Royal Mail Pension Plan

Standard Note: SN 4940

Last updated: 18 July 2013

Author: Djuna Thurley

Section Business and Transport Section

The Royal Mail Pension Plan (RMPP) is a funded Defined Benefit pension scheme for employees of Royal Mail Group. The actuarial valuation of the scheme as at 31 March 2009 showed it to have a deficit of some £10 billion.

On 16 December 2008, Richard Hooper, who had been asked by the Labour Government to conduct an "independent review of the UK postal services sector", published his report. This proposed that, as part of a package of recommendations, the Government should "tackle the historic pension deficit, to enable the company to reap the benefits of modernisation." The Government agreed and the *Postal Services Bill 2008-09* published on 26 February 2009 would have provided for the transfer of historic pension liabilities to the government. However, on 1 July 2009, the then Business Secretary, Lord Mandelson, announced that he would not proceed with the plans as market conditions meant the Government had not been able to find a partner for Royal Mail on appropriate terms. In June 2010, the Conservative-Liberal Democrat Coalition Government asked Richard Hooper to produce an update of his report. Again, he recommended that the Government should relieve the Royal Mail of its pension deficit as part of a wider package of measures. The Government agreed and legislated for the transfer in the *Postal Services Act 2011*.

On 1 April 2012 the Government transferred Royal Mail's historic liabilities of around £40 billion from Royal Mail's pension scheme to a new public sector scheme (the Royal Mail Statutory Pension Scheme, RMSPS) to be administered by the government. At the same time around £28 billion of Royal Mail's pension assets were transferred to government. The Trustee of the RMPP would be responsible for pension benefits earned after 31 March 2012. The RMPP was left fully funded at the time of transfer.

In May 2013, Royal Mail Group launched a consultation on a proposal to reform of the scheme. It said that, although the transfer of the historic deficit had left the RMPP more secure, it had not addressed the cost of accruing benefits. The Communication Workers' Union said it would oppose any change to pension arrangements by executive action.

This note looks at: the development of the RMPP, the deficit and proposals for dealing with it and recent reform proposals. For more on the background to the Bill, see Library Research

Paper 10/67 *Postal Services Bill 2010/11* and RP 11/01 *Postal Services Bill – Committee Stage Report.* Other notes of possible interest include SN 6668 Privatisation of Royal Mail.

Contents

1	**Development of the scheme**	**3**
1.1	Background	3
1.2	Consultation on reforms - 2007	4
1.3	Introduction of reforms - 2008	6
	Response	7
2	**Overview of scheme rules**	**8**
3	**Pension fund deficit**	**10**
3.1	2003 valuation	11
3.2	2006 valuation	12
3.3	2009 valuation	12
4	**The Labour Government's plans**	**14**
4.1	Hooper report – December 2008	14
	Response	17
4.2	*Postal Services Bill 2008-09*	18
	Debate on the Bill	20
	Decision not to proceed	21
5	**Developments from 2010**	**22**
5.1	Update of the Hooper Report – September 2010	22
5.2	*Postal Services Act 2011*	24
5.3	State Aid Approval	25
5.4	Transfer of historic liabilities and assets to the Government	28
5.5	May 2013 - consultation on reforms to RMPP	29

1 Development of the scheme

1.1 Background

The Post Office Staff Superannuation Scheme (POSSS) was established on 1 October 1969 under the terms of the *Post Office Act 1969* when the Post Office ceased to be a Government Department and became a public corporation.[1] Prior to this, its employees were members of the Principal Civil Service Pension Scheme.[2]

1 Trade and Industry Committee, Royal Mail after Liberalisation, Second Report of 2005-06. HC 570-II, Ev 116

2 HL Deb, 10 March 2009, c1070

POSSS was a final salary scheme,[3] with benefits accrued at 1/80th of pensionable pay for each year of service, plus a lump sum of 3/80ths. This scheme was replaced by the Post Office Pension Scheme (POPS) from 1 April 1987. This again was a final salary scheme, with benefits accruing at 1/60th of pensionable pay for each year of service. The two schemes were merged to become the Royal Mail Pension Plan (RMPP) on 1 April 2000: The POSSS is now sections A and B of the RMPP; the POPS, Section C. The sponsoring employer of the RMPP is Royal Mail Group Limited.[4]

The RMPP closed to new members on 1 April 2008. For existing members, benefits accrued from 1 April 2008 are calculated on the basis of "career salary"[5] rather than on final salary. The normal pension age has increased from 60 to 65 in respect of service from April 2010.[6] As at 31 March 2011, the RMPP had 431,622 members: 129,678 employee members, 118,432 early leavers with a deferred pension entitlement; and 183,512 pensioner members.[7]

This note concentrates on the RMPP. There is also a Defined Contribution (DC) scheme[8] - the Royal Mail Defined Contribution Plan. This was launched in April 2009, for new recruits who joined from 1 April 2008, when the RMPP was closed to new members. Employees can start contributing after they have worked for the company for a year. Existing employees who are not already members of the RMPP or the RMRSP may also join. Another DC scheme – the Royal Mail Retirement Savings Plan (RMRSP) (originally designed as a lower cost and lower benefit alternative to the RMPP[9]) was closed to new members and new contributions on 31 December 2009 on the grounds that it "would be preferable, from a costs and administration perspective, to operate only one defined contribution plan in the future."[10]

There is a separate pension plan for senior executives - the Royal Mail Senior Executives Pension Plan (RMSEPP). Like the RMPP, this was closed to new members from 1 April 2008 and pension for service from that date accrues on a career salary basis.[11]

1.2 Consultation on reforms - 2007

In February 2007 (at the same time as it announced an agreement for funding the pension deficit – see section 3.2 below) Royal Mail said it would consult on "replacing the final salary scheme for newly recruited employees with a defined contributions scheme." [12] It proposed to keep the final salary scheme for existing employees but would begin consultation to examine "how we can de-risk the cost of the pension scheme in the future and make it affordable."[13]

---

3 With pension benefits based on final salary and length of service

4 *Postal Service Bill [HL] – Explanatory Notes*

5 On the basis of pensionable pay in each year of service

6 Royal Mail Group, 'Royal Mail Pension Plan, A detailed guide for Section A and B members', September 2009, p2

7 RMPP, Trustee report 2011, August 2011

8 In a DC scheme, pension benefits are based on contributions and any investment returns on them. The fund is generally used to purchase an annuity on retirement.

