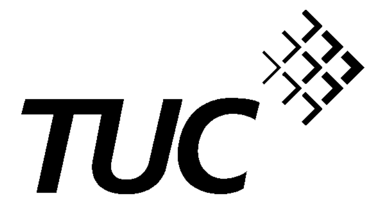

Thornton Review of Pensions Institutions

TUC response to Emerging Issues Consultation Paper

March 2007

Introduction

1.1 The TUC welcomes the opportunity to submit a response to the consultation paper on emerging issues published by Paul Thornton as part of his Review of Pensions Institutions.

1.2 As Britain's national trade union centre, the TUC represents 6.5 million working people through its 64 affiliated trade unions but touches the lives of many more. The TUC is Britain's largest voluntary organisation. As well as working to raise the quality of working life, one of our main objectives is to promote social justice. This includes a direct interest in pensions policy in the round, where our priorities have been:

- to see today's poorest pensioners lifted out of poverty with a level income reflecting their contribution to society;
- ensuring today's workers are supported in saving for their pensions through compulsory employer contributions to good quality occupational schemes;
- indexing of the basic state pension to earnings;
- achieving recognition in the state system of the contribution made to society by women and carers with interrupted employment patterns.

1.3 While we appreciate the desire for this review to come to speedy conclusions, the short period allowed for consultation on this paper has not allowed us to consult widely among our affiliates or prepare a full answer to all the points set out in the consultation paper. This is therefore a somewhat abbreviated response.

1.4 Although the general thrust of our response is that major changes are neither necessary nor desirable, we recognise that it makes sense to review the regulatory and institutional framework that govern UK pensions. There have been major changes in the way that pensions are regulated and pension scheme members protected in recent years. The new pensions settlement flowing from the work of Lord Turner's Pensions Commission will introduce further radical changes in our pensions architecture. As the institutional infrastructure has grown on a piecemeal and ad hoc basis, often in response to the failures of the pre-existing framework, it is right to ask whether it is possible to rationalise the current system and/or whether the current boundaries between the different institutions and regulators should be altered.

1.5 While the TUC is opposed to unnecessary or overly bureaucratic regulation, pensions still need a tough and effective regulatory regime. Losing one's pension or being sold an inappropriate pension that fails to deliver a suitable income in retirement will be a catastrophic event for anyone. Nor have problems or abuse been confined to marginal companies or obvious high-risk groups. Employees of household names have found their pensions schemes to be worthless overnight. Long established blue chip companies have been found guilty not just of mis-selling pensions but other financial products such as endowment mortgages.

1.6 Employers that decide to close good pension schemes, either completely or to new entrants, will always try and blame others. Government and regulators, red

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tape and over-regulation will all inevitably feature in the list of scapegoats. But employers close schemes or reduce their generosity when they calculate that the money saved is greater than the disruption, reduced staff morale and recruitment and retention costs. It is not red tape to have rules that require defined benefit schemes to have sufficient funds to meet their pensions promises.

1.7 It would therefore send the wrong message both to those who look for regulation to protect their pensions and the regulated to cast this review as 'deregulatory'. Pensions and the financial services industry have shown time and time again that they need strong regulation, and that any laxness in the regulatory regime will be exploited and almost certainly create identifiable victims, who will expect redress.

1.8 We group our responses under the three main questions used to organise the emerging issues paper.

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Is there a good case for bringing the Pensions Regulator (TPR) and Pensions Protection Fund (PPF) closer together?

2.1 While of course there should continue to be good relations between these two organisations, we are strongly opposed to any proposal to merge them. We see little or no advantage from any merger, but strong disadvantages and potential conflicts of interest from bringing their roles together in a new body.

2.2 As the consultation paper notes, both these bodies were created by the 2004 Pensions Act (although TPR can be seen as a continuation of OPRA as the regulator of occupational pensions). The PPF however is an entirely new body with an entirely new compensatory function within the UK pensions system. While the TUC had pressed for the creation of a similar central discontinuance fund during the course of the 1995 Pensions Act, these arguments were rejected at the time.

2.3 The consultation paper is right to say that both bodies have made a "quick and effective start" (para 22). This is a particular tribute to the PPF whose establishment was more controversial, and which has the inherently unpopular task of raising a significant levy each year. Any disruption to the current organisational set-up runs the risk of disrupting the good track record both organisations have established since they were created two years ago.

