplifts that have happened.

Q157 **Selaine Saxby:** Good morning. I am starting to look into the grounds for increasing compensation, so my questions are coming to Neil and Roger, but I will then hand back to Sir Stephen and the gentleman at the other end.

The 2022 departmental review said that the DWP and the PPF should “work together to understand the implications of the PPF’s funding position...and plan well ahead...to address what happens to any funding which is surplus to requirements.” What do you think should happen, and when?

Neil Walsh: I hope that that review happens as soon as possible. I said in the previous answer that we believe members are bearing a disproportionate burden and that they are bearing more of the costs of providing the PPF structure than was originally anticipated. Not to put too fine a point on it, if we wait too long before we do something about that, many members will have died and will not have benefited at all from any further measures that we make to address their compensation.

By default, improvements in the funding position are just going to result in a lower levy. The levy has obviously been reduced significantly over time, and it is proposed that it will be halved again next year. There is just no mechanism by which further improvements in the funding position or even the existing improvements that we have already seen can be shared with members.

Selaine Saxby: Is there anything you would like to add, Roger?

Roger Sainsbury: I think that, as soon as possible, the clause should be deleted, or the effect of the clause should be deleted, depending how you do the drafting. Then, of course, there will be the question as to whether the indexation is going to be paid only in the future or whether the losses that people have suffered from this in the past—right through from 2005—are going to be properly recognised. Those losses are just as real as any; they are really real. The losses in the future have yet to come, but the PPF will clearly have to make a decision as to whether they are really, fully recognising the damage that has been done by the clause or are only partially doing so.

Q158 **Selaine Saxby:** Has either the DWP or PPF started to engage with you on what the priorities should be?

Neil Walsh: I don't think the PPF can, because they are simply bound by what is in the legislation and can only apply that. We have been in correspondence, from time to time, with various Pensions Ministers, and there doesn't seem to be any impetus from Government to bring forward any changes to legislation that would address any of the issues that Roger or I have identified.

Roger Sainsbury: And it does not matter how many people have written how many letters to different MPs, Government Departments or whatever: all we have ever had is the same reply, simply telling us, "That's the way it is, because that's the way it is in this clause". That is all we have ever had. We know that, and we want the clause eliminated. We haven't had any meaningful dialogue about it at all, to be quite honest.

Neil Walsh: At the time those clauses were written and Parliament scrutinised the original legislation, I don't think it was obvious that the outcome would turn out to be gender discriminatory. I think that is new information—I certainly read all the *Hansard* reports, and that never came up—and I think it is an opportunity for Parliament to say, "Well, we shouldn't have gender discrimination in the rules of such an important scheme. Let's address that."

It might have been a bit more obvious that there would be age discrimination, but, of course, that was brought in before age discrimination was outlawed. Other aspects of the statutory framework have been found wanting in terms of age discrimination and the level of benefits. They have been addressed and have improved the cap for the best earners.

I think it's time to address the gender discrimination and age discrimination affecting the people who have got the least, because their compensation has been frozen and they may have lost over 50% of their original benefit at this point, in real terms.

Terry Monk: Can I chip in with something there, which I think is an important point to make? Having been through the birth of FAS—in fact, before the birth of FAS—and all the way through it, we have always

developed and worked very well with the Pension Protection Fund—the financial assistance scheme, as they were formerly called—and we have no complaints whatsoever. They do a very, very good job. I am not saying that because they are sat behind us; I really do appreciate what they have done. They have always been prepared to listen and to take time. For six years, with Sir Stephen's help, we have tried to get in front of one of the Pensions Ministers and, for six years, we have been batted away. We have never had the opportunity that you are giving us today to express our thoughts and views on the members. For giving us this opportunity, I thank you very much.

It should be recognised that, if PPF were given a bit more flexibility—I will try not to be too long on this. Several years ago, there was an issue where mistakes were being made in how benefits were calculated—that was never the members' fault, but often by the trustees or the administrator—and there came a point where FAS, as they were then, were writing to members and asking them to repay quite substantial sums of money. PPF—or FAS—did not have the discretion to deal with that unless it was below a minimum figure of £2,500. It was discussed with the people in Croydon when Steve Webb was the Pensions Minister, and the discretion and powers given to the PPF were increased to enable it to deal with some of the day-to-day things. I would like to see that degree of extra flexibility. I would like the Minister, whoever it might be this year, next year and the year after, to understand a bit about what has been going on. Richard and I have been doing this for 20 years, and we keep thinking we are getting near the end. Hopefully, this is the beginning of the end.

Q159 Selaine Saxby: How do you think the interests of PPF members and levy payers should be balanced?

Roger Sainsbury: Can I just come back on that last point? For a long time, I thought the PPF had been doing their job absolutely right. More recently, I have taken a more nuanced view of it. I now think that, through that period of time, the PPF should themselves have recognised the serious faults and very bad effects of this pre-1997 clause. Obviously, so long as the clause is in existence, which I hope will not be for very much longer, they have to abide by it. I think what they should have been doing is, at the same time, lobbying Government and pointing out that it is a thoroughly bad and damaging clause, and that it needs to be got rid of. They had a duty of care to the members to try to do something for them, even in the face of what the legislation says. They should have joined us and lobbied the Government to get rid of this rule.

Neil Walsh: Prospect sponsors three defined benefit pension schemes and pays the PPF levy in respect of them. We have tens of thousands of members of pension schemes that are subject to the PPF levy and feel the consequences of how high that is. I absolutely recognise that the needs of levy payers and members of the PPF have to be balanced, but we think the balance has just gone too far against the members. They are taking a greater hit on their benefits because of the impact of inflation being higher than expected. They are suffering greatly because of that.

The funding position has led to the levy being improved. Clearly, the PPF would like to make adjustments to the statutory framework for the levy. We support those, but we think the balance has gone a bit too far. The members are bearing a disproportionate share of the cost, and it would be appropriate for the levy to reflect that benefits should be improved and that indexation needs to be given in respect of pre-'97 accruals.

Q160 **Selaine Saxby:** My final question is to you, Neil. In your evidence, you raised concerns that the judgments of the European Court of Justice that had improved PPF compensation might be revoked. Is that still a concern?

Neil Walsh: It was at the time. At that stage, in the most recent debate, amendments had been tabled by the Opposition and rejected by the Government, so it appeared that, as part of the revocation Bill, the Government were going to remove the effect of the Hampshire judgment and, for example, the requirement for the PPF to provide at least 50% of the accrued benefits. They have since U-turned on that, and that is very welcome. It is unfortunate that the outstanding impact of the Bauer judgment—the requirement that the compensation is not any lower than is needed to keep somebody above the poverty level—is lost under the revocation Bill, but it is unclear whether that will have much impact in practice. Those concerns are certainly not as great as they were at the time that the evidence was drafted.

Q161 **Chair:** As you have indicated, if indexation were to be introduced, it could either be from now on or it could be retrospective. What are your views about that choice if it came to that point?

Roger Sainsbury: If it is going to be a true change of position and a recognition that the indexation should have been there from the start, the proper legal outcome should be that you pay the past as well as the future. But that is about all I could say.

Terry Monk: If it didn't do the past, the oldest people, who have suffered the longest, would lose even more.

Neil Walsh: I am sure our members of the PPF feel exactly the same way. We have members who previously had a public service pension with full indexation, backed by the Government, when they worked for the UK Atomic Energy Authority. They were privatised and paid for higher indexation, but when the scheme was transferred to the PPF, they lost all that. Because they transferred into the PPF in 2012, their benefits are now nearly 40% lower than they were then. I am sure that they would absolutely love the indexation to be restored retrospectively as well—we fully support that; it is right and what they paid for, because they paid extra for it—but, if this is about the art of the possible, anything would be better than where we are now. Clearly, prospectively is better than doing nothing, and retrospectively is better than doing prospectively. We argue that the best thing is to pay retrospectively as well, but we would welcome any improvement on the current situation.

