TfL Pension Fund

Pensions Review, Stage 1 Call for Evidence, August 2021

Joint Trade Union Response from the Staff Side of the Pensions Working Group

1. How should long term sustainability be viewed and how does this look from the perspectives of members; the employer; taxpayers; farepayers; the Trustee and others? What are the key features of long-term sustainability for the pension arrangements of TfL?

Pension schemes like TfL's are a long-term pooling of risks in the interests of all stakeholders and their sustainability must be measured over the long-term. As illustrated in the Call for Evidence consultation paper, over the years, the TfL Pension Fund has reacted to various events in the very same way as other Defined Benefit (DB) Pension Schemes. The events we allude to are changes in legislation, poor investment performance and improvements in mortality, to name just a few. However, while we acknowledge that these events have had at times impacted negatively on the TfL Pension Fund, its strong governance has meant that these challenges have been dealt with effectively. It is of the utmost importance to the TfL scheme, as will all schemes, that decisions are made on the basis of evidence and with the long-term sustainability of the scheme in mind and are not governed by short term and politically motivated decisions.

There is no case for this review. The Independent Review into the TfL pension arrangements is in our view not only badly timed but clearly politically motivated. We would ask why anyone would seek to review the TfL Pension Fund at a time when it's almost fully funded, and perhaps more importantly while the Trustee Board are carrying out a full Triennial Actuarial Valuation. The timescale for the Review is established in order to drive the Review to conclusions before vital evidence is available and at the whim of the government, without any internal rationale. In our experience the tried and tested method in dealing with similar pension arrangements is when the results of a triennial valuation reveal a deficit which needs to be addressed. Setting up a review panel is not only unnecessary it is also a waste of TfL's time and resources which would be better focused on ensuring and safe and sustainable increase in passenger numbers back onto the network. It also causes wholly unnecessary anxiety to employees who have risked their lives through the pandemic. Too many have died giving this service.

Neither is it legitimate to judge the long-term sustainability of the TfL pension scheme through quick and facile comparisons with other schemes. Comparisons to Network Rail and Local Government pension schemes, for example, are totally inappropriate. Each scheme has been established on the basis of different historic labour markets and reward packages, different mixes of public and private employment, different funding levels and assets and with differing precision, variations in the role of the state and the taxpayer. The taxes of our members, for example, contribute toward the pensions of government ministers. Each scheme needs to be judged on its own merits and not through a politically motivated imperative to drive a race to the bottom aimed at making our members poorer in retirement.

The TfL pension scheme has a well-established governance structure along with a very focused investment strategy based on the principle of diversification which is very well-equipped to manage the scheme in the interests of its long-term sustainability.

2. How should long term affordability be viewed, and how does this look from the perspective of members, the employer; taxpayers, farepayers, the Trustee and others? What are the key features of long-term affordability for the pension arrangements of TfL?

The sustainability of the TfL Pension Fund should be viewed in line with the scheme's liabilities and assets on a long-term basis considering the characteristics and obligations placed on the fund in providing benefits in retirement for all beneficiaries.

These characteristics and obligations are ingrained into three fundamental principles we believe are unremovable:

1. The pension fund must remain open. We believe that if the TfL Pension Fund is closed to new entrants this will create a spiral of decline in the scheme. The experience of closing schemes to new entrants over the last 20 years is that it reduces the investment horizon, refocuses schemes on cash and bonds with lower returns, and produces more pressure to raise contributions and cut benefits. Closing the scheme to new entrants must be avoided to escape such a spiral. Current benefits must be retained for current and new members.
2. Current contributing members have an expectation of a certain level of benefit not only for past service benefits but also for future accrual. These promises should be honoured in full. We do not accept that change is necessary for the sake of change and our members expect and deserve a certain level of benefit in retirement. Cutting benefits for future members will build inequity and instability into the scheme. Future members of the TfL Pension Fund should have the same expectations as existing members.
3. All pension schemes should be affordable and fit for purpose. We do not accept bald statements that the TfL Pension Fund is somehow outdated and must be modernised. This is, in our view, nothing more than political propaganda which aims to divide workers by using the narrative that DB final salary pension schemes are 'gold plated', unaffordable and must be closed.