2.4 While the decisions of one body will have an impact on the other, this is not the same as an overlap of function. Each has distinct and different responsibilities. TPR regulates pensions, while the PPF pays out pensions to members of failed schemes. Indeed the 2004 Act recognised this by forbidding any overlap by the board members of either organisation with the activities of the other. In practice the activities they carry out are also different. Most PPF work is concerned with management and distribution of money, while TPR is primarily a regulatory body. As there is this clear difference in function it is hard to see that there are many savings to be had from a merger. The consultation paper only manages to list IT, HR, finance and media relations as potential cost savings from a merger. As these are functions carried by almost all organisations, this is hardly a compelling case for merger of these two bodies.

2.5 There are clearly areas where the two bodies need to share information and co-ordinate strategy. If there was any evidence that the current structures were preventing this, it might provide an argument for change. But as the paper concedes, the organisations work well together as shown by the joint production of the Purple Book.

2.6 The recognition that the decisions of one body can have an impact on the other is suggested as an argument for merger, but it could also be taken as pointing to an inherent conflict of interest. Decisions about the future of the PPF, such as the size of the levy, should be based on the projected requirements to pay out pensions to members of failed schemes. Those responsible for regulating funds – and in particular – solvency requirements may have an interest in keeping the levy down. This is a straightforward conflict of interest.

2.7 Keeping these two functions separate builds a useful check and balance mechanism into the current system. Currently when the PPF sets its levy, as part of this process it has to make an independent assessment of how effectively TPR is managing risk. If it believes the risk of schemes failing has risen, then it will set a higher levy. In a merged organisation there would be no independent assessment of current risk, and there could be pressure on those setting the levy to keep it low to justify the current regulation of risk.

2.8 Combining the different functions of the two bodies could cause further similar conflict of interest problems. The PPF actively participates in capital markets. The funds under its control are invested in a range of different types of fund. TPF is a regulator, and it is therefore inappropriate for it also to be an investor. A merged organisation would be both a player and a referee.

2.9 The PPF's own submission lists further potential conflict of interest issues.

2.10 In our limited research we have not found any other country that combines the compensation and regulation regimes.

2.11 These all add up to a set of compelling reasons for keeping the two organisations separate, while continuing to encourage co-operative working.

Is there a good case for bringing the Financial Services Authority (FSA) and the Pensions Regulator (TPR) closer together?

3.1 While there are not the same compelling conflicts of interest that should preclude a merger between the PPF and the TPR in a merger of the FSA and TPR we are also opposed to such a move. We think the two organisations already have clearly defined roles, and although both are regulators, they operate in different environments with different stakeholders.

3.2 In particular we see a close connection between the Pensions Regulator and the world of work. It needs to win the trust and co-operation of both employers and trade unions, making it to a large extent a social partnership organisation. This close relationship has helped build up trust in the new Pensions Regulator. This could easily be lost if its work was absorbed into the much bigger FSA.

3.3 We are not aware of any difficulties caused by having separate organisations to unions or our members. The nature of employer backed occupational pensions differs in important respects from capital backed products provided by insurance companies, and the nature of the regulatory process is therefore different.

3.4 Neither organisation appears to have difficulties with the current arrangements and both are opposed to merger.

3.5 This does not mean that there will not be the occasional confusion in roles with either an overlap, or more worryingly, a gap in regulation becoming apparent. The growth of DC pension schemes in the workplace inevitably means that there will be more of a role for the FSA in pensions. But we see these as reasons for keeping current arrangements under periodic review and encouraging close working, not as an argument for merger between two organisations that do not want to join together.

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Is there a case for bringing the Pensions Ombudsman (PO) and the Financial Ombudsman Service (FOS) closer together?

4.1 While the responsibilities of the FOS go wider than the functions of the FSA, the PO's responsibilities closely mirror those of the Pensions Regulator. If the review concludes that the FSA and TPR should remain as separate organisations, then it makes sense to keep separate ombudsman functions.

4.2 There do not seem to be any great difficulties caused by the current arrangements. Given how few people will ever need to use an ombudsman, it would be unrealistic to expect consumers and employees to have a clear understanding of the boundaries, but as long as the two organisations co-operate in referring cases and advice agencies understand the difference, this is not a problem.

4.3 One issue that should be resolved by the review is the current jurisdictional black hole between the Pensions Ombudsman and the Financial Ombudsman in relation to complaints about advice on transfers within and between occupational schemes. The FOS will not adjudicate on complaints against non-FSA regulated firms, and the PO cannot deal with them because they concern advice rather than management. As the FOS has expertise in dealing with advice, it would seem to be make sense to extend the FOS's role in this area.

4.4 While there are no great issues of principle involved in merging the PO and FOS, we see no compelling arguments for merger - and practical arguments against. But the review does provide a golden opportunity to ensure an ombudsman service covers disputes about advice on transfers.