Roger Sainsbury: It is not too serious for me, because we have only been in the PPF for about three years. Some people have been losing this money for 18 years. For them, it has been really serious, and they deserve to be recompensed.

Terry Monk: You should meet John Benson.

Q162 **Chair:** I have a question specifically for Richard and Terry about the financial assistance scheme. If there was to be an improvement in indexation, it would require taxpayer funding—I do not think any other source could be used. What would be the justification for additional taxpayer support?

Richard Nicholl: One thing to make clear is that, initially, the residual funds of our schemes that were absorbed by the Government were not ringfenced into FAS. FAS has ended up being administered by the PPF, and it has made very good investment returns.

First, that money was quite considerable—about £1.8 billion. Then, as for the taxpayer, let us not forget where we started: if the Governments of the day had implemented the of article 8 directive, we would not even be sitting here and there would be no need for taxpayer funding. If they had put the safety net in place, an equivalent of the PPF would have been in place before we had any of our problems.

My view is that, yes, there will be a need for some taxpayer funding, but the people involved did everything they had been expected to do to save for their retirement, and they deserve that. We see wastage in the DWP of over £8 billion a year in errors, so we feel there is money there that could be saved and used to help us in our position. We feel very strongly about that.

Terry Monk: The insolvency directive was in place long before FAS came into force. It was in place long before some of the companies started going bust in the late '90s and early 2000s, but the protection required by the European courts was not there. It eventually came following the Robins case, I think—from cases that went to the European courts to prove that the Government should sign up to the directive, which they did, but that was after FAS. In the meantime, our money had been absorbed and, as the previous Pensions Minister wrote to tell us, it was taxpayers' money—it was almost, "It's not your money." Sorry, but it was my contributions and Richard's contributions. It was our money that went into whatever the Government then decided to spend it on—mending potholes maybe; I don't know.

Chair: I think it is fair to make the point that the liabilities for FAS are a lot more than the £1.6 billion that went into it.

Roger Sainsbury: You might not think that I have anything to say on this, but I do. I think it depends on what sort of reputation the Government want to have. If it were to be decided that indexation would be given to the PPF members, but not to FAS, I could well understand that

as being legal, but I would have great difficulty in thinking it to be fair. I merely give you that thought.

- Q163 **Nigel Mills:** On a similar theme, the PPF only provides 90% of benefit to people who are below retirement age if their scheme ends up in the PPF. Is that still appropriate, given how much money the PPF now seems to have, or should we in effect be giving people everything they have lost, rather than just 90% of it?

Neil Walsh: There are certain areas where benefits are cut in order to meet the objectives of the PPF and to balance taxpayers, the levy payers and everything—choices have to be made. If we were looking at choosing which improvement we might make over the current situation, that 90% cut is one of the few things that survives a discriminatory challenge. If it was a choice between improving that 90% factor or providing some indexation for pre-1997 accruals, well, the lack of indexation for pre-1997 accruals discriminates against older people and women, and the 90% cut does not. If you could do both, that would be fantastic, but I don't think we are in that situation. If it is a choice about doing something, the case for addressing the lack of indexation for pre-1997 accruals is far stronger.

Terry Monk: I agree with that totally.

Roger Sainsbury: So do I. We should not forget that age discrimination is illegal, and it is only being allowed to carry on because it is sheltered by the wording in the clause. If we were still in the European Union, that would be fairly easily overridden. We have always been fighting against the age discrimination. The other aspects might be thought merely to be unfair or unfortunate, but this angle of it is basically just wrong.

Richard Nicholl: In terms of our stances, we think we should get what the scheme paid for—what we paid for that went into the scheme—so 100% would be ideal. I agree that if we were ever able to sit in front of the DWP, those are the type of things we would have to know the figures for. We have been trying to get figures out of the DWP for years, to understand how deep the problem is and what the cost to remedy it would be, but they have not given us any figures. They seem to pluck figures out of the air to scare everybody away.

It is the dialogue with the DWP that is missing, and also their communication, as was pointed out by the ombudsman in her report in 2006. The communication surrounding this has been very poor, even with trustees. I was a member-nominated trustee and went on a Government-sponsored training course as a new trustee, where the MFR was not explained in the true sense of what it was able to do or, more importantly, not to do.

Even now, anybody entering PPF is told, "You will get 90% of your pension." They do not mention—except in the very fine detail—the lack of pre-1997 indexation. Whatever happens, they need to learn lessons, as far as I am concerned, on communication.

Terry Monk: I think hardly anybody will actually be getting that headline 90%. Sir Stephen, you mentioned it in relation to some comments in the press about the company that went bust and protecting their pensions. People should have what they paid for protected, whether it is 100% or even 90%, but 90% and all the add-ons must surely be right. Anything less than that is not right. It would be interesting to know the statistics, but I doubt there are many people—in FAS, probably nobody—getting anywhere near 90%. The reality is that that so-called headline of 90% is getting close to 50% or 60%.

Richard Nicholl: You may have seen my deposition. I have been in FAS for only four years, and over those four years, inflation has been a total of between 18% and 19%. My increase from my FAS award, over the four years, is 0.67%. That is not 6.7%; it is 0.67%. That is because the majority of my pensionable service was pre-1997. That is seriously affecting people. Obviously those people who are older than me and have been in FAS for longer are really suffering now financially because of the high rates of inflation that we have had in the past couple of years.

Q164 **Nigel Mills:** Neil, we are about to see the PPF; do you have any other issues that are pressing for your members with PPF? I think there is a bit of a view that at some point we will need to proactively manage the long tail of schemes that are never going to be able get to buy-out value and will need to be resolved at some point. Is that something you would like to see them be proactive on, rather than just wait for things to fall over and then try to clear them up?

Neil Walsh: PPF is one of the few schemes that I have never had my members contact me about with a problem. It seems to be a very well run scheme. There is lots of speculation about whether there might be a future role for the PPF, and Prospect does not have a particular policy on that yet.

I think it would be informative—not necessarily from the PPF, but more from Government—to understand what is behind that. So far it has principally been about how to release funds and make pension scheme assets work more productively for the economy, but I think our members would be much more interested in knowing what the impact would be on them, how their outcomes would be either protected or improved, and how it would work in practice. Who is in scope for this? Is it the entire market? Is it just where, as in the original PPF submissions to this Committee, there are failures in the market so far? I think it is at a stage where the conversation is about high-level issues around investment and the competitiveness of the consolidator market. We would like to see a lot more information about what it would mean in practice for a member of the scheme being taken on by the PPF, or any consolidator, and how that would happen and what the impact would be on their outcomes.

Q165 **Chair:** You have all made a very clear case to us. Is there anything else that any of you want to put on the record?

Siobhan Baillie: You have waited six years to see the Minister; what

would be your key takeaway for the Minister today?

Terry Monk: The key is that we have not been listened to. In the very early days we had roundtable meetings, when Peter Hain was Secretary of State and Mike O'Brien was the Pensions Minister—or one of several during that time—and he was very good. He listened and he had members of what is now FAS around the table in Caxton House talking about the impact and how they have been affected.