9 Royal Mail Group, Pensions Review 2007, Q and A accompanying letter of 8 February from Allan Leighton and Adam Crozier, Q3

10 Letter to Scheme Members from RMG, 27 November 2009

11 *Royal Mail Group Accounts 2009-10*, page 15 and 87-88

12 Royal Mail Group, Press Release, 'Royal Mail Unveils Financial Re-Organisation and Investment Plan', 18 February 2007

13 Q&A accompanying Allan Leighton and Adam Crozier letter – 8 February 2007

In a paper published on 28 September 2007, the Communication Workers Union (CWU) set out their view of the proposed changes. It argued that the only way to fully protect accrued service was to retain the link to final salary:

> The only way of fully protecting accrued service is to retain the link to final salary at the point of retirement. Simply linking to RPI (with a cap) is likely to mean that the pension payable on retirement will be less. Royal Mail's proposal therefore not only reduces the cost going forward from 1st April 2008, it also reduces the liability prior to 1st April 2008. It would wipe something like £1.6 billion off the pension deficit. Make no mistake, this money comes straight out of the projected value of the pension benefits arising from service accrued to date. In effect, having created a deficit by not paying into the scheme for 17 years, the employer is proposing to pay off a big chunk of that deficit by freezing accrued benefits and only uprating them by RPI in the future.[14]

In December 2007, *Occupational Pensions* reported that Royal Mail and the CWU had agreed on a framework of reform. The CWU said it had secured some key principles, including:

- Full protection of the use of final salary to calculate benefits already accrued;
- The final-salary scheme to be replaced for the future by a similar defined-benefit scheme;
- The right to retire at 60 for existing scheme members;
- The option to take pension at 60 with unreduced past-service benefits and to continue working beyond that age;
- The ability to negotiate a new scheme for new entrants; and
- The existing accrual rates (1/80th and 1/60th) to be maintained.[15]

On 4 October 2007, Royal Mail and Unite CMA (which represents Royal Mail managers[16]) issued a joint statement announcing that they had reached "agreement in principle regarding pay and pensions."[17] Unite CMA would support the company's proposals on pension reform, summarised below:

- Pensionable service before 1 April 2008 will continue to be calculated on the current final pensionable salary basis. There will be no change to existing arrangements for past service.
- There will be a change in how the pension is calculated from a final salary to a career salary defined benefit arrangement from 1 April 2008.
- Future service will be subject to an annual indexation by RPI (up to a maximum of 5% for each year) though the company has the discretion to raise this cap.
- Normal retirement age to be increased to 65 with effect from 1 April 2010. Existing scheme members will retain the right to take their pension from their 60th birthday onwards, though there would be actuarial reduction for pensions earned after 1 April 2010.
- AVC arrangements will be available for those who wish to increase their contributions to mitigate the effect of the changes.
- The current scheme will close to new members from 31 January 2008.
- Eligible existing employees will be given a final opportunity to join the scheme prior to 31 January 2008.

---

14 Communication Workers Union, Royal Mail Pension Proposals Question and Answer

15 'Royal mail agrees framework for pension reform', *Occupational Pensions*, No 247, December 2007

16 Unite website, Communication and Manager' Association section

17 'Royal Mail and Unite CMA Joint Statement. In Principle Agreement on Pay and Pensions', October 2007

- A high quality defined contribution scheme will be put in place for new joiners after 31st January 2008. The detail of the scheme including governance arrangements will be discussed with the union. There will be a one year waiting period before employees will be eligible to join the scheme.

Unite CMA said:

> In respect of pension we have set out our views which puts us in a positive position for the 60 day consultation period starting. We will now be seeking further comments from our members during this time and we will represent those to Royal Mail.[18]

1.3 Introduction of reforms - 2008

In February 2008, Royal Mail announced that in the absence of alternative suggestions to achieve the same level of saving, it had decided to proceed with changes to the scheme:

> In the feedback received, there were no suggestions on how else the Company might achieve the same level of saving as that was contained in the Proposal (just under 9% of pensionable pay).
>
> In the absence of alternative suggestions that were able to meet the 9% level of savings, the Company's decision is to:
>
> - To increase the normal retirement age from 60 to 65 with effect from 1 April 2010.
> - To change how people's pension is calculated from a Final Salary to a Career Salary Defined Benefit arrangement from 1 April 2008.
> - To close the Pension Plan to new members on 31 March 2008, and introduce a replacement plan on a defined contribution basis.[19]

Royal Mail said that the changes followed extensive talks with the unions and employee representatives:

> The changes follow extensive talks with unions and employee representatives since last April, which resulted in major changes to the original proposals, followed by a formal consultation with every employee member of the pension plan lasting more than 60 days from last November to mid-January this year.
>
> Royal Mail reiterated the announcement made last autumn that both the CWU and Unite had agreed to support the changes as part of wider agreements with each on pay, modernisation and pension reform.[20]

It said that changes had been made in response to the consultation. In particular, the Plan would be closed to new members from 31 March 2008, instead of 31 January 2008. Furthermore, all pension earned before any change would continue to be linked to final salary at the time of leaving or retiring rather than being linked to inflation.[21] The initial proposals, main comments received and the company's decision are summarised in the table below:[22]