From a member perspective, having new members contributing to the fund on a continuous ongoing basis is we believe is the most important element of long-term sustainability when combined with an effective diversified investment strategy that takes fully into account fluctuating investment markets. While it can be argued that using such investment strategies, such as Liability Driven Investment, can stifle investment growth, it is clear that over the last 18 months the TfL Pension Fund, like many similar DB schemes, has seen funding levels grow and not reduce which is primarily due to the protection provided by way of diversification as a cornerstone premise of the TfL Pension Funds Investment strategy.

3. What do you consider to be the key risks and challenges in the short-, medium- and long-term in relation to the Scheme (for example, investment risk, salary risk, longevity risk) and how could these risks and challenges be mitigated?

All pension schemes pool risk and while we recognise the risks associated with DB pension schemes in general, we do not accept that they cannot be managed or indeed mitigated on a long-term basis. The challenges faced by the TfL Pension Fund are nothing new and the existing governance structures are entirely fit for purpose in managing those challenges. especially in the pursuance of its investment strategy. This investment strategy has been a great success story for the Fund since first embarked upon in 2009 following the global financial crisis.

The key risk we face now is that the TfL scheme is being reviewed as part of a reckless, opportunistic, politically motivated attack on workers who have put their lives on the line throughout the pandemic. Political pressure is being applied to remodel a scheme and potentially undermine the strength of the Employer Covenant without any inherent justification arising from the scheme itself. Pressure is being applied to find a 'solution' to a non-existent problem in order to cut our members' deferred pay. This is not only morally reprehensible, it is, pragmatically, a highly dangerous way in which to make policy regarding a substantial pension scheme.

However, while we do not accept the rationale of the review, we would like to comment on possible key risks mentioned.

The risks mentioned are of course a concern for all DB pension schemes but if there is good Trustee governance and strong employer covenant, when it comes to managing these risks over the long-term horizon these challenges can be mitigated.

This is exemplified by the crises which resulted from the Covid-19 pandemic which saw the leading index of both global and UK company shares plummet by 30% in the three months up to the end of March 2020, the largest quarterly fall in UK equities since Black Monday in October 1987. However, while we saw, for example, the FTSE 100 fall by almost 2,000 points, from 7,542 to 5,672 points, as we have experienced with other financial crisis the markets have since rallied and these leading stocks, in the FTSE 1OO as an example, are now valued by 7000 points.

While the above clearly was of some concern, as noted above DB pension schemes do not invest in the short-term but set their horizons much further out. Of course, in the short-term pension schemes will want to have liquid investments to react to such events and of course pay benefits. The TfL Pension Fund has diversified its investment portfolio to take into account the many different types of scenarios as well as taking advantage of the falls in different markets as mentioned above.

The good governance we mention above is in respect of the skill of investment advisors appointed by the Trustee and while you cannot always rely on this expertise due to certain events the TfL Pension Fund has and hedge its investments. to offset the risk of any adverse price movements or falls in markets. It is not by chance that the fund now finds itself almost fully funded based on the most recent valuation forecast despite financial market volatility and the turmoil experienced at the beginning of the pandemic.

It needs to be pointed out that the fact the Government has only offered a short-term funding agreement with TFL will consequentially negatively impact on the fund's investment strategy. This will result in the Trustees having to take a less aggressive or de-risking of investment approach due to the weakening of the sponsoring Employers Covenant. Therefore, the failure of the Government to agree a long-term funding agreement with TfL will therefore adversely affect potentially the current and continuous ongoing growth in investment returns and therefore damaging the fund in itself.

In respect of wage inflation and longevity, we also see these as being mitigated by the structure the existing, and still growing, investment portfolio and continued contributions being made into the fund. Experience taught us that most DB pension schemes now mitigate the pressure of an ageing population by matching their investments to the membership profile of the scheme. Investment concepts such as Liability Driven Investment are now used to manage the liabilities being built up by both active and pensioner members. While you can't always put faith in all these investment techniques all of the time, but it is crucial that the Trustees of the TfL Pension Fund are regularly monitoring their investments which we know to be the case based on the improved funding level of this pension scheme.

Additionally, these positive valuation outcomes are notwithstanding on going actuarial updates since 2018 which have been based on more conservative valuation criteria.

It is noteworthy, for example, that most of the still existing DB pension schemes that remain open to new members, including the TfL Pension Fund, have come out of the pandemic in very good financial shape.

4. How should TfL's pension arrangements compare with other pension arrangements available elsewhere in the public sector?