I just happen to have come from a financial services background, so I have a reasonable understanding of the history and what has gone on in some of the legislation, but that is the past. The company and the scheme that I was in went belly up. Rightly or wrongly, they dumped us, and I went from a pension in excess of £30,000 into a pension of £3,000, which eventually got sorted—fortunately, by several million pounds being spent in the Hampshire case. The amount of money that was spent in defending it, whether it's PPF or DWP, or challenging it by all the members who contributed to the costs, must run into a few million pounds to just try to get the Government to comply with the legislation.

It does not seem that we have ever had the dialogue with whoever the Minister is or has been to say, "This is what it has done. These are real people." It is fine to produce legislation and cut-and-paste letters. We could write our own replies now to the letters that we write. I don't think they have had the courtesy and decency to listen to the people. The people who are affected, who we are trying to help, have not had the opportunity, other than standing on street corners and taking their clothes off on beaches to say, "We are stripped of our pensions," and saying to Ministers, "Treat us as we are: we are victims," and that is who they are there to serve.

Richard Nicholl: I will read out part of a testimonial from one of our members. It is his words and I think it sums up how people who are receiving FAS have gone through this long journey with us over 20 years of campaigning. This is my 93rd meeting. We have had some improvements, but we still need to go further. This is from a member in south Wales: "In December 2007, a number of us were asked to attend a meeting at the House of Commons with the then Pensions Minister Mike O'Brien, and we were told that we would receive 90% of our pensions. I left the meeting and phoned my wife and told her that all those past five years of relentless campaigning had paid off and we were to receive 90% of our promised pensions, but we would continue to fight for the 100% that we had paid for and were promised—only to find out some days later that the 90% was a mythical figure and over time our pensions would be eroding year on year as it did not include our scheme's pre-'97 indexation. The ASW scheme provided 5% per annum at RPI. To put it bluntly, we had been stitched up, so our campaign had to continue for what was rightfully ours, what we had paid for and what we deserve." That is how members of the PAG feel.

Terry Monk: The only contact that they had was when Stephen Doughty, who I think is a Member of Parliament for Cardiff, arranged—during the

covid days, admittedly—the only communication we had with the then Pensions Minister with the ASW boys. I sat in on the meeting and it was in a conference call. That is the only contact we ever had.

Roger Sainsbury: I would like to get away from the detail a bit and talk about some general principles. For example, to what purpose was the PPF originally created? What is it actually meant to do? To whom does it owe a duty? We know the answer to the first question—to what purpose was it set up?—because the Secretary of State, Andrew Smith, in leading the debate on the Second Reading of the 2004 Bill, said to the House: “a pension promise made should be a pension promise honoured”. That is why we are today scouting the creation of the Pension Protection Fund.

It seemed to be pretty clearly stated that the first obligation of the fund is to ensure that pension promises are honoured. It has been impossible for them to do that because the 1997 clause specifically says that there should be zero indexation for the pre-1997 service. That has made the situation pretty well impossible for the fund, because they are prevented by that clause from doing that which they have been charged to do: ensure that promises are honoured. In that very bad situation, what they should have been doing—and, as far as I know, what they have not been doing—is pointing out to the Government the tremendous evil done by this clause, which I think any fair-minded person has to see as being arbitrary, unjust, unfair, discriminatory and very damaging to the members. They should have been arguing to the Government all those wrong things about the clause and lobbying the Government to get rid of the clause.

Neil Walsh: The thing I would emphasise to the Minister is the timing. We recognise that the most likely way to achieve the just outcome for members of the PPF and FAS is through changing legislation. That will take time. As time goes on, members’ pensions and the benefits compensation are being eroded further and further and further. Some of these members will die before any of these changes come in, so I would urge the Government and the Minister to address this as soon as possible.

Terry Monk: Twenty-five thousand FAS members have died since it started, out of about 140,000.

Richard Nicholl: And we should remember, just to finish off, in terms of the taxpayer, that if we were to get any sort of uplift, 20% goes straight back to the Treasury, because at the moment the state pension is getting towards the frozen threshold. Our people feel that we are getting kicked a bit when we are down.

Chair: Thank you all very much indeed for the clear case that you have made and for being willing to put it to us this morning.

Examination of witnesses

Witnesses: Barry Kenneth, Oliver Morley and Sara Protheroe.

Q166 **Chair:** Welcome to you all; thank you for being with us. Can I start, as I did with the earlier panel, by asking each of you to tell us briefly who you are, starting with Barry Kenneth?

Barry Kenneth: I am Barry Kenneth. I am the chief investment officer of the Pension Protection Fund. It is my role to set the investment strategy of the fund and implement it in order to pay our members the compensation that falls due. I have been in post at the PPF for just over 10 years.

Oliver Morley: My name is Oliver Morley. I am chief executive of the Pension Protection Fund. We protect the pensions of around 10 million DB savers.

Sara Protheroe: Hello. I am Sara Protheroe. I have been involved with the PPF since before it opened its doors in 2005, but I am now the chief customer officer, responsible for the transfer of schemes to the PPF, the operational management of the Fraud Compensation Fund cases, and the payment of PPF and FAS members.

Q167 **David Linden:** The Pension Protection Fund now has £12 billion in reserves. Is it time to remove the regulators' objective of protecting PPF?

Oliver Morley: We have been fairly open, more widely, about that objective's looking a little bit anachronistic now, given the scale of reserves and the funding level. What I will say is that we are obviously going to come on to some of the calls on those reserves in the future—not only changes to compensation, but potential claims that are still out there, even though they are looking less likely. So it is not completely true that the PPF is safe under all circumstances in terms of providing compensation on that basis, but it is looking much more likely that we are.

What I would say is that it is still really important that there is an objective for the regulator. Obviously this is not my decision, but we still certainly believe that it would be worth having an objective specifically around the protection of DB savers.

Q168 **David Linden:** What would that revised objective look like, in your view?

Oliver Morley: I think it would be that wider sense of making sure—I would not want to get into drafting it—that there is clarity that DB savers are still a really important part of the pensions landscape, even if we make a transition to a world where there is much more DC.

Q169 **David Linden:** The 2022 review recommended that you work with DWP to ensure that the levy could be reduced, but of course raised again if needed. What progress have you made?

Oliver Morley: In terms of the PPF levy?

David Linden: Yes.

Oliver Morley: We have made very significant progress over the last five years since I joined the PPF. We started around the £600 million level in

terms of levy collection, and our most recent consultation is bringing that down to £100 million. As someone said to me, it is a rare thing, particularly in these days of indexation, that you will see costs reducing. We have made very significant strides in reducing levy over that time.

Q170 **David Linden:** Assuming that necessary legislative changes are made, what are your plans for the levy?

Oliver Morley: Certainly, if we had the right legislative framework, which would allow us to put up levy in a case of either significant changes on compensation or, indeed, large claims, then we would certainly be able to take levy—notwithstanding those two possibilities—to zero, ideally, over time.

Q171 **Sir Desmond Swayne:** Comrades, you were listening attentively to the demands that we discussed on indexation earlier. Which of those would you be prepared to accommodate? If you were, should the rule be an equality between FAS and PPF, and should any indexation of pre-1997 benefits be restricted to the original rules that members had signed up to in their schemes?

Oliver Morley: I will ask Sara to take you through some of the figures. Going to the point about the £12 billion in reserves, I think it is clear there are options for Government. Notwithstanding Roger's comment, we have made absolutely sure that the representations of the Deprived Pensioners Association and others have been made clear to the DWP and Ministers more widely. We think it is really important that that is transparent, and we have tried also to be transparent with the Committee in terms of the options.