---

18 Unite Press Release, In-principle agreement on Royal Mail pay, 4 October 2007

19 Royal Mail Group, Pension Consultation Feedback, February 2008;

20 Royal Mail Group Press Release, 'Decision On Pension Plan Reform', 03/03/2008

21 Royal Mail Group website, The Company's Decision FAQs

22 Royal Mail Group, Changes to the Pension Plan. The Company's Decision, 18 March 2008

Royal Mail's Original Proposal	Main comments received	Company's Decision
Close plan to new members on 31 January 2008	Acceptable if a fair and attractive alternative pension scheme is made available to new entrants	**The plan will close to new members on 31 March 2008**. Existing eligible employees will have a final opportunity to join the Plan before it closes. New recruits will be eligible after 12 months' service to start paying contributions to the new Defined Contribution plan that will be launched in April 2009. Employees who are not members of the Plan wil also be able to join the new arrangement at that time.
Change the way pension benefits build up by EITHER moving from a Final Salary to a Career Salary basis OR capping increases in pensionable pay at the level of the annual increase in the Retail Prices Index (RPI)	What members have earned so far should remain untouched. The RPI cap would be less fair for younger and lower earning members.	**The Plan will change to a Career Salary Basis from 1 April 2008.** All pension earned before this change to the Plan will be still linked to members' final pensionable pay when they retire or leave, as it is now.
Increase Normal Retirement Age (NRA) to 62 on 1 April 2008 and to 65 on 1 April 2012	Increase in retirement age would be too soon	**Normal Retirement Age will increase to 65 from 1 April 2010**
	Some members want to pay more contributions and continue to retire at 60	Members can pay more on an individual basis using Additional Voluntary Contributions (AVCs) to reduce the impact the changes will have on their pension.
	Can the Company increase the maximum number of years a member pays into the Plan?	Members will be able to build up pension for 45 years instead of 40 years by NRA. This has already been agreed following changes in age legislation.
	Members still want to be able to take benefits earned before the change to NRA (on 1 April 2010) at age 60	When they reach the age of 60, members will be able to take pension earned before the change to retirement age (in 2010) AND carry on working and contributing to their pension until they reach the maximum level of benefits.

Royal Mail expected the reforms to result in future service costs being reduced by an estimated five per cent initially, rising to around nine per cent over five years:

> The charts illustrate the level of pension contributions before and after the changes, with the Company paying around 20%, or £580 million, of pensionable pay into the Plan towards future pension benefits, and on top of this another 10% of pensionable pay to clear the deficit over 17 years. In total, the Company expects to pay around £850 million into pensions this financial year (2007/08) – around 30% of pensionable pay. Our competitors typically pay around 9%. Plan members pay contributions of 6% of pensionable pay, or around £170 million.
>
> The Company considers that after the changes the future service costs for the Company could be reduced by about 5% initially, rising to around 9% after 5 years, bringing the Company's contribution to future pension costs down to around 11% - which will still be more than the Company paid in 2006 and is still above our competitors but more affordable and sustainable.[23]

Response

On 3 March 2008, Unite CMA recommended that its members reject the pension changes:

> Unite National Secretary, Paul Reuter, says: "Royal Mail are asking for too much to soon. Its consultation has been a complete sham. We have no option but to recommend that our members reject Royal Mail's pension plan. Royal Mail have not acknowledged their responsibility for allowing the deficit to become as large as it is. They have locked themselves into such a difficult business plan, that Royal Mail is attempting to underwrite it with our members' pensions. We are urging Royal Mail to take a more reasonable approach to the issues of retirement age and future pensions

[23] Ibid

provision. In the event that our members reject the pension plan we can not rule out industrial action. We will be co-ordinating our response with the CWU."[24]

On 19 March 2008, Unite reported that in a ballot "an overwhelming 85%" had rejected Royal Mail's proposal to change their pension.[25] The CWU said it would ballot its members, with a recommendation to reject the company's pension plan:

> Both Royal Mail and CWU told you that the pension consultation process and proposal – was not the final outcome – and did not constitute an agreement.
>
> Both Royal Mail and CWU told you that the consultation process would be meaningful – and your views would be taken into account.
>
> Royal Mail's decision to move ahead with the consultation proposal means they have treated the whole exercise as a sham.[26]

On 2 April 2008, the *Financial Times* reported that CWU members had voted to reject the changes:

> The threat of postal strikes was raised yesterday after workers voted overwhelmingly to reject Royal Mail's decision to close its final salary pension scheme to new employees and raise the retirement age from 60 to 65…
>
> The Communication Workers Union said that almost two thirds of its 141,000 Royal Mail members had taken part in the ballot, with more than 90 per cent voting to reject the company's pension proposals.
>
> Dave Ward, CWU deputy general secretary, called on Royal mail to reopen negotiations with the union. He said "After the last year of unrest, Royal Mail needs to take the workforce along with them in this major change to postal workers' terms and conditions. With such overwhelming opposition to their plans, if Royal Mail can't find an acceptable solution with the CWU, industrial action will be inevitable.[27]

2 Overview of scheme rules

RMPP members comprise the employees of Royal Mail Group's main UK businesses: Royal Mail Letters, Post Office Limited, Parcelforce Worldwide, Romec and Quadrant.[28] The RMPP was closed to new entrants on or after 1 April 2008. There are three different sections of the scheme:

- Section A applies to members who joined before 1 December 1971. A person with unbroken membership since before 1 December 1971 may have rights to benefits similar to those provided under the Civil Service Pension Scheme. These are unaffected by changes made to the plan on 1 April 2008.

- Section B applies to all members who joined on or after 1 December 1971, or to members of Section A who at retirement choose to receive Section B benefits. Section B was closed to

[24] Unite Press Release, 3 March 2008, 'Unite urges managers to reject Royal Mail's pensions decision'
[25] Unite Press Release, 'Unite sees overwhelming rejection to Royal Mail pension plans', 18 March 2008
[26] CWU Northwest region, News 2008 archive, 'CWU consults members on Royal Mail's pension changes'.
[27] Andrew Taylor, 'Postal staff in threat to strike over pensions', *Financial Times,* 2 April 2008
[28] BERR, *Impact Assessment of the Postal Services Bill 2009,* page 26, para 5

new entrants from 1 April 1987. From 1 April 2008 members who have left or opted out can no longer rejoin Section B [29]

- Section C (formerly POPS) is for those who joined after 1 April 1987. Membership of section C was closed to new members from April 2008.

