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Ms Eliza Twaddell
Regulatory Finance and Governance
Ofgem
9 Millbank
London SW1P 3GE

13 July 2015

Dear Eliza

**Consultation on Ofgem's policy for funding Network Operators' pension deficits**

I am pleased to attach our response to the specific questions contained in the above consultation.

We recognise our important role in stewardship of pension schemes and that consumers ultimately bear significant costs of these schemes. We manage our schemes in a robust way, within the constraints of our duties and in general believe:

- It is timely to review Ofgem's pension principles. The artificial constraints of the 2025 end point and the asymmetrical treatment of costs and the benefits of actions has resulted in us being unable to make changes that we believe would have been beneficial to consumers.
- We welcome Ofgem's clarification of its commitment to fund established deficits and provide for a longer term and more flexible basis for this funding, coupled with the move away from the historic benchmarking of assumptions.
- We are pleased that Ofgem recognises the independent duties of trustees and that pension schemes are regulated by the Pension Regulator (tPR). Collaborative working between Ofgem and tPR will be essential to ensuring that these changes can work.
- It's particularly important to recognise that NWOs will make decisions in this arena based on a balanced view of risks and opportunities – Ofgem needs to take care not to create a mechanism that will only be viewed with the benefit of twenty twenty hindsight.

However we would like to take this opportunity to highlight our concern that any consumers or consumer bodies reading the consultation may be left with the impression that we have taken no action to manage our pension scheme. We believe that we have taken many steps to better manage costs and risks already – steps which we hope Ofgem will consider when it conducts the next reasonableness review. In particular:

- We closed to new joiners early in 2006 – this means that additional salary linked pension accrual and the funding risk associated with it was capped off nearly 10 years ago.
- We also introduced salary sacrifice in 2006, reducing the cash funding costs ever since.
- In 2010 we negotiated the deficit down from £191m to £145m.
- We put in place a comprehensive de-risking flightplan in 2012 using asset outperformance to pay for the de-risking. This has optimised the balance between cost and risk and now held our deficit at a rate considerably below our 2013 deficit.

- In 2013 we negotiated the deficit down from around £212m to £188m. We also put in place an innovative recovery plan that back loaded cash contributions to after the next valuation in 2016, anticipating that our deficit would fall below the £188m.
- We also negotiated hard on the actuarial assumptions in 2013, such as on pension and salary increases to lower our deficit.
- We considered an alternative inflation hedging mechanism in 2012 which would have directly benefitted consumers, but were unable to agree a true up mechanism with you.
- We have also considered liability management exercises a number of times and again recently. Clearly we are constrained by protection legislation and do have concerns that the bulk of our members would not wish to convert or transfer out any of their benefits and therefore those that would, for example single people or those with an impaired life, would actually worsen our funding position.

The above steps directly benefit consumers by lowering the cash funding and volatility risks.

We look forward to meeting with you to discuss our strategy for pensions in the near future.

Yours sincerely

Fiona Brown

**Fiona Brown**
**Head of Pensions & Reward**