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Louise Robinson
The Pensions Regulator
Napier House
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Dear Ms Robinson

Funding of defined benefits

I am writing on behalf of the Hundred Group of Finance Directors in response to your invitation to comment on your consultation document. The Hundred Group represents the Finance Directors of the UK's largest companies and we have worked closely with OPRA in the past on various issues.

We are broadly supportive of your initial proposals and recognise the work that has gone into producing the consultation document. We acknowledge that many UK pension schemes are underfunded and that corrective action is desirable. As such, where financial and commercial circumstances permit, it is undoubtedly right that companies seek to repair deficits over an appropriate period - in many cases shorter than before. We do however have some reservations about your proposals which we set out below. As such, we would welcome the opportunity to work with you in the coming year to refine your proposals in the light of emerging experience.

Statutory funding target

We agree that a filter mechanism (with use of trigger points) is an appropriate method of identifying schemes most at risk. For many schemes a funding target that is close to that produced by accounting standard setters is likely to be desirable although we recognise that accounting standards themselves are subject to modification from time to time and pension standards are no exception. We do however have concerns that your trigger points are expressed as a percentage of buy-out costs. The buy-out market is a very limited, and somewhat opaque, market. If trustees focus unduly on the drivers of buy-out cost, undesirable consequences, potentially difficult to predict, may emerge.

Last week, we experienced unprecedented volatility in the index-linked gilt market. The potential squeeze on corporate cashflows that may result from your proposals should not be underestimated. If, at the same time, trustees decide to move away from equities to bonds, in order to de-risk, the combined effect could be very severe with trustees being given in effect a perverse reason to sell at the bottom. There is clearly a delicate balance between short term solvency and long term sustainability.

Security

While we support the government's intention to make pension obligations more secure, we believe that more flexibility should be introduced into the regulatory system where alternative sources of security are available. This is a matter we believe needs further consideration and we would be pleased to work with you in developing alternative approaches which provide the flexibility needed to ensure the existence of successful businesses (particular small and private businesses) is not threatened by a rigid "one size fits all" approach.

Deficit repair period

In practice, we consider your attitude to the deficit repair period to be the key issue. You have indicated that companies able to afford increased contributions should seek to fund their deficits more quickly than over ten years. The attitude of the Hundred Group is particularly important because many of our members, despite large pension deficits, are sufficiently strong to be able to fund their deficits over relatively short periods - indeed a number of us have chosen to make substantial one-off contributions over the past year or so. However we do not operate in a vacuum and if measures are introduced which adversely affect smaller companies then we could well be affected as well.

Many companies within the Hundred Group are sympathetic to shorter funding periods but have practical concerns about the consequences. I mention just two briefly:

- 1 If market conditions improve and surpluses emerge, it will be very difficult for companies to get full value for the contributions that have been made. In view of the widespread closure of DB pension schemes, the position will become exacerbated over time as these schemes become less relevant for current employees (generating shareholder value) compared with former employees (no longer generating such value). The current asymmetry of risk for companies is not helpful for longer term pension security and we believe changes need to be made in the medium term.
- 2 The current restrictions on tax deductibility and immediate relief are not helpful for us when considering accelerated funding plans. Whilst we realise that tax issues are not within your jurisdiction, it would be helpful if companies were able to obtain tax relief in full when they are simply funding in accordance with your expectations and we would suggest that it might help if you were able to make representations to the Treasury to this effect.

Competitiveness of UK industry

Whilst the diversion of additional funds into underfunded UK pension schemes is clearly desirable from the perspective of members and pensioners, the money that therefore becomes unavailable for investment in UK businesses will have ramifications for members of the Hundred Group, and more widely for other companies generating wealth for the country. As The Economist said this week in analysing stagnation in levels of productivity in the UK, "firms are having to tackle big pension-fund deficits, leaving less money available to invest in plant and equipment." Perhaps more importantly, it may reduce investment in innovation and research and development. Striking the right balance is never easy. We suggest a close working relationship between our respective bodies can help to ensure the early lessons are learned and emerging risks are anticipated.

In conclusion, we are able to give broad support to your proposals. It is an initial step that addresses the current risks within the system. We do, however, expect new risks to emerge. We urge you to work closely with interested parties to ensure such risks are speedily identified and acted upon. As you may know the Regulator and Chairman of the PPF participated in a most useful meeting with a large number of our members last year and we are happy to commit to a constructive dialogue with you in these early stages of the new funding regime.

Yours sincerely

Philip Brodley
Chairman of the Hundred Group