Leaflets for scheme members explain the provisions of the three different sections:

- *'Royal Mail Pension Plan. A detailed guide for Section A and B members';*

- *'Royal Mail Pension Plan. A detailed guide for Section C members'.*

A very broad overview of the main provisions is set out below:

- Members contribute six per cent of "contributory pay", up to a maximum of 45 years (or age 75). The company pays contributions at a rate calculated to meet the cost of accruing benefits. Following the 2009 valuation of the scheme, this is 17% of pay (down from 20% at the previous valuation).[30]

- Members with at least two years' qualifying service get a pension and a lump sum from the Plan. For service before April 2008, pension benefits accrued at a rate of 1/80th of "final salary" for each year of service. For service after that date, benefits accrue at a rate of 1/80th of salary in each year of service. Members are also entitled to a lump sum of 3/80ths (calculated differently for service before and after 1 April 2008). On retirement, a member may give up part of their pension in exchange for a higher tax-free lump sum, of up to 25% of the total value of their pension benefits.

- Normal pension age is 60 for service up to 31 March 2010 and 65 for benefits accrued after that date.[31] From April 2010, there is provision for a member to take part of their pension (for service up to 31 March 2010) while remaining in company employment and continuing to build up benefits.

- Members with at least five years' qualifying service may draw their pension early, provided they are of at least minimum pension age (55 from 6 April 2010) and the company agrees. Benefits will generally be actuarially reduced to reflect the fact that they will be in payment for longer.[32] A person retired on the grounds of redundancy after minimum pension age with at least five years' qualifying service may receive immediate payment of pension and lump sum.[33] A member with five years' company service (including at least two years' qualifying service) whose is retired early on ill-health grounds may be eligible for immediate pension benefits and a lump sum.[34]

- A lump sum may be payable on the death of a member. Dependants' pensions may be payable to a surviving spouse or civil partner and dependant children. A

---

[29] Royal Mail Group, 'Royal Mail Pension Plan, A detailed guide for Section A and B members', June 2008

[30] Royal Mail Holdings plc, Report and Accounts. Year ended 29 March 2009, page 15; Royal Mail Pension Plan Trustee Report 2010 – click on the link to summary report

[31] Ibid, p2

[32] Ibid, p11

[33] Ibid, p12

[34] Ibid, p14

> dependant's pension may be payable to an unmarried partner, at the discretion of the Trustee.[35]

The RMPP has been affected by the Government's decision to switch to the Consumer Prices Index (CPI) when setting the minimum increases occupational pension schemes are required to provide.[36] The trustees explained:

> In July 2010, the Government announced it was altering how it measures changes in the cost of living for future pension increases, moving from the Retail Prices Index to the Consumer Prices Index. This change, which came in time for the April 2011 increases, affected the way in which the Plan increases deferred pensions and some pensions in payment.[37]

Information about the RMPP can be found on the pensions section of the *Royal Mail Group website*. The RMPP website has more detailed information – including the scheme's reports and accounts and leaflets aimed at scheme members.

3 Historic deficit

In October 2010, the Government described the RMPP as having a "huge deficit, proportionately larger than that of any other major company scheme in the UK".[38] There are two main ways of measuring pension scheme funding:

- Companies making work-based pension provision available to their employees must account for the cost of doing so in their financial statements. For accounting periods beginning on or after 1 January 2005, UK listed companies are required to report their pension costs in accordance with International Accounting Standard (IAS) 19.[39]

- Trustees of Defined Benefit (DB) schemes are required to undertake a full actuarial valuation of a scheme's assets and liabilities at least every three years.[40]

Both measures show the deficit in the RMPP to be rising. Richard Hooper, who conducted an independent review of the postal services sector (see sections 4 and 5 below):[41]

> There are two ways of valuing the pension deficit – accounting and actuarial. Both tell the same story. In March 2008, the accounting deficit was calculated as £2.9 billion. Since that point the deficit has nearly trebled in size. The accounting deficit in March 2010 had risen to £8.0 billion. The triennial actuarial valuation process reported the deficit to be £3.4 billion in 2006. The latest triennial valuation showed a deficit of £10.3 billion at 31 March 2009.

The figures most often referred to are those from the actuarial valuations, on the basis of which Royal Mail's contributions to the RMPP are set.

---

35 Ibid, p17-18 and 21-22

36 For more detail, see Library Standard Note SN 5656 Occupational pension increases

37 RMPP, Trustee report 2011

38 BIS, *Delivering for the future: A universal mal service and community post offices in the digital age*, Cm 7946, October 2010, page 13

39 Companies that are not listed can chose to report in accordance with IAS19 or FRS17

40 The scheme specific funding requirements introduced by the *Pensions Act 2004* are covered in more detail in HC Library Standard Note Pension Scheme Funding, SN/BT/4877.

41 Saving the Royal Mail's universal postal service in the digital age' – An update of the 2008 Independent Review of the Postal Services Sector. Richard Hooper CBE', Cm 7937, September 2010, p26

3.1 2003 valuation

The last three actuarial valuations have shown the RMPP to be in deficit. However, this has not always been the case. From 1988 until the 2003 valuation, the POSSS scheme (now sections A and B of the RMPP) was in surplus. The 2003 actuarial valuation found the RMPP to have a deficit of £2.5 billion. Royal Mail reached an agreement with the trustees to pay £140-150 million a year towards the deficit, with a view to repairing it over 40 years (the longest period allowed under the Trust Deed). It recognised that its payments were likely to have to increase in future, in part because a repayment period of this length was out of step with normal practice.[42]

Royal Mail has had to explain on a number of occasions why it took a "contributions holiday" in the 1990s in relation to POSSS (now Sections A and B of the RMPP). In 2005, it told the Trade and Industry Select Committee that the surplus in the scheme from 1988 onwards meant it made little economic sense to continue contributions:

> Under the Prescribed Basis (set out in Schedule 22 to the *Income and Corporations Taxes Act 1988*), employers have to take action to utilise any surplus assets above the 105% funding level on this basis either to improve benefits or to take a contributions holiday. The intention was to control the funding of the plan to below the Prescribed Basis. It did not make economic sense to continue making contributions, only to take a contributions holiday enforced under this legislation.

Furthermore, it said the scheme "would have been expected to be in a surplus position in March 2003 had it not been for the fall in equity values and future assured dividend yields and the strengthening of mortality."[43]

Alex Smith, Director of Strategy at Royal Mail, told the Committee that the contributions holiday was taken for "the 13 year period prior to 2001 when the pension fund was, I believe, in surplus for the whole period".[44] Company contributions restarted in full when the scheme was no longer in surplus:[45]

> During the holiday, the financial position of the Plan was regularly monitored. However, at that time, no one could have predicted the significant fall in investment markets in the years prior to 2003 or the sudden rise in the number of people living longer. As soon as the Trustee's actuarial valuation showed that the Plan was not in surplus, company contributions restarted in full. The company has always contributed to Section C (formerly POPS).