These are choices we feel should be made by Government, because it is not true to say that the PPF is, effectively, a free fund; the reserves of the PPF are included in the whole of Government accounts, so they are offset against Government debt. It is important to note that any increase in spending on compensation for the PPF is, effectively, still borne by the taxpayer from that point of view, because of the implications for debt. So it is a choice that we feel needs to be made more widely. I do not think the PPF should be in a position where it is making those decisions, even if I think there is a good case, on equity grounds, around pre-1997; certainly I think some of the witness testimony there was compelling. Sara, do you want to give a comparison on some of the costs?

Sara Protheroe: Absolutely. As was recognised in the first session, our primary role is to implement the existing legislation, but we think we also have an important role in informing the debate about any potential future policy changes. That means sharing the member concerns you have just heard with colleagues at the DWP, but it also means providing analysis about potential future options, which we have obviously done with the Committee, both from a financial point of view and in terms of the wider implications for the broader pensions system. We have shared with you costs that range from about £2 billion up to £12.3 billion—so there is a very significant range of costs—on the PPF side. We have shared some

higher-level costs on the FAS side, looking at paying pre-1997 increases prospectively at CPI, capped at 2.5%. That would add £1 billion to FAS liabilities over the lifetime of those payments, with £57 million being paid out in the first five years.

Your question covered quite a lot of ground: it covered the PPF and FAS. As was mentioned in the previous session, it is important to recognise that, typically, a greater proportion of FAS member service was before 1997; 92% of FAS members have pre-1997 service, and 40% of those FAS members have only pre-1997 service. So this issue has a particular impact on FAS, but again, as covered in the previous session, FAS is funded by general taxation, so there are particular considerations there in terms of the funding source. But we do understand the concerns of both PPF and FAS members.

Q172 Selaine Saxby: There have been improvements in DB scheme funding levels over the last year. Within this overall positive picture, what do you see as the main risks to the PPF?

Barry Kenneth: Well, of course, most of the funding level improvement has been a back-up in long-term interest rates, and obviously that has been improving funding levels through the last two years, since we have, effectively, come out of the quantitative easing programme.

In terms of risks to the PPF, obviously the higher the funding levels, the less risk there is to the PPF, specifically on the basis that those funding levels have been locked in. So I think one point worth considering is this: how much of these funding levels has actually been locked in and, if there is a reversal of interest rates, do we end up in the position that we were in before?

In general, funding levels have improved, so that is a positive for us and for the overall community, but it is important that the universe of schemes continue to risk-manage these schemes and ensure that they can lock in the funding-level improvements they have had.

Q173 Selaine Saxby: Would you be able to track the extent to which they have been able to lock them in?

Barry Kenneth: Like any data source that we get, it tends to be retrospective, and we will get different scheme funding levels through time. What I can tell you is that, obviously, I am involved in and dealing in markets every day, and I would say the level of demand for liability protection over the last 12 months has certainly been less than it has been previously. The jury is probably out on how much of that funding level has been locked in. Many schemes have now given their long-term plans. You would expect that, as funding levels improve, they continue to reduce the volatility in their schemes in order to get to the end solution.

Q174 Selaine Saxby: Are there any underfunded schemes that are of particular concern?

Oliver Morley: Generally, we obviously do not talk about them more widely. We work very closely with the regulator on concerns around

particular schemes and particularly where there is a potential for insolvency. At the moment, I would say that the overall level of insolvency, particularly in our universe, is very low. The level of risk and indeed the overall volume of claims—even though we have obviously had a relatively high-profile one recently—both in terms of numbers and liabilities, has been relatively low recently.

- Q175 **Siobhan Baillie:** Barry, I would like to look at the significant decline in asset values. We have got the PPF estimate at about £400 billion lower than the ONS estimate at £626 billion. I think that, looking at the prep we were doing, the ONS starts from a higher place at over £2 billion. Can you explain the difference between your assessments and is there work under way to try and agree a figure with the ONS?

Barry Kenneth: First, we have had engagement with the ONS in terms of their data collection. I think it is worthwhile pointing out that the rationale for the collection of both sets of data is different, and the construction of how we extract the data is different. From a PPF perspective, we obviously take the last funding levels of schemes that we have on a section 179 basis and project that forward. There is an element of an expected movement through the roll-forward basis. The ONS has a smaller sample of schemes; I think they sample about 900 schemes broadly across both DB-DC and some hybrid schemes, and their extraction of data is every three months.

From an asset-side perspective, the ONS has a different data set than we have. We are trying to do slightly different things, whereby we are trying to look at the risk on the PPF's balance sheet in terms of what schemes may come in to us. The funding level is extremely important on a section 179 basis. To my understanding, the ONS is more dedicated to the asset-side valuation, of which it takes a different data set on. There are differences for the reasons I have explained. Are we trying to get to a homogeneous place? I do not think so. We collect data for our balance sheet and for the risk to the PPF. We are quite comfortable in the methodology with which we collect data. As I said, I think the ONS collects it for a different reason.

Oliver Morley: We are very keen that we understand the differences and that we work with the ONS, but the data is effectively collected for two different purposes. The other thing I would say is that of course an asset-value decline inherently is not a bad thing if the other side, i.e. the liabilities, have gone down at the same time. There was some reporting around asset prices going down. As long as the other side—in terms of pension liabilities—is going down simultaneously, that effectively reflects a good hedge, as opposed to bad news across the board.

- Q176 **Siobhan Baillie:** My next question was going to be about the extent to which, and under what circumstances, does the decline in asset values have a negative impact on the scheme. I think you are saying that, if the other side is not going down, then that is where it has the negative impact. It is case by case.

Oliver Morley: Generally, in terms of the markets, it has been more than offset by the liabilities, and that is as a result of the interest rate changes. You would see a problem if asset prices have declined without a related decline in liabilities.

Siobhan Baillie: Do you want to come in, Nigel? You were sucking teeth—noisily.

Q177 **Nigel Mills:** I suppose it wanders us back into the accounting questions, doesn't it? If I have invested in index-linked investments and inflation just changes the assets and the liabilities because it is the same calculation, that makes sense, but there is not necessarily a logic for why. If interest rates go up, your asset value has gone down—it is just a function of the accounting methodology we are using, I suppose.

Barry Kenneth: I do not think it is just accounting, ultimately. Effectively, if you have a long-term payment to make and you buy some form of fixed-income security in order to make that payment, then the value of the asset and the prospective payment should move in tandem. You can maybe look at it as an asset-side issue, whereby you can turn around when rates were lower and say there is a hurdle rate in which to meet liabilities—let's say when interest rates were closer to 1 or 2%. The asset side needs to generate 1 or 2% in order to meet that liability. Now, given that interest rates have gone up, for the same liability the hurdle rate increases. With interest rates now around 5%, the asset-side hurdle needs to be 5% in order to make that long-term payment. So fixed-income solutions do allow the volatility of that payment and the certainty of that payment to be realised. I do not think it is just an accounting point.

Q178 **Nigel Mills:** I suppose if pension schemes have invested in gilt, you have still got all the same cash flows you thought you were going to have—it is just that in theory, if you wanted to sell them, they are worth less because there are new gilts at a higher rate. You could have an asset value reduction on your balance sheet, but in actual fact it does not change any of your future cash flows, so it is a slightly counter-intuitive position, isn't it?

Barry Kenneth: It leads us back to Oliver's point. In terms of the asset and liability values, if you're holding a gilt versus a liability, if the gilt value goes down and the gilt is used to hedge that future payment, the asset value deterioration and the liability value deterioration should be equal—which is no different from the converse side of that post-2008 when the liability values increased materially in value but, on the same side, if you were holding Government bonds at that point in time they would have increased at the same rate in value.

Q179 **Nigel Mills:** It just makes you wonder how meaningful these numbers are, doesn't it? "I'm holding a gilt, I'm going to hold it through to maturity—all I really care about is the future cash flows that are coming in to meet my outgoings, and yet somehow my balance sheet has materially changed by £400 billion in the last year."

