



**OFGEM CONSULTATION:  
PRICE CONTROL PENSION  
PRINCIPLES  
THIRD CONSULTATION DOCUMENT**

**- GMB Response -**

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**GMB  
22-24 Worple Road  
London  
SW19 4DD**

**General Secretary: Paul Kenny**

For further information  
please contact:

**Naomi Cooke  
National Pensions Officer  
020 8971 6967**

# **OFGEM CONSULTATION: PRICE CONTROL PENSION PRINCIPLES THIRD CONSULTATION DOCUMENT**

GMB, with over 611,000 members, is the UK's third largest trade union and the leading union for employees in the energy sector. GMB has thousands of members throughout the industry covering all the pension schemes referred to in this latest OFGEM consultation. Our members, the vast majority of whom are members of the industry's occupational pension schemes, perform a vital role in providing electricity and gas services to the public. Our members are integral to the sustainable future of the UK energy market and have been central to many key reforms that have improved the efficiency and quality of the sector. Many have decades of service within the industry and have skills and commitment unparalleled in Europe. They have also followed successive governments' advice and saved for their retirements through occupational pension schemes. A loyal and motivated workforce is essential if the UK is to meet the energy challenges of the twenty-first century. GMB is keen to engage in this endeavour but will not accept attempts to arbitrarily reduce energy workers' core terms and conditions.

GMB is submitting this formal response to OFGEM's latest consultation despite little if any evidence that the consultation process the industry regulator has undertaken has had any impact on its thinking whatsoever. When the vast majority of consultation responses, seminar views and other representations express one view: that the current framework works reasonably and proportionately, the fact that OFGEM chooses to accept the unsupported view of a small minority of stakeholders and determine that the system needs to change, completely undermines the credibility of the consultation and the regulator. OFGEM's consultation timescales throughout this process have been overly short, this third consultation is worse still, allowing less than a month for respondents to reply. Once again this leads to a direct impression that OFGEM regards consultation and the responses it receives as a procedural rather than a substantive element of their policy formation process.

OFGEM is referred to GMB's previous responses for discussion of the current arrangements and the dangers of interference by an industry regulator in the management of occupational pensions. In this, third

formal response, focus will be on the main 'minded to' positions OFGEM has adopted:

- Benchmarking total employment costs going forward
- Extending the notional period of deficit funding to 15 years
- Introducing a new 'economic and efficient' test for pension costs

Contrary to the insinuation made by OFGEM, GMB and other unions are not steadfastly opposed to any change in occupational pensions. Many of the changes to other schemes highlighted in this consultation were done through negotiation with trade unions. Nor, it should be pointed out in light of the statements made by OFGEM at the third seminar on 9<sup>th</sup> November, do we regard the current approach as one of 'automatic pass-through' of pension cost to the consumer. GMB supports the efficient operation of pension schemes but believes the Pension Regulator (tPR) is the appropriate judge of this, not OFGEM. Our opposition to OFGEM's proposals which remains as true at this stage of the consultation as it was at the start, is that it is not appropriate for OFGEM to interfere with occupational pension schemes. Not only is it not appropriate, it is potentially very dangerous: to the schemes themselves, to the Pension Protection Fund, to the Pension Regulator's position, to the scheme trustees and to the scheme members. GMB has always engaged with employers who wish to change their pension provision as the sustainability of pensions is a key priority for the union. We cannot however, support the heavy-handed involvement of an industry regulator in this process, in particular one whose interests are so narrowly focused and short-sighted.

GMB maintains that responsibility for managing occupational pension schemes effectively and efficiently lies with the trustees and the Pension Regulator. As OFGEM has provided no evidence to support its assertion to be the appropriate judge and jury on 'efficiency' we repeat our view that OFGEM should stop threatening the retirement security of pension savers in the distribution sectors and focus on real issues that force up costs for the consumer without any justification.

### **Benchmarking Total Employment Costs**

As with many of the ideas sketched out by OFGEM in this consultation, its plan to benchmark ongoing pension and employment costs lack sufficient detail to assess the full extent of the impact of this proposal. There does seem to be a danger that OFGEM will be benchmarking costs that are not within the gift of companies to change. A much greater concern

however, is that where employee terms and conditions (including pensions) are in question, the regulator seems to wish to circumvent the negotiation between employer and unions/employees on these issues and impose its own maximum provision. In the absence of national bargaining with OFGEM in place of the multiplicity of employers in the sector, GMB does not view this suggestion as either helpful or workable.

### **Extending the Notional Deficit Funding Period**

The arbitrary setting of a 15 year notional deficit funding period by an industry regulator is an intrusion into pension scheme regulation that is not without risk. GMB does not doubt that some employers affected by this will welcome this move as it enables them to defer cost. Whether it is in the long term interest of the scheme, its members, the Pension Protection Fund and the public is another matter.