In debate on the *Postal Services Bill 2008-09* in the House of Lords, the Labour Peer, Lord Clarke of Hampstead, a former union representative and trustee of the pension fund, said he had queried the contributions holiday at the time:[46]

> Besides being a trustee of the pension fund, I was the negotiating officer for pensions. When it was announced that the 6 per cent paid by the staff would continue but that the management would put nothing into the scheme at first, you could live with it for a year or so. I took the matter to the legal profession and asked how right their action was. The reason that the holiday was enjoyed by the management and, in turn, the Government was that the trustee explicitly said that as the fund—thereby, the

[42] TISC, *Royal Mail after Liberalisation*, HC 570-II, Second Report 2005-06, Ev115-22
[43] *ibid*., Appendix 20, Section 3
[44] *ibid*., Q68
[45] RMG, Pensions Update 01, May 2007
[46] HL Deb, 31 March 2009, c1008

> Government—had responsibility for deficiencies, it had the right to deal with surpluses. It was game, set and match to the lawyers; I folded up my tent and went home. I could not do anything about it; it was there in black and white.

Speaking for the Labour Government, the then Parliamentary Under Secretary of State, Lord McKenzie of Luton, said it was "difficult to discern what the subsequent funding arrangements might have been after the 2003 triennial valuation, had there been more funds in the scheme in the interim".[47]

3.2 2006 valuation

The 2006 actuarial valuation showed the deficit to have increased to £3.4 billion.[48] Royal Mail Group reached an agreement with the trustees to repair the deficit over 17 years.[49] The terms of the agreement included:

- Placing £1 billion in an "escrow account" to provide security for the pension scheme trustees. The money cannot be used for other purposes and can only be released in the event of certain defined events or circumstances.[50]

- Making deficit recovery payments to the RMPP of £260 million a year (increasing in line with the RPI) over the 16 years from 31 March 2007. This was in addition to regular pension contributions (at that time, equal to 20% of pensionable pay).

The result is that Royal Mail currently pays approximately £280 million a year to reduce the deficit, on top of approximately £550 million in regular service payments.[51]

Royal Mail explained that a number of factors had contributed to the increased deficit as at March 2006:[52]

> - people are generally living longer and this has significantly increased the value put on pension fund liabilities. On average, men retiring at 60 are now likely to take their pension for 26 years (29 years in the case of women) and people are increasingly living longer.
>
> - lower predicted long-term investment returns mean less will be earned by pension funds in the future than expected.
>
> - recent changes in pension laws mean pensions now cost more to provide.

3.3 2009 valuation

Despite Royal Mail making deficit recovery payments of at least £260 million in 2007, 2008 and 2009, the deficit had increased to £10.3 billion by 31 March 2009.[53] Reasons for this were:[54]

---

47 HL Deb, 31 March 2009, c1050

48 BERR, Impact Assessment of the Postal Services Bill, 26 February 2009, Annex 1, para 6

49 RMG, 'Royal Mail Unveils Financial Re-Organisation and Investment Plan', Press Release, 18 February 2007

50 Q&A accompanying Allan Leighton and Adam Crozier letter – 8 February 2007

51 BIS, *Delivering for the future: A universal mail service and community post offices in the digital age*, Cm 7946, October 2010, para 2.11

52 Royal Mail website: Funding of Pension Plan FAQs

53 Richard Hooper CBE, *Saving the Royal Mail's universal postal service in the digital age: An Update of the 2008 Independent Review of the Postal Services Sector*, Cm 7937, September 2010, p26

54 Royal Mail Pension Plan – Trustee Report 2010

- The financial crisis of 2008 and the recession both hit the value of the Plan's investments.

- The years that members are expected to enjoy retirement continued to increase. It is good news that our pensioners are enjoying longer and healthier retirements but it does mean that more money will be needed to pay pensions for longer.

- Bond yields have fallen since the last valuation. The low bond yields have meant that a higher value has been placed on the Plan's liabilities.

Following this valuation, the company reached an agreement with the trustees to repair the deficit over 38 years. The key points of the plan were:[55]

- Deficit payments of £282 million a year (rising in line with inflation), plus contributions of four per cent of pay, with effect from 1 April 2013 until 31 March 2023.

- The £1 billion that Royal Main Group had set aside for the RMPP in 2006 had risen in value to £1.2 billion and remained available to call on if necessary.

This agreement was subject to formal review by the Pensions Regulator.[56] Richard Hooper's report of September 2010 said this compounded the problems already associated with the deficit:[57]

> This latest triennial valuation has led to an agreement between the Pension Trustees and the company to fund and repay the deficit over 38 years, representing the shortest period of time over which Royal Mail can realistically afford to pay. Such a long repayment period is quite unprecedented by modern standards and The Pensions Regulator (TPR) has expressed substantial concerns about this and the deficit figure. The agreement is now subject to a formal review by TPR. TPR has wide-ranging powers that could extend to imposing a new and more difficult recovery plan, with unknown consequences for the affordability of the deficit repayments. The review by the TPR compounds the problems already associated with the pension deficit.

A funding update, as at 31 March 2010, showed an "improvement in the funding level to 76%, primarily due to strong investment returns". The assets were valued at £26 billion as at 31 March 2010 and the liabilities at £34.4 billion, giving rise to a deficit of £8.4 billion".[58] The Government said:[59]

> The conclusion is clear – the deficit is huge and it is extremely volatile. Even at £8.4 billion, the pension deficit is proportionately larger than that of any FTSE100 company. The pension funds assets, which are valued at £26 billion, are dwarfed by its liabilities, which are estimated at £34 billion. With net assets (excluding pensions) of only £1.8 billion, the pension deficit means Royal Mail is balance sheet insolvent.

---

55 *ibid*.