Barry Kenneth: The actual expected payment you would receive would be the same regardless of the mark-to-market variability through time.

Nigel Mills: Yes. It doesn't actually give me any useful information as to whether I am going to be able to meet my pension obligations at all. It is just a point-in-time set of assumptions that do not tell us anything.

Q180 **Chair:** Can I pick the point up a little? The figures you have given us—asset values of £1.8 trillion, and now £1.4 trillion. That is a huge fall. How much of that £400 billion would you expect to come back if, or when, interest rates go in the other direction? It certainly isn't all of it, is it? Is it any of it?

Barry Kenneth: If the £1.4 trillion of assets you talk about was purely invested in fixed-income related assets or Government bonds, and the current liability was £1.4 trillion—without going into too much technical detail, that is discounted cash flow. Cash flows you make in the future—you discount a certain value to get to today's value. If you discount that the gilt yield, then you will have equal and opposite for your assets and liabilities. Through time, if long-term interest rates fall, both the assets and liabilities of any scheme will increase. If interest rates continue to rise, then you would expect the assets and liabilities both to fall.

As the gentleman explained there, mark-to-market through time is just a point-in-time valuation. Ultimately, when we are putting these types of strategies in place, you are doing it with the future cash flow payment you are expected to make in time—you are trying to figure how you actually meet that payment with a large degree of certainty. Buying fixed-income instruments allows you to do that.

Q181 **Chair:** But how much of the £400 billion loss do you think resulted from the LDI problems and those particular difficulties?

Barry Kenneth: Most of it, I suspect. To say it is a loss—it is a fallen asset value, but in the same vein as that when interest rates deteriorated, the value of these assets and liabilities would have gone up, so they are just changes in values. But we are here to try to build an asset allocation, like many of my colleagues and peers out there, to try to meet these compensation payments that have been defined, in the future. Part of that strategy will always be to invest in fixing—

Q182 **Chair:** Can I push you a little bit on this LDI point? You are saying that most of it, if not all, was down to the LDI problems. A lot of panic selling happened at that period, as we have heard in the Committee. That is not going to be recovered at any time, is it?

Oliver Morley: Sorry, just to clarify—Barry can correct me if I am wrong—that the asset decline is not due to the LDI problems per se. Some amount of that will come from the LDI problems—the fire sales, as Barry spoke about. The decline in assets comes from the liability-driven investment approach as a whole, as in using fixed income to effectively hedge the liabilities. So it is not the problems, per se, that created that asset decline.

Q183 **Chair:** How much of the £400 billion do you think was caused by the fire sale problems around September of last year?

Barry Kenneth: You are effectively talking about the actual loss that these schemes, from a balance sheet perspective, have lost?

Oliver Morley: As a short-term disruption.

Barry Kenneth: I think it is difficult to tell. For those schemes that were able to hold the asset, or hold the LDI fund or security or Government bond: by definition, if they haven't sold it, it would still be there in order to pay for the future liability. Where the losses would have come is for the schemes that have invested in these securities or these products—pooled funds—that were forced liquidators of these funds and were not able to then hedge back into the market.

What I can say is that the values of long-term interest rates today are not quite back up to where they were at the time of the crisis, but have certainly moved back there post the Bank of England's operations of buying gilt securities at that point in time.

Q184 **Chair:** Is it possible for you to estimate the aggregate value of the fire sale losses through the mechanism that you have just described?

Barry Kenneth: I think we will find that through time, because different schemes are in different positions.

Q185 **Chair:** How long do you think it would take us to find it?

Barry Kenneth: I think that will depend on the data we receive, but I imagine it would be years until we find out the true extent of what has actually happened for each individual scheme.

Q186 **Siobhan Baillie:** There is a real-life scheme in all our post boxes, because Wilko has stores near all of us—we have lost jobs everywhere. We understand that the Wilko scheme used LDI and lost about £30 million of assets. We understand it also might be entering the PPF. Are Wilko members likely to experience an absolute loss? Sara, can you tell us about any conversations or engagement with Wilko?

Sara Protheroe: The Wilkinson Group pension scheme has entered a PPF assessment period, and this is precisely the situation that PPF was set up to deal with, which is employer insolvency. Member payments are continuing uninterrupted, and those above the scheme's pension age are receiving 100% of their starting pension. It is hopefully a reassuring time for members, where they know they will ultimately receive at least a minimum of PPF level of benefits, if not more. As is usual, we take on the creditor rights during the assessment period, and so we will be actively seeking to maximise recoveries from the employer.

Q187 **Siobhan Baillie:** Can I turn to Barry on the LDI involvement with Wilko?

Barry Kenneth: In terms of the data that I have seen thus far, the LDI programme they adopted was there to hedge the scheme, so they have not over-hedged the scheme. For any paper loss that they would take on

the asset side, there would be an equivalent write-down on the liabilities side. Their LDI programme, per se, did not cost any money, but they have adopted that programme in order to hedge their liabilities. I would expect to see an equivalent on the liability side to what you would see on the asset side.

Q188 **Shaun Bailey:** I want to touch on the debate around a potential increase in PPF compensation, and perhaps funding that through easier access to fund surpluses. I want to get your take, first, on whether that is a feasible option, and secondly on the risk-to-reward factors that are involved, particularly with access to surplus. My potential concern is that there is perhaps a benefit to larger schemes that may have a surplus, but for other schemes that may not necessarily be a viable option. I am curious to get your perspectives. Barry or Oliver, would you like to start?

Oliver Morley: Specifically on providing them access, for example, via the LCP proposal?

Shaun Bailey: Yes.

Oliver Morley: Barry, do you want to speak on this?

Barry Kenneth: There are two elements to the LCP proposal. The first concerns pension schemes re-risking their balance sheets to try to generate a larger surplus that can be used to fund future pension payments from the company.

The first thing I would say is that we have been on a journey for the last 20 years whereby pension schemes have de-risked and have tried to manage the volatility of their funding levels, certainly from a corporate sponsor and trustee perspective. As we have previously mentioned, the scheme funding levels have improved materially in that time.

From a corporate sponsor perspective, I would imagine—this is certainly our experience—that to get closer to the end solution but then re-risk the pension scheme and create more volatility, not only on the pension fund balance sheet but on the corporate balance sheet, would be unlikely to result in a large take-up. It is a question that you would have to ask them, but it is unlikely that the corporates would allow that to happen.

Obviously there have been other parts to it, with regard to enhanced PPF benefits and so forth. I will open this up to my colleagues as well, but I would guess that in order to create a new proposition to enhance benefits, you would need a wide levy pool and a wide breadth of businesses. The intelligence that we have received thus far is that there would not be a wide take-up, so it would be a challenge to get a breadth of levy and timespan.

The last thing I would say is that it would take a long time to get the benefits from investing in riskier investments, which I think was part of the proposal. With increased volatility, and generally on the riskier side of the asset spectrum, you would expect to receive these returns through time. Obviously, if there is a funding level drop in the intervening period, I

would imagine the trustees would be asking the corporate for more funding payments through that time. It is something that schemes can run on, and they can add a little bit more risk to the portfolio, depending on the corporate sponsor, but I think it would be a challenge to get a large take-up.

Q189 **Shaun Bailey:** So what you are saying, Barry, is that the LCP proposal could in some respects create more risk for certain schemes when you are pulling from that funding pool, in terms of those levies? Am I understanding that correctly? Apologies if I am misunderstanding you.

