

Consultation Response: “British Steel Pension Scheme”

To: Department for Work and Pensions (DWP)

By: The Intergenerational Foundation

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The Intergenerational Foundation (www.if.org.uk) is an independent think tank researching fairness between generations. IF believes policy should be fair to all – the old, the young and those to come.

Introduction:

The Intergenerational Foundation (IF) is glad to have the opportunity to comment on government policy towards the British Steel Pension Scheme (BSPS). We believe that the current problems with the BSPS raise much broader questions about the sustainability of occupational pension schemes as a whole, which IF is deeply concerned about because of the intergenerational nature of pension promises. The points we would like to make in response to the consultation are outlined below:

1. Unaffordable pension promises are harming the UK economy

The issues raised by the BSPS consultation have significant overlap with the themes of a recent IF research paper, [DB Pensions: Choking Hazard](#). This paper argued that final salary occupational pension schemes are proving ruinously expensive for the UK's private sector firms because of rapidly rising life expectancy and low returns on investment. Its author calculated that the UK private sector as a whole is currently having to pay £35 billion per year in meeting the deficits of its final salary pension schemes, money which he argued these firms could instead be using to increase their investment in research and development (R&D) and/or pay their current staff higher salaries. The report also argued that this situation is intergenerationally unfair because virtually all of these companies have now ceased offering defined benefit (DB) pension schemes to their current workers, who are left with far less generous defined contribution (DC) pensions instead (the typical worker in a DB pension scheme receives employer contributions which are worth 15.8% of salary, compared to just 2.9% for his counterpart in a DC pension scheme, [according to the ONS](#)).

[As Frank Field MP said recently](#) when he announced the new Department for Work and Pensions Select Committee inquiry into pension law, there are thought to be around 5,000 private sector occupational pension schemes currently in deficit, which altogether have a combined shortfall of at least £805 billion. In IF's view, the key problem affecting most of these pension schemes – including the BHS pension scheme and the BSPs - is essentially that workers were made promises about the level of pension they could expect to receive in the past which have turned out to be over-optimistic. As Lord Turner, the former

chairman of the government's Pensions Commission, [said in 2007](#), in hindsight DB pensions were "a house of cards that was always going to fall."

2. Intergenerational fairness is key

If the problem affecting the BSPS is essentially that there are insufficient funds remaining in the pot to honour everyone's pension promises in full, then IF's key message is that the solutions have got to be intergenerationally fair to all workers. This is especially important given that so many occupational pension schemes currently have deficits, and that the incredibly rapid pace of technological and economic change in the modern economy means more sponsoring employers are likely to run into distress over the coming years, as it seems likely that whatever happens to the BSPS could form an important precedent which informs how similar situations will be handled in future.

Achieving an intergenerationally fair solution requires a) not burdening younger workers or taxpayers with supporting the scheme, and b) not unreasonably discriminating in favour of existing pensioners over active or deferred scheme members who are yet to begin drawing their pensions. There is also a related practical consideration, which is that given that less than 11% of BSPS members are currently still active workers, achieving any serious cost savings against the scheme's current liabilities will almost certainly involve reducing the benefits of retired and deferred members. Therefore, IF agrees with the government's position that for the scheme to enter the PPF would be undesirable, as it would result in existing pensioners receiving 100% of their expected benefits while active and deferred members would only get 90%, and it would mean that the scheme was ultimately being supported by the active members of other occupational schemes through the PPF levy.

3. IF supports Option 3

This analysis of the situation has led IF to support Option 3 from the BSPS consultation document – we believe there needs to be legislative changes which would permit the scheme to reduce its future liabilities through less generous indexation and revaluation arrangements. Indeed, one of the policy recommendations from the recent IF research paper referred to above was that all DB schemes should be allowed to switch from RPI to CPI indexation without requiring the consent of their members, as this may be the only way of maintaining the viability of many distressed schemes and means that the burden of adjusting benefits to more affordable levels is being shared by both current and future pensioners.

However, we disagree with the consultation document where it argues that such a solution should be restricted only to the special case of the BSPS – we think that, as long as the safeguards outlined in the consultation document are implemented (such as requiring the support of the Pensions Regulator before such a change could go ahead), this intergenerationally fair method of adjusting the benefits of DB pension schemes to more affordable levels should serve as a model for other distressed schemes as well.

Conclusion

If you would like to learn more about the work of the Intergenerational Foundation or would like to organise a meeting to discuss the points we raise further, please contact:

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