56 The Pensions Regulator was established under the Part 1 of the *Pensions Act 2004* as the regulator of UK work-based pension schemes. For more information, see: http://www.thepensionsregulator.gov.uk/index.aspx

57 Saving the Royal Mail's universal postal service in the digital age' – An update of the 2008 Independent Review of the Postal Services Sector. Richard Hooper CBE', Cm 7937, September 2010, p26

58 Royal Mail Pension Plan – Trustee Report 2010

59 BIS, Delivering for the future: A universal mail service and community post offices in the digital age, Cm 7946, October 2010, para 2.11

In 2011, the Trustee said that because it was working with the Government on the "pension solution", it had not asked the Actuary to carry out a funding check for 2011. However, it did not think the funding level had decreased in the last year:

> Given that the Plan's investment return (8.0%) was higher than the benchmark return (6.7%) and Royal Mail Group continued to pay deficit contributions, all other things being equal, the funding level is not expected to have decreased during the last year. [...]
>
> In the meantime we set out below the funding levels of the Plan as at 31 March 2009 and 31 March 2010. Plan funding levels change as the market value of the Plan assets rise or fall and the assumptions used by the Actuary are updated.
>
> | | 31 March 2009 | 31 March 2010 |
> |---|---|---|
> | Value of assets: | £20.2 billion | £26.0 billion |
> | Value of liabilities: | £30.5 billion | £34.4 billion |
> | Funding deficit: | £10.3 billion | £8.4 billion |
> | Funding level: | 66% | 76% |
>
> The funding level improved in the year to 31 March 2010 mainly due to strong investment returns and, as a result, the deficit decreased by £1.9 billion.[60]

Talks with the Pensions Regulator about the deficit would continue:

> In last year's Report we informed you that the Pensions Regulator had substantial concerns about the deficit and other aspects of the funding agreement which the Trustee had reached with Royal Mail Group. We can report that discussions continue with the Pensions Regulator in relation to these concerns and the potential impact of the *Postal Services Act.*[61]

The Government took responsibility for the historic liabilities of the RMPP at 1 April 2012 (see section 5.4 below).

4 The Labour Government's plans

4.1 Hooper report – December 2008

On 19 December 2007, John Hutton, the then Secretary of State for Business and Regulatory Reform announced an independent review of the UK postal services sector. This was chaired by Richard Hooper CBE.[62] The report of this review was published on 16 December 2008. It found that Royal Mail was "bearing a much higher level of risk associated with the pension fund deficit than many larger, financially stronger companies":

> 74. Royal Mail has taken action to reduce the cost of future pensions provision. But it must also make contributions to address the deficit: the gap between the assets of the pension plan and the forecast liabilities. At the time of the last triennial valuation, the deficit was calculated at £3.4 billion. In 2007-8, Royal Mail's cash deficit payment was £284 million, with payments expected to continue for the next 15 years. In spite of this,

60 RMPP, Trustee report 2011

61 Ibid

62 Richard Hooper is currently Chairman of VocaLink Holdings Ltd, and a non-executive Director at YELL Group plc. For further details, see page 163, 'Modernise or decline. Policies to maintain the universal postal service in the United Kingdom'. An independent review of the UK postal services sector, Cm 7529, 16 December 2008

> the deficit has increased by £2.5 billion (some 75%) since 2006, with the most recent estimate putting it at £5.9 billion. Even before this recent increase, the deficit was among the largest of any reported by a UK company, as is illustrated in Figure 17.
>
> 75. Although consumers bear part of the cost through higher prices, the burden of the deficit payments contributes significantly to the current financial pressures on Royal Mail, and makes it more difficult for the company to compete in a liberalised market. The recent growth in the size of the deficit means that the size of its contributions may have to be increased (or the repayment period extended) following the next triennial valuation due in 2009.
>
> 76. The volatility of the deficit is also highly significant for a business of Royal Mail's size. The company is bearing a much higher level of risk associated with the pension deficit than many much larger and financially stronger companies. On an accounting basis, its pension deficit is over six times larger than the cash generated by its business operations (before financing and investing activities). Both the size of the deficit and its volatility adversely affect the company's ability to finance and invest in its core business. Because of the size of the deficit, this is likely to remain a problem for the foreseeable future.[63]

It found that customers were paying higher prices because of the deficit and that the constraints which the deficit imposed on Royal Mail, "particularly in terms of investment, would make it harder to achieve the necessary efficiency improvements across the business and build an innovative responsive service for consumers with the universal service at its core."[64] It argued that a new approach was needed:

> 157. Although Royal Mail is not the only business or public sector body with a significant pensions deficit, its circumstances are unique. Following the decision by Government to liberalise the market, Royal Mail is having to respond to new competitive pressures whilst also meeting its obligations to provide the universal service. And it is now having to do so against a background of falling volumes and revenues brought about by the digital revolution. A new approach is needed to tackling Royal Mail's pension deficit if the benefits of liberalisation are to be realised.
>
> 158. In other sectors previously dominated by a state-owned monopoly, Government has taken action to address historic liabilities in order to facilitate beneficial change in the industry. Changes to the rail industry in 1993, and the coal industry in 1994 are examples where action on pension liabilities was fundamental to enabling necessary restructuring of the industry – including in the case of coal against the background of a contracting market.
>
> 159. In the case of Royal Mail, the cost of the deficit is currently shared between consumers, Royal Mail and the taxpayer as shareholder. We doubt whether this is appropriate or effective as a long-term solution, particularly given the prospect of a significant increase in the size of the pension deficit.
>
> - The increasing resistance of customers to paying higher prices for postal products, and falling letter volumes, mean that further price rises to meet the increasing cost of the deficit are unlikely to be effective. Instead, they are more likely to accelerate market decline driven by e-substitution.

---

63 Richard Hooper CBE, Dame Deirdre Hutton, Ian R Smith, 'Modernise or decline. Policies to maintain the universal postal service in the United Kingdom'. An independent review of the UK postal services sector, Cm 7529, 16 December 2008

64 Ibid, para 155-6

- Although Royal Mail does have scope for significant efficiency savings, the benefits of these savings will be fully absorbed in placing the company on a sustainable financial basis going forward. There is very little margin, particularly in the short term, to fund increased deficit contributions, and doing so could in fact endanger the universal service.