As noted above, in our view easy and facile comparisons with other pension schemes should be resisted. Whether in the public or private sector, each scheme has developed its own benefits structure, membership profile, employer covenant, funding arrangements and so on to reflect the particular characteristics of the industry, workforce, employers, employment patterns and labour markets in question. The need for reform should be established with reference to the particular industry and the particular scheme in question and not through headline grabbling, politically motivated comparisons. That is why the best locus for discussions of any need for reform is within the existing governance structures of the scheme and not a review established as part of a politically motivated funding settlement.

We are aware that the Trustee Board of the TfL Pension Fund are currently carrying out the 31st March 2021 triennial actuarial valuation which we believe will indicate the financial position of the fund and that is where any discussion should be directed. The synopsis to the review frames the issue in a way that is highly revealing, asking the question of whether other workers, regardless of where they work, receive benefits similar to those of TfL employees. This is a direct and leading reference to the nasty, divisive mantra used to drive a race to the bottom in public sector pension schemes: that these schemes are somehow "gold plated". This is pure political propaganda, designed to pitch working people against one another in the interests of those who seek to drive down working class living standards while protecting the wealth of the super-rich and promoting the parasitic profiteering of big business.

Pension reform should not be established on the basis of a race to the bottom and we do not and will not accept workers being played off against one another.

5. What are your views on how TfL's pension arrangements can be fair to all going forward, including different cohorts of members and the sharing of risk between the employer and the employee?

We do not view the TfL pension fund as being unfair. TfL employees join the fund with an expectation of receiving a certain level of benefit at retirement in exchange for carrying out their employment duties as part of an overall remuneration package within a given industry. The sponsoring employer in return contributes to its employee's pension scheme on a balance of cost basis. There is no sleight of hand this is the contract both parties enter knowingly under a contract of employment.

This arrangement between TfL and its employees works no differently to any other agreement across UK industry. The contract between both parties only becomes unfair, in respect of pensions, when the workers' expectations are reduced or taken away.

Raising the question of how a scheme can share risk more fairly is almost invariably a thinly coded way of employers arguing for reducing their share of the risk and shifting it onto workers, by closing DB schemes and offering inferior DC schemes, reducing employer contributions and so on. By the very nature of DB pension schemes there is a risk which regardless of the contribution rates or benefit structure will still exist even if changes are made to members benefits. The key to this debate is how to manage risk and fairness. As noted throughout, we believe this can only be achieved by total transparency, evidence-based debate and negotiation within the governance structures of the scheme.

A fair balance of risks will certainly not be delivered by a government-mandated attack on workers' pensions, justified, cynically by the financial costs of a national covid pandemic crisis which has claimed the lives of a significant number of TfL employees.

6. How are the current pension arrangements valued by TfL's staff? How important are the current pension arrangements in recruiting new staff and retaining existing staff?

This is a key question which we believe is a crucial to understanding why our members value the TfL Pension Fund. While we acknowledge that there may be some members of the fund who do not fully understand the benefits offered by the fund, it is our very firm belief that most employees across LUL are very much engaged when it comes to their pension scheme.

Members understand that they are given a promise that on conclusion of their work based career they will receive a certain level of income upon retirement, This of course is highlighted in their Annual Pension Statement which provides estimates of their retirement benefits at age 60 and 65. They also recognise that in the event they are no longer able to carry out their employment duties the fund will provide them with an income e.g. ill health and survivor dependant(s) benefits etc.. And lastly in the event of their death, whether that be during their employment or in retirement, their loved ones will be protected.

In respect of recruitment and retention the TfL Pension Fund is a fundamental reason why individuals join LUL and remain employed in the long-term. This is mirrored across many different types of industries where similar DB pension schemes are offered, the railway industry to name one where the turnover across Train Operating Companies is much lower when you compare it against other railway employers who don't offer their staff a DB arrangement.

Offering any type of inferior pension arrangement to existing or new staff would negatively impact recruitment, as well as retention, and undermine the morale of those workers choosing to remain. Pensions have never been so important when you consider the inadequacies or limitations of the Basic State Pension (BSP). Due to the State Pension Age progressively increasing from age 65 to age 68 many workers will continue to need a decent occupational pension scheme which will allow them to retire at a reasonable age to enjoy a long retirement. Also the current single persons BSP of £179.60 a week is not in the majority of cases going to give individuals financial stability. So building up a decent occupation pension is fundamental.

7. Are there other considerations or criteria the Review should consider?

We have already commented on the opportunistic, cynical and politically motivated timing of this Review. We would also note that the terms of reference of the review do not enable it to examine other questions that directly affect the issue. For example, the financial sustainability of the scheme for the employer would be boosted significantly it TfL were not wasting hundreds of millions every year on funding profiteering by outsourcing companies.