Barry Kenneth: I would expect it to create more short-term risk, because of the underlying investments. If we are talking about UK productive finance, in putting more capital at risk for these assets you would expect them, by definition, to be slightly more volatile, and for their returns to come to fruition through time. You would expect more balance sheet volatility within that time span.

Q190 **Shaun Bailey:** I suppose that this is the question from a policy perspective: do you take the short-term volatility, but potentially the longer-term security that may come from that? Clearly, it is how you manage that short-term volatility in that initial period, were those proposals to be adopted.

Oliver Morley: It is also a problem for trustees under those circumstances, because we are effectively asking them to make a short-term decision, notwithstanding that they may have protection for that decision. When we talk to trustees about this issue, it certainly seems to be an understandable worry when it comes to their fiduciary duty and their duty to members. Even that short-term risk is of concern to them.

Q191 **Shaun Bailey:** What would you say in answer to the question whether the risks outweigh any potential benefits? I know we have talked about it in the context of short-term risks, but is it inconclusive?

Oliver Morley: I am sure you could structure it in such a way as to mitigate some of those risks and make it worthwhile, but it is quite a complicated hammer to crack a nut, in terms of being able to get that policy to work in such a way that you get the right kind of scale, trustees go for it, it makes sense for members in particular under those circumstances and it gives you scale on productive finance. That is quite a lot to ask from a policy.

Q192 **Shaun Bailey:** I want to turn quickly to the DB code, particularly the new DB funding code. Do you think the code still has a role to play within the pensions landscape, or do you think it may be time to re-evaluate where we are with that?

Oliver Morley: I am sure colleagues will have a view. I think some of Barry's comments apply more widely. It is this question as to whether this is a point in time of DB pension surpluses or whether that could change in future. We strongly believe that there is still a role for a DB funding code in a situation in which schemes do not necessarily maintain surpluses or have funding issues in the future. Although it may look extremely positive

at present, and we are obviously pleased about that, there certainly is still a role for a funding code.

Sara Protheroe: I support what Oliver said. We are conscious that there remains a subset of stressed schemes. There are 240 schemes, for example, that are funded below 80% on a PPF basis and have sponsors that, on our levy methodology, are ranked 8 or worse. There are still schemes that are facing significant challenges, and it can only make sense for schemes to have a long-term objective and a journey plan for how they are going to get there.

Barry Kenneth: I have nothing further to add.

Q193 **Nigel Mills:** It almost feels a bit like “job done”, doesn’t it? We have had 20 years of the PPF; we have had a cocaine-fuelled rollercoaster ride for the last 20 years, and now everything is fine and so well-funded that we can all just let these things mature into the distance and worry about something else. But I think you are going to tell me that that is not a fair assessment of the sweet spot we have got ourselves into, and there is still quite a lot of risk out there.

I think Sara said that there are 240 schemes that you still have on your watch list. If they are really, at this present pension optimum, funded at below 80%, is there any realistic chance that they will ever be able to pay the full benefit that they have promised?

Oliver Morley: Let’s start with the cocaine-fuelled rollercoaster. I am looking back for various reasons at the moment, as you can imagine. Since the PPF has started, there have only been two years in which our reserves have fallen. I do not think, in terms of consistency of performance, you would really describe that as a rollercoaster. We have managed to give that kind of consistency over time. That is part of the reason things have worked, but also one of the reasons we have been able to give assurance to members.

One of the reasons we have engaged with the call for evidence around the future of DB is that we believe that there need to be some solutions to the schemes that are not necessarily attractive or on an elegant path to buy-out. We need to think in policy terms about what we do with that, and we think it is a useful debate to get into. What is going to happen to those schemes in the long run, because they may well not be able to solve the question of those long-term benefits? We certainly believe that there is a discussion to be had about that.

Q194 **Nigel Mills:** Which takes us neatly into the consolidator options. My first question is: are you saying that there is a better solution than you sitting around, waiting for things to go pop and then picking them up? Could you proactively take on schemes before they go pop, although there is an expectation that, at some point, that will happen anyway? What are the advantages of doing that? Is it just that you can invest better and use the funding better, so in the long run it is less of a hit on the scheme because you can manage the deficit down better than the scheme could? Is that the kind of pitch you are making?

Sara Protheroe: We have a really strong track record of delivering against our current remit. We have transferred over 1,000 schemes into PPF, and a further over 1,000 schemes into FAS. We have reached a position of financial and operational maturity with strong in-house capabilities. As the DWP review that some of you referred to mentioned, it is perhaps time to think about what more we could do in the pension space. We feel we potentially have further value to add.

Q195 **Nigel Mills:** Where do we draw the line? We never really wanted to have a nationalised DB sector, and obviously there are commercial consolidators out there. I think we all agree that that consolidation would probably be a good thing—we have seen the first deal go over the line this weekend—so is your pitch, “Let’s have a nationalised super-DB scheme. We’re so great that we don’t need all these other ones”? Or are you saying, “We shouldn’t touch schemes that can get to buy-out. We also shouldn’t touch schemes that can’t quite do that, but the private consolidator can get them there; that should be left”? Do you only want the ones that are a problem and will never get to buy-out or private consolidation? Is that what you are pitching? Is that what your role could be?

Oliver Morley: In some ways, this goes to the question you are trying to answer. If there is a wider productive finance question, you need scale. That is something we can address at scale. I wouldn’t go to the extent of a nationalised DB, etc., but you do need scale. At a smaller scale, you are really solving for a different question, which is the question of smaller underfunded schemes. That is where you start talking about drawing lines.

Barry Kenneth: I just thought that a couple of stats might be important here. The deal you allude to—the Sears pension scheme—was £600 million. Ultimately, in terms of the capacity in the buy-out sector, the types of scheme that commercial consolidators are looking at tend to be of higher value. There are lots of well-funded pension schemes out there for the insurance model, and they only have a limited amount of capacity to price transactions, so they get the biggest bang for their buck from larger transactions.

The commercial consolidator approach is to get scale in asset management. Again, as we have seen previously—the two super-funds have obviously been trying to do business for the last few years—the schemes that are on their radar tended to be the higher-value ones. If you take that back into our universe, 3,500 of the 5,100 DB pension schemes are less than £100 million. The solutions that are open to those smaller schemes are more limited than might be suggested. From a scale perspective, the top 4,500 schemes out of those 5,100 schemes account for only about 15% of the total DB assets, so there is a huge amount of concentration at the smaller end of the DB universe.

From a consolidator approach, whether it is for stressed schemes or just the smaller elements, as Sara mentioned, our experience of transferring in schemes is important. The second thing is that, when trying to improve the efficiency of these small schemes, they have high governance costs

and limited access to investment management solutions. They tend to be pooled approaches. They do not really have the access to a wide array of diversified investments, and they have high governance costs.

In terms of consolidating these schemes, I think there are two elements. One is that they are quite inefficient at the moment, and I am sure that most companies would like to get these smaller schemes off their balance sheet. The second thing is that, on the solution side, there are actually more limited solutions out there for these schemes. Certainly that has been our experience when we have talked to some of these schemes.

If you link that back into the Chancellor's objective in his Mansion House speech—getting growth into the UK—then scale allows you to be able to do that, so effectively you can solve the two issues with one consolidator. As Oliver has mentioned, in terms of the time horizon, we look at long-term investments, so we take a different approach from that of a typical DB scheme, where the corporate has to announce its balance sheet every year and so one-year returns are important. Time horizon, scale and professional management allow these smaller schemes to lose the governance cost and invest in diversified asset pools that should give them better outcomes.

Q196 Nigel Mills: I get all that. I am just trying to work out what your pitch is. Are you saying to DWP and the Government, "We would like to be the consolidator for all small schemes that want to be consolidated, please"? Is that what you are asking to do?