160. Other, short-term measures are possible. But, on their own, they would not address the underlying causes of the deficit, nor would they alleviate the adverse impact of the deficit on Royal Mail and the wider postal services market.

- the sale of GLS would be one option to reduce the pensions deficit. But since GLS generates cash, it may also weaken the ability of the company to fund the significant ongoing deficit payments that would still be required.

- a one-off injection of taxpayer funding into the scheme by Government would require clearance under state aid rules, and could well make it more difficult to obtain subsequent approval for longer-term measures to address the underlying cause.

161. A long-term solution is therefore essential. And it is our view that that the best long-term solution must be for the risk around the historic liabilities to be managed by the body – central Government – that has the size and financial resources best suited to perform that role in a way which does not threaten the universal service.

162. Provided that the constraints on Royal Mail's ability to modernise have been removed, we recommend that:

- the responsibility for the historic liabilities should be transferred from Royal Mail to the Government. This would leave Royal Mail with a much smaller scheme and liabilities that would no longer be of a size that called into question the financial viability of the business. It would relieve the cash and balance sheet constraint on new investment and increase Royal Mail's competitiveness. It would also benefit consumers by reducing the pressures on stamp prices.

- the Government should take responsibility for the historic liabilities in a way which provides an incentive on all stakeholders, including the unions, to modernise Royal Mail. It could, for example, take a staged approach in which the scheme's assets and liabilities related to pensioners and members with deferred benefits were transferred to separate, Government-backed arrangements. As active members left the company as a result of the modernisation process, their liabilities and assets could be also be transferred.

163. These recommendations are not a complete solution for the problems currently faced by Royal Mail. On their own, they will not bring about the company's modernisation. They are, however, a significant part of the solution if implemented with our other recommendations, especially partnership.

164. Detailed practical arrangements for transferring the risk associated with the pension liabilities should be a matter for Government. Options might include, for example, legislation to take over relevant assets and liabilities of the scheme and pay benefits from general taxation; the purchase of annuities; or the operation of a separate, managed fund. As part of this process, Government would need to obtain state aid approval from the European Commission.

165. We recognise that the long term impact on public finances arising from risks such as longevity could be significant. Nevertheless, we believe that the recommendation is consistent with our objective to reduce the risk to public finances and, therefore, to the

> taxpayer. It does not require the Government to fund the full deficit immediately. And by removing a very significant financial risk and business constraint, the transfer of historic pension liabilities from Royal Mail would result in a compensating uplift in the value of Government's equity stake in the business.[65]

Response

In an initial response to the report, Lord Mandelson, the then Secretary of State and Government Spokesperson for Business, Enterprise and Regulatory Reform, said:

> The Report recommends that as part of a package of changes, the government should take over responsibility for reducing substantially the pension deficit. I would stress that Hooper says this would only be justified as part of a coherent package to secure the Royal Mail's long term viability…
>
> My Department will want to study the report in detail. I intend to respond with a full statement of our policy in the early part of next year...I can say now that the Government agrees with Hooper's analysis and the recommendations.[66]

In debate in the Commons, the then Shadow Business Secretary, Alan Duncan said he was concerned at the implications for the public finances if the Government took on responsibility for the deficit:

> The Government intend to raid the pension fund in order to plug the black hole in the public finances, dumping the cost of a multi-billion pound liability on future generations. The seizure of £22 billion from Royal Mail's pension fund would make the Government's woeful borrowing figures look a little better, but it would saddle future generations with an almost open-ended bill.
>
> Can the Minister tell us what he estimates the long-term annual pensions liability to the taxpayer to be? Will Royal Mail's pensions liability be included in the Government's borrowing figures? What exactly will happen to the £22 billion that is currently in the pension fund? Will the Minister keep the fund intact and top it up, or not? Has he been assured that such action would comply with European Union state aid rules?[67]

Responding, the then Business and Enterprise Minister Pat McFadden said the Government would be relieving Royal Mail of a burden:

> As I say, the hon. Member for Rutland and Melton (Alan Duncan) has a weird concept of stealing if he thinks that our proposals amount to stealing. The proposals take into account the fact that there are assets and liabilities in the pension fund. The problem for the company is that the liabilities are far greater than the assets. The Government will therefore try to address that problem to relieve the company of the burden of the additional payment that that deficit poses for it at the moment.[68]

This would be all the more important given the expected increase in the deficit at the 2009 valuation:

> We expect it to have grown substantially from the valuation in 2006 of a £3.4 billion deficit. That starkly shows the size of the burden imposed on the company, which is why, in the context of a package of wider reform, it makes absolute sense to relieve the

65 Ibid
66 HL Deb, 16 December 2008, c742-5
67 HC Deb, 16 December 2008, c967
68 HC Deb, 16 December 2008, c978

company of that burden, so it can concentrate on the investment that is required to finance the transformation that the Royal Mail sorely needs.[69]

The CWU welcomed the proposal to secure the pension scheme, while reacting "with dismay" to other parts of the proposal:

> 27. CWU welcomes Hooper's recommendation that the Government should take over responsibility for Royal Mail's pensions deficit. It was Government legislation which permitted the irresponsible "holiday" on pensions contribution for the employer. This does need to be reversed if the company is to be allowed to operate with a viable financial balance sheet. The Government benefited from this "holiday", so the reform is overdue and appropriate.[70]

On 19 February 2009, Jane Newell, the then chair of Royal Mail Pensions Trustees Limited said in a letter to Lord Mandelson that there could be very severe consequences for the Royal Mail Pension Plan if the recommendations of the Hooper Report were not implemented:

> If the recommendations of the Hooper Report were not implemented, the consequences could be very severe indeed for the Royal Mail Pension Plan and for Royal Mail itself. In particular, in light of the weakness of Royal Mail, the Trustee would consider it necessary to seek to significantly strengthen the funding basis for the 2009 actuarial valuation. On a self-sufficient basis this would value the liabilities far higher, resulting in a deficit that would be significantly larger than the £5.9bn quoted in the Hooper Review, which is on the existing ongoing basis. The law gives the Trustee and Royal Mail until 30 June 2010 to agree this valuation.
>
> Whatever its precise amount, the deficit resulting from a strengthened funding basis for the 2009 valuation is highly unlikely to be affordable by Royal Mail, with potentially devastating consequences. If this were the case, the Plan's financial resources would not be sufficient to provide the full value of benefits, which would need to be very significantly reduced. At present, in a winding-up the Plan would not even be able to provide as much as 50% of members' benefits.[71]