GMB is very concerned that the apparent collusion of the Pension Regulator in this proposal conflicts with its duties to ensure schemes are properly supported and funded. The interference of the industry regulator in the decision making process of the scheme sponsors reflected in pressure on the trustees, despite OFGEM's lip service to 'non interference or influence', is inevitable. The intermittent repetition by OFGEM that it has no intention of exerting untoward influence over the trustees is completely subverted by the other statements of intention in the consultation.

Setting a 15 year notional deficit recovery period cannot but influence and affect trustees' decisions. It is exactly this form of interference that GMB believes OFGEM should avoid.

### **PPF7800 Comparison Test**

Further unwarranted interference comes from OFGEM's notion of a comparison test with the PPF7800 index. In 1.17 OFGEM state that "If the companies [sic] deficits were higher than that indicated by the index it would be for the network company concerned to demonstrate that it had managed its pension fund effectively and efficiently on behalf of consumers." It is quite clear from tPR guidance, pension legislation and trust law that scheme trustees set the investment strategy and have to do so in an appropriate manner. Seeking to demand from the employers that the trustees have lived up to OFGEM's standards of efficiency is absurd double regulation. Presumably OFGEM intend to issue guidance

on what they will deem efficient or otherwise, GMB would be interested to know if OFGEM intend to reflect the existing regime of guidance and regulation in this area or intend to produce their own conflicting material.

Presuming the intention of OFGEM is to influence investment practice - otherwise it is hard to see why it should make assessing fund management performance a priority - an appreciation of the purpose of trustee autonomy is essential. Unlike OFGEM, trustees have a legal responsibility to act in the best interests of the scheme. It follows therefore that their motivation in determining investment policies will also differ. If they did not it is to be assumed that OFGEM would have no desire to intervene in the process. Trustees are obliged to take advice and make reasoned and appropriate decisions about the investment strategy appropriate to their scheme. This is not the same as slavishly following others as OFGEM seems to suggest is the ideal by proposing this arbitrary test. In fact in many, if not all, cases it would be utterly inappropriate for a scheme to follow the average investment strategy of the PPF index and to do so would bring into question whether the trustees were appropriately exercising their duties.

It may be that OFGEM's implicit intention is for schemes to reduce their benefits to the level of those provided by the PPF in order to make its trigger approach reasonable. If so, it is disingenuous of the industry regulator not to have said so. If this is not the case then it is perplexing that the PPF7800 index is used at all. The only apparent reason for using this index is that it is readily available, hardly a considered rationale but in the absence of any logical explanation it is difficult to draw other conclusions.

If, as stated in the seminar on 9<sup>th</sup> November, part of OFGEM's motivation for using this index is to give certainty then the use of any index requires a lot more discussion and guidance than the regulator appears to intend prior to coming to a decision. All information available to us indicates that the use of this index in this way would lead all schemes to be called to account unless OFGEM has the impact it claims not to want and influences trustees to match the PPF index's strategy. This means that the only certainty is that every scheme sponsor would be called upon to justify the action of their scheme's trustees. Certainty would require OFGEM to outline how it planned to evaluate the companies' justification. There is absolutely nothing in either the consultation document or expressed in the November seminar that could be seen as a transparent explanation of this point.

In line with points elsewhere in this response about the cost of OFGEM's proposals, GMB is also unclear what obligation OFGEM believes there is on schemes and specifically trustees to justify their actions. Assuming tPR has no issue with the efficient running of a scheme why would the scheme incur cost helping an employer demonstrate that the trustees had not breached the industry regulator's unseen efficiency criteria. In the absence of trustee cooperation, how is the company going to be in a position to defend its action, irrespective of the fact that it does not know of what, exactly, it is accused.

## **Conclusion**

GMB does not believe OFGEM has a legitimate case for interfering in the management of occupational pension schemes. No evidence is provided to justify such interference apart simply from a desire to do so. OFGEM's 'minded to' proposals fly in the face of the existing functional regulatory framework and despite hollow protestations from the industry regulator, seek to undermine scheme trustees and the Pension Regulator simply on the basis of a desire to do so. No savings have been identified for the consumer, although GMB understands OFGEM has decided that increasing the cost burden (through extending the deficit recovery period) on future consumers to the benefit of current consumers is consistent with its obligations. If anything these proposals would drive up scheme costs as employers and schemes attempt to jump through the spurious hoops set by OFGEM. We therefore again call on OFGEM to rethink its intentions and focus on the real issues facing the energy sector and energy consumers.