Oliver Morley: I probably would not use the word "pitch". In terms of where we are, we are engaging in the policy discussion. Putting aside the huge-scale policy discussion, which is in some ways separate, at this smaller-scale level we are conscious that there is a desire to avoid encroaching on areas where there is no market dysfunction. Where there is a functioning consolidated/buy-out market, we should obviously not supersede that area, unless you wish to have that huge scale.

We cannot necessarily define that, and we are very conscious that a lot of the stakeholders, for example the insurers, will want to be involved in it. They want to be able to engage in that too. We are not overtly saying, "This is the market; this is the level." We understand that there is going to be more policy discussion to define where those areas are.

I would add one other thing about the efficiencies if we do consolidate: the quality of administration is one of the areas that is a real challenge for small schemes. We see them when they come into us—when there has been an insolvency, obviously—and there are certainly efficiencies and improvements that can be made around the administration of small schemes too.

Q197 Nigel Mills: I don't know if I am any further forward. So, let the schemes that can reach buy-out run themselves to buy-out. I think we have had evidence that even small schemes can get buy-out, and there have been quite a lot of buy-outs at the smaller end of the sector, so we are not

saying that there is a problem there.

Oliver Morley: I have had discussions with the insurers. I think that that is for the most part right, but it is not always true. If they are administratively complex, more marginal on funding and very small-scale, it is not always that attractive for the insurers to take them on. They may issue a quote, for example, but that quote may not be competitive.

Sara Protheroe: There is also an issue of timescales. The largest level of buy-out business in a previous year was, I think, £44 billion in 2019. We expect this year to be a landmark year in terms of its size. But against the backdrop of £1 trillion in liabilities, it will be many, many years hence before all schemes would get the opportunity to buy out, and it is likely that smaller schemes would fall towards the end of that queue.

Q198 **Nigel Mills:** I think I'm getting there now. You are basically saying that if the Government decided we wanted to strongly encourage consolidation of smaller schemes and trustees were minded to agree with that, you in theory would be quite willing to clear up the tail if somebody asked you to do that. You are not necessarily asking to do it, but you would be willing if somebody else thought that it was a good idea.

It leaves us in a slightly counterintuitive position, which you alluded to earlier. You are on the Government balance sheet—you are on the books—and so we end up with this huge pension scheme having, effectively, lent the Government a load of money. It almost looks like it is lending itself a load of money to pay for gilts. Then what we are effectively doing is that, on balance sheet, we are investing in slightly risky parts of the economy. Generally, the Government has decided that it is not the role of the Government and public finances to go wholesale investing in risky things around the economy; that is for the private sector to do. So don't we end up in a slightly odd position? We want more money in productive finance, but do we really want that on balance sheet? We are unravelling years of public sector financial orthodoxy here by starting to go in and, effectively, invest ourselves.

Oliver Morley: It would be separate—

Barry Kenneth: When we build a strategic asset allocation investment strategy of the PPF—I am sure this would be similar to a consolidated model—we are doing that with risk management in mind. If we look at the assets in terms of that, the PPF's current asset allocation is that about 70% of our assets are invested in what you would classify as an annuity or bond-like strategy; the remaining 30% is in what you would maybe classify as productive finance, and that productive finance is distributed geographically and in different sectors. So there is a huge amount of diversification. It is not sitting in the UK specifically.

I think that about 6% of our total assets are in UK productive finance, so we don't have a huge exposure, in terms of our whole balance sheet, to UK productive finance. And 24% of the fund will sit in different geographies, and that could be split between private and public equity—infrastructure, real estate and the like. So in every investment strategy

that we would run, whether it be a public consolidator or the current PPF model, diversification is huge, and risk management is also paramount.

So I wouldn't say that the way we invest is risky. In fact, I think our risk budget, certainly in historical terms, has been a fraction or a percentage of that of a general DB scheme. So I think that our investment strategy is relatively low risk. It is extremely well diversified in order that we are never exposed to one factor or one geography that would hugely impact the investment strategy of the scheme.

Q199 Nigel Mills: At what point does the levy model start to become a bit odd? If we see a lot of buy-outs taking schemes out of the market and we saw you consolidate a lot, presumably there are not many people left for you to levy on if things start to go wrong. We are effectively then towards the end of the—

Oliver Morley: And that is exactly why we have been taking down the levy over time as the risk has declined in terms of the wider universe. Certainly there are arguments—if we were to be a consolidator that could actively deal with some of those schemes that were more of a risk to us, that would also reflect in the levy, not directly, because as I said it would certainly be seen as two separate funds with two separate approaches, but, in terms of the overall risk to the PPF as it currently stands, we would believe that we would be in a position to gradually reduce that risk also as we took out some of the tail at the same time.

Q200 Nigel Mills: Let's say the Chancellor got creative and decided, "I've got this great idea. I can go and effectively not quite force but strongly regulatorily encourage a large amount of consolidation quite quickly into a public consolidator. I can get myself several hundred billion pounds in there and I can then use a good chunk of that to invest in the kind of productive growth investing that we all want to see." Are we not basically just nationalising the risk? Will we have to have taxpayers on the hook, because if this goes wrong we will have to meet the promise? That is effectively where we would be. If it was all on the balance sheet, we would have effectively directed this. We would go from a situation where we have tried to keep the taxpayer off the hook for a long time, not giving people pre-1997 indexation and not taking on all those old liabilities, to saying, "We are near enough maturity now. We will take the risk now and use the money how we want to."

Oliver Morley: May I refer to Barry's previous comment? It needs to be understood in the context of a wider portfolio. The scale and longevity would mean there is more opportunity for productive finance, but you are not saying that you are going to make significant changes to the overall risk. Within a very large-scale, diverse portfolio, there would be more opportunity for productive finance without increasing the overall risk of that portfolio considerably.

Q201 Nigel Mills: So there is no chance this could go wrong and effectively put the taxpayer on the hook.

Oliver Morley: It all goes to the policy design and the legislative framework that you would have for the consolidator. On the PPF, there was always the chance that the PPF could have gone wrong. From a legislative perspective—Sara was there from the beginning, as others were—the design of that legislation was scrupulous in making sure that the risk was carefully managed and that the board had a responsibility for managing that risk.

Q202 **Chair:** I have a further question on consolidation. On a different aspect of consolidation, Nigel mentioned in passing the fact that earlier this week Clara Pensions has announced its first transaction, which is perhaps a positive indication for the prospects of a superfund consolidation. On the other hand, there wasn't a pensions Bill in the King's Speech yesterday, although the Chancellor has referred to the importance of a statutory framework for superfunds. Do you think that in the absence of legislation it will be harder for superfunds to develop?

Oliver Morley: Obviously it has taken a long time. We were first generally talking about superfunds when I arrived at PPF five years ago and the first sale has just happened. It has taken a long time. The lack of regulatory clarity has to an extent hindered the development of options. It is not the whole story in terms of some of the reasons that it has taken a long while to get to this point, but clearly for a new business, having that regulatory clarity does help. We have engaged throughout with the regulator and both of the consolidators to talk to them about how to implement levy and things like that for a consolidator. So, yes, I think that on balance I would be more positive. A clear regulatory environment would help consolidators.

Q203 **Chair:** I think your first appearance in your current capacity before this Committee was five years ago. At that time you said to the Committee that superfunds could be a risk for the PPF. This is your last appearance before the Committee in your current capacity, but you might be back in a different one shortly. What is your view now? Do you still see risks to the PPF from the development of superfunds?

