Written evidence from the Railways Pension Trustee Company Limited (RPTCL) LDI0015

We write to you on behalf of Railways Pension Trustee Company Limited (RPTCL) in response to the above call for evidence launched by the Work and Pensions Select Committee (WPSC).

RPTCL and its subsidiary, Railpen, have been proactively engaging with the Department for Work and Pensions (DWP), the Pensions Regulator (TPR), and other key stakeholders throughout the development of a new funding and investment regime for UK Defined Benefit (DB) pension schemes. We are concerned that the latest proposals, as set out in the DWP's *draft Occupational Pension Schemes (Funding and Investment Strategy and Amendment) Regulations 2023* (the 'draft regulations'), could exacerbate systemic risks to the UK economy due to pension scheme 'herding'. Therefore, while we are not commenting on the LDI specific aspects of this call for evidence, we thought the WPSC may find our views on the draft regulations helpful, noting that the implications for DB funding rules were an area of particular interest.

About us

RPTCL is the corporate trustee of the principal pension schemes in the UK railway industry, including the Railways Pension Scheme (RPS), the British Transport Police Force Superannuation Fund (BTPFSF), the British Railways Superannuation Fund (BRSF), and the BR (1974) Pension Fund. Collectively, the schemes we support provide DB pensions for over 350,000 members from almost 150 companies operating within the railway industry, with combined assets of over £35 billion.

These schemes serve as excellent examples of the variety of schemes that UK pension regulations need to cater for within a truly flexible, scheme specific, funding and investment regime. For example, the RPS is a sectionalised multi-employer scheme, having over 100 distinct sections that each carry out their own actuarial valuation under Part 3 of the Pensions Act 2004. Many of these sections operate on a shared cost basis, with contributing members paying 40% of the cost of benefit accrual and deficit contributions, if required, and employers paying the remaining 60% of this cost. Within the RPS and the BTPFSF, there are still over 100,000 active members accruing defined benefits for future service. Around 90,000 of these members belong to over 40 schemes/sections that remain open to new entrants and, in 2021, there were over 6,000 new entrants admitted to defined benefit membership in the RPS and the BTPFSF.

We recognise that our schemes have characteristics that are not typical in the universe of UK DB schemes. However, our schemes are important, not simply to our members, but also to employers and the wider UK railway industry. It is essential that pension regulations allow members to continue to build up affordable and sustainable DB pensions, and that the Trustee remains able to pay these benefits over the long-term.

RPTCL's views on increases in systemic risk arising from draft regulations

RPTCL is concerned by the DWP's recent consultation on its draft regulations, and the implications these proposals could have on systemic risk events in future. RPTCL highlighted three key concerns in its response to the DWP (full response available here):

- **Scheme closures due to higher costs** – contrary to previous assurances in the Houses of Parliament[1], the draft regulations could lead to significantly higher costs that risk forcing the closure of many of the UK's remaining open DB schemes, thereby substantially reducing the retirement incomes of many people across the UK, and placing these schemes on a path of de-risking.

- **Increase in systemic risk** – the draft regulations are more prescriptive than the existing funding regime, which we believe could exacerbate systemic risks to the UK economy due to the effects of pension scheme "herding". For example, the draft regulations set out a narrow definition of the requirements for "low dependency" (more details of which can be found in our full response), which may lead to all schemes following similar funding and investment strategies that rely more heavily on gilts and a properly functioning gilt-market. Whilst LDI with a controlled and low level of leverage can be an effective risk-management tool for some schemes, the use of synthetic assets with excessive leverage is likely to make the impact of "herding" worse.

- **Difficulties supporting Government's growth agenda** – we are concerned that the impact of the draft regulations could be contrary to the Government's growth agenda, as they will make it more difficult for schemes to increase (or even maintain) current levels of investment in long-term productive UK assets and to support the UK's transition to net zero.

Pensions consultancies Lane Clark & Peacock (LCP)[2] and WTW[3] have both raised similar concerns about the draft regulations. We agree with the concerns raised.

It is our understanding that the DWP has decided not to carry out an impact assessment of key aspects of its proposals, pending the publication of TPR's second consultation on its revised DB Code of Practice. We suggest the WPSC may wish to encourage the DWP to conduct a thorough assessment of the above key issues.

Furthermore, recent market turbulence makes this a particularly unsuitable time for substantive changes to DB funding and investment regulations to be made. Pension schemes, their members and their employers benefit from a stable regulatory regime, allowing them to make long-term decisions which are in the best interests of members. We therefore strongly suggest that it would be beneficial for the DWP, together with the WPSC, to take more time to fully consider the proposed changes, in light of recent events in the pensions industry.

I hope these comments are helpful as part of your important inquiry. If you have any follow up questions, please contact Martin Hunter, Head of Funding Analysis at Railpen (Martin.Hunter@railpen.com) in the first instance.

November 2022

---

[1] Source: https://hansard.parliament.uk/commons/2020-11-16/debates/298AA028-D49E-4F07-A001-C483ADF38659/PensionSchemesBill(Lords)
[2] https://www.lcp.uk.com/media-centre/2022/10/new-pension-funding-rules-could-thwart-chancellor-s-pro-growth-agenda/
[3] https://www.wtwco.com/en-GB/News/2022/10/pension-funding-rules-should-be-sent-back-to-the-drawing-board