TfL's search for 'efficiency' has led it to continue using outsourcing to deliver key transport services. The failure of the Metronet and Tubelines PPPs led London Underground to take much of its maintenance work back in-house. Yet much maintenance work on the Underground is still performed by agency workers, so called "independent contractors", and external companies. In addition, cleaning across TfL is outsourced to the US facilities management company ABM. Bus services are delivered by the private transport companies under franchise agreements. Spending on these franchise agreements represents the largest component of spending on outsourced services. Finally, London Overground and TfL Rail services are delivered by private rail operators under Concession agreements.

Analysis of TfL's procurement spending on these outsourced services shows that around 50% of TfL's procurement spending is on services that could be brought in-house. Trade Union research has shown that:

- Between 2017 and 2021, TfL has spent on average around £6.3 billion every year on procurement.
- Of that spending, an average of £3.0 billion (50%) is spent on outsourcing contracts for services that could easily be brought in-house by TfL. These include contracts for agency staff, bus operation, operating the Overground and TfL Rail franchises, as well as catering, cleaning, maintenance and security work.
- The companies operating these contracts will all demand a commercial margin of profit. In maintenance and facilities management these can be conservatively reckoned at about 5% of costs. On the bus contracts they are around 9%.
- On average around £230 million is lost to London's Transport network every year in commercial profits from outsourcing.
- Bringing these services in-house would save TfL at least £230 million every year, around 7.6% of its total procurement spending, in commercial profits.

To give a sense of the scale of this outsourcing waste, £230 million represents almost 8% of TfL's total spending on procurement (across operational and capital budgets). It's also equivalent to 75% of the £300 million that the government demanded TfL cut from its operating budget in 2021/22. This happens to be also the equivalent to around 60% of what TfL reports that it spends on pensions each year.

The review should also consider the potential impact of establishing a Crown guarantee for the scheme's liabilities. The TfL Pension Fund is technically defined as a private sector scheme but this is more a technicality than a reality. The Covid crisis has for the moment *wrecked* the 'commercial self-sufficiency' funding model that fantasised about fare revenue covering operating costs, but it also revealed the extent of co-dependence between the state and the transport system. The continued running of the Underground, rail and bus networks, were essential for the continued running of essential services and the government's bailout demonstrated this clearly. The government's letters of comfort and continued access to the Public Works Loans Board are the only things that enable TfL to continue borrowing on the private bond markets. Whatever the technical appearance, the actual reality is that the government sits behind TfL as the funder and lender of last resort. A Crown Guarantee of historic liabilities for the TfL pension scheme would be nothing more than a recognition of this reality and, as the Independent Review of Financial Sustainability commissioned by TfL argued, would reduce TfL's contributions to the scheme and save the public sector money.

8. Is there anything else you would like to add?

The Mayor of London is clear that this review of the TfL Pension Fund is wrong. In June this year, he said "Boris Johnson's Tory Government is also forcing us to look at reforming TfL's pension scheme. I've made it clear that the Government's approach to try to rush through reforms is wrong and ill-judged when our transport key workers have done so much to keep our city moving during the pandemic." The Tory plans risk unnecessary industrial action, which would be extremely costly to our city's economy and entirely of the Tories' own making".

We agree with the Mayor's observations about the political ideology that has enforced this review. To launch a review on the basis of effecting a cynical, opportunistic and politically motivated attack on the future livelihoods of all essential workers employed by TFL and London Underground who have done their duty throughout one of the worst crises of recent times, is both deplorable and contemptible.

We should also not forget that as well as risking their lives and suffering illness, many TfL key workers have tragically lost their lives in the fight against Covid -19. Many of the dependants of those who have died have rightly been able to draw upon a "critical safety net" by way of some financial support from the benefits provided by the TfL Pension Fund Occupational Scheme in line with the longstanding current fund rules. It is sobering to reflect that had the government or some employers managed to translate their long-standing hostility to the TfL pension fund into regressive reforms prior to the pandemic, the families and dependents of the workers would have had less protection.

The joint unions' position is that this review should recommend absolutely no change to the TfL pension scheme and that future discussions on the financial sustainability of the scheme should be conducted on the basis of evidence through the appropriate mechanisms, not as a consequence of cheap, nasty and divisive political manoeuvre.

Staff Side of the Pensions Working Group

15th September 2021