Oliver Morley: The same risks exist. This was always a question around capital adequacy and the ability to make sure that the promises made to members at the time of a consolidator taking over would be able to be supported. Obviously, that depended to an extent on the scale. Certainly, at that point, our view was that consolidators could be a real, considerable shift in the market in terms of them being able to take over schemes. That has been less because the volume has been lower, and the risk therefore is significantly smaller. If consolidators did take off, there would still be a risk and that is indeed part of the reason and the purpose of the regulatory framework that would be put in place to ensure that was managed.

Q204 **Chair:** So if a regulatory framework does come forward, you would be reasonably relaxed in the PPF?

Oliver Morley: We would be supportive if it were the right regulatory framework and it ensured that the interests of members were protected.

Q205 Chair: Can we go back for a minute to the discussion we were having earlier about what happened around the LDI event? I want to press you a little bit further. Your figures say that £400 billion in defined benefit pension scheme assets has been lost pre-LDI and post-LDI. Some of that was a result of the fire sale difficulties that a lot of schemes got into at that point. You made the point that it is going to take quite a long time until we know how much of it was that, but some of it certainly was. Are you able to give us a finger-in-the-air guess as to how much of the £400 billion was a result of that fire sale?

Barry Kenneth: It is a more complex issue than just how much money was potentially lost on pension funds that were forced to liquidate their hedges because they had to liquidate assets in order to get the cash. Some schemes were able to liquidate assets to get cash in order to pay collateral into the positions that they had, so you could argue that the assets they sold maybe did not sell for true value. The actual loss—it is going to be almost impossible to look at that crisis in isolation, or the Government yields rising so quickly in isolation, and try and figure out a number. There were lots of different moving parts for different pension schemes in order to satisfy the ramifications for interest rates moving higher in a very short space of time.

If you want to confine it to, “How many schemes lost money on the liquidating of hedges?”, I suspect over time you will see that through the funding level of schemes. But in the round, as the PPF, we would never get data on schemes that have liquidated hedges and on what it cost them to liquidate hedges based on what they invested in at. I do not think we will ever come up with a true number. What we do know is that there was a significant amount of pooled vehicles that were liquidated around the same time. I would guess that the biggest asset managers who look after the pool vehicles will be able to give you a better steer to what that would be than the PPF. We will get information in the round as opposed to on specific parts of investment strategy.

Q206 Chair: A finger-in-the-air guess?

Barry Kenneth: I would not know how to answer that.

Oliver Morley: The problem for us, and we are not trying to avoid it, is that it is perfectly possible for a single scheme—as a kind of case study—that has lost significant amounts of money liquidating for cash to have actually come out with a very large asset decline, but also now have a much rosier picture in terms of surplus. All those three things can happen in one scheme over that period as a result of the asset disruption. It is almost impossible, in terms of the way they would report, to have picked out that one element of a decline on the asset.

Q207 Chair: Let me ask you about one specific scheme that we have touched on—the Wilko scheme. This morning, we published a letter sent to us from the Pensions Regulator showing that the value of the Wilko pension scheme assets fell from £158 million in the second quarter of 2022 to £121 million in the second quarter of this year. That is a big fall—£37

million or so—and of course that has now crystalised, given the insolvency of the company. You have obviously looked at Wilko very carefully. Are you able to tell us how much of that loss was a result of these fire sale problems around LDI?

Oliver Morley: We would have to come back to you. I am not overly sure we could, but we could come back to you and see if there is any breakdown. I think it is unlikely that we would be able to piece it back to that specific level. If the surplus as a whole—I think it is very slightly in surplus on S179—has improved, that would almost entirely be netted out anyway, so we would have to have a look. We could give you some breakdown, based on our figures.

Q208 **Chair:** That would be interesting to know. It is not anywhere near surplus on a buy-out basis, is it?

Oliver Morley: No—on S179.

Sara Protheroe: And I think we are still looking into the situation.

Q209 **Chair:** I imagine the £37 million loss will have had a material impact on the outcome of your assessment.

Sara Protheroe: As we discussed earlier, it depends on what has happened to the liabilities during the same period. I don't think we have the figures in front of us today.

Chair: It would be very helpful if we could see those.

Q210 **Siobhan Baillie:** I think Wilko had quite a lot of problems. I listened to Barry when he said that they didn't over-hedge the scheme, so it seems quite a complicated picture.

I have almost a wrap-up question, subject to the Chair's final points. My assessment—and not just because they are "my gang"—is that we have a very capable and caring Pensions Minister and a very financially literate Secretary of State, and the Chancellor of the Exchequer is taking direct aim at pensions in big speeches and things like that, and yet if His Majesty the King had talked about pensions yesterday, I would have fallen off my chair, because it is just not sexy. It is really hard to get parliamentary time for any changes in legislation. I was thinking during the previous panel that all the political parties—Labour, the Conservatives and the Lib Dems—are on the hook for not making improvements to pensions legislation over the years.

I just wanted to get your comments—Oliver, in particular. I don't want to put words in his mouth, but Roger Sainsbury pointed out that he felt slightly let down that PPF had not started fighting a bit harder or using your very capable voice. Sara said—I wrote it down—that PPF has more to add in using your voice to do things like arguing for changes, post the Hughes case, to the compensation cap. Can we hear more from PPF, and all of you with your expertise, to get some of these changes? It is quite hard for MPs to get this stuff heard, even with all this attention that we are getting.

Oliver Morley: We are conscious that we are an arm's length body, so there are limitations. I understand Roger's frustration with it, but we are limited, particularly in what we say publicly. We make absolutely sure that these representations are passed on, and we try to be clear with everyone involved. We haven't been opaque; we have been explicit about some of the trade-offs. Where Roger and I differ is that I feel strongly that these are big decisions. Regardless of anything else, even if it is not pre-'97—not retrospective—this is £2 billion. Even if it is not directly taxpayers' money, it still has implications, and there are still wider choices that need to be made. It is not just about DB; it is about DC pensions obligations, etc. There is a wider framework around pensions. For me—I am not a civil servant but a public servant—it is important that these decisions are made in the right way by Parliament and Ministers. We will always be as transparent as we possibly can be about those trade-offs so that people can understand them and make the right decision.

Q211 **Siobhan Baillie:** Sara, you are close to the schemes coming in. Is there anything else that you want to add to that?

Sara Protheroe: We recognise that PPF's position has evolved since the legislation was introduced back in 2004. We recognise that our funding is now more robust and that the risks that we face have reduced. As we talked about earlier, the current inflationary environment is of significant concern. We see why that is leading to renewed interest in our compensation levels, and we would be open to direction from Government on that issue.

Q212 **Siobhan Baillie:** I have one more question. If you get to self-sufficiency in 2030, does that change how you are governed as an arm's length body or is it literally about your financial status?

Oliver Morley: We actually have moved away from that approach. It is probably fair to say that in some ways we are reaching, or have reached, self-sufficiency much more quickly than we would have expected. That is the reason for our funding strategy work, which we have effectively completed. I think we are already in a different place, in terms of our long-term sustainability, and that is also why we are looking to reduce levy.

Sara Protheroe: But it doesn't give us any greater powers.

Siobhan Baillie: It doesn't change the way you can push the Government. Okay.

Q213 **Chair:** You said you have reached self-sufficiency. Is that what you are saying?

Oliver Morley: We haven't had a fundamental point where we have assessed whether we have reached self-sufficiency or not, but I think the implication of our reserves and our financial position is that—I put it in terms of levy—we can substantially reduce levy.

Chair: Thank you. It has been a very helpful and interesting session. Thank you all very much indeed. Oliver, all our best wishes, and we look

forward to seeing you again with a different hat on, hopefully before too long.