4.2 Postal Services Bill 2008-09

The Labour Government published its *Postal Services Bill 2008-09* on 26 February 2009, the same day as its response to the Hooper report.[72] Part 2 of the Bill provided for the Secretary of State to transfer the historic pension liabilities to government. In particular, the Secretary of State would be given power to: [73]

- Establish a new statutory scheme which may be used to provide benefits to certain members of the Royal Mail Pension Plan ("RMPP"');
- Transfer rights and remove liabilities from the RMPP;
- Transfer assets from the RMPP to the government;
- Divide the RMPP into sections and to allocate assets and liabilities between those sections.

---

69 HC Deb, 16 December 2008, c974

70 CWU Response to the Hooper Review, CWU Press Release, CWU responds to Mandelson, 16 December 2008

71 Jim Pickard, The letter from the chair of the Royal Mail Pensions Trustees, *Financial Times,* 24 February 2009

72 BERR, The Future of the Universal Postal Service in the UK, Cm 7560, February 2009

73 Postal Services Bill [HL] Bill 100 2008-09 – Explanatory Notes

The Bill would have enabled the Secretary of State to create a new public service scheme, comparable to the NHS, Teachers and Civil Service schemes.[74] This was the Government's preferred mechanism for meeting the historic liabilities as it did not involve "government taking investment risk with taxpayer's money".[75]

Future service liabilities would be the responsibility of Royal Mail. The Government aimed to leave the RMPP with sufficient assets to meet its liabilities, with the result that government would absorb an estimated deficit of £6 billion:[76]

> 3.6 Future pensions liabilities accrued after 16 December 2008 for the current 160,000 employees (including liabilities resulting from salary increases) will remain within the Royal Mail Pension Plan, and will be much smaller than the current scheme. The Government will ensure that sufficient assets remain with the scheme so that at the date when the historic liabilities are transferred to the new pension scheme, the assets that remain in the Royal Mail Pension Plan are sufficient to meet its liabilities. There will be no change to the arrangements for employees who joined the company after April 2008, who will continue to participate in a defined contribution scheme.
>
> 3.7 Once the amount of the assets required to meet this funding level has been agreed, the remaining assets will be transferred to Government. We estimate that approximately £23.5 billion assets will be transferred, meaning that Government will absorb a deficit of £6 billion. These assets will only be sold over a number of years to protect value for money for the taxpayer.

Because the transfer of the historic deficit involves government support to a company operating in a competitive market, state aid clearance would be required from the European Commission.[77] Furthermore, because it would require a significant commitment from the taxpayer, the Government said the transfer would be dependent on there being a "partnership agreement" to place the company "on a sustainable basis going forward":[78]

> 3.10 A decision to take on responsibility for historic pension liabilities is a significant commitment, both for taxpayers and for members of the scheme. For this reason, the Government agrees with Hooper's recommendation that it should be linked to the agreement of a partnership that places the company, and the universal service, on a sustainable basis going forward. If it proves impossible to conclude a partnership agreement, the Government will not proceed with this change to the pension arrangements. This is the choice we all face.

The Government emphasised the security that the proposal would give to scheme members:[79]

> 3.4 Under these proposals, all members of the scheme with accrued rights earned before December 2008 will have complete security that their entitlements will be honoured in full. This is a significant improvement for scheme members on their current position given the funding level of the Royal Mail Pension Plan. The Government will ensure that this protection for past entitlements is enshrined in primary legislation, so that no member's historic rights are adversely affected by the

74 BERR, The Future of the Universal Postal Service in the UK, February 2009
75 BERR, Impact Assessment of the Postal Services Bill, 26 February 2009, page 30, para 22
76 BERR, The Future of the Universal Postal Service in the UK, February 2009
77 BERR, Impact Assessment of the Postal Services Bill, 26 February 2009, page 27, para 9
78 *ibid*.
79 *ibid*.

> changes. This will provide comfort to scheme members that the benefits they have earned through past service are protected and cannot be reduced. In addition, taxpayers will have the certainty that it is Royal Mail that will bear the full cost of future pensions provision for its current employees and costs relating to future salary increases.

Debate on the Bill

The Bill passed through its House of Lords stages, with Third Reading on 20 May 2009.[80] One of the key issues raised in the debate was whether the transfer of pension liabilities to government should be contingent on restructuring of Royal Mail (see section 2.4 above). The then Business Secretary, Lord Mandelson, argued that public support would be dependent on the Government having taken steps to "ensure that the company as a whole has a future and is engaged in transforming the service it provides".[81] He also argued that state aid clearance would not be forthcoming in the absence of modernisation:[82]

> A bailout of the pension fund on this scale is clearly state aid and is quite a tall order. It requires clearance by the European Commission. We will be in a position to obtain that clearance from the Commission if the measures that we are adopting to tackle the pension fund deficit are accompanied by modernisation, reforms and transformation of the business, which the legislation as a whole, including the introduction of a minority strategic partner, aims to achieve. If anyone imagines that it would be simple or even possible to go ahead simply with a bailout of the pension fund and nothing else, I am afraid that they are not weighing properly the implications of that for state aid clearance. I do not think we would get it.

Opposition Work and Pensions Spokesperson, Lord Skelmersdale, agreed that the rescue of the pension scheme should be "contingent on putting the Royal Mail on a secure footing for the future to prevent the need for any more taxpayer money going to subsidise a company that, to say the least, has failed to keep up with the times".[83]

On the other hand, Labour Peer, Lord Clarke, a former union representative and trustee of the pension fund, argued that the Government was in any case responsible for the deficit:

> In the final analysis, under the trust deed, the Government are responsible for the deficit. Whether we like it or not, that is part of the trust deed, which allowed the Post Office to take almost a 13-year contribution holiday.[84]

In its report on the *Postal Services Bill* the Business and Enterprise Committee also argued that a strong case could be made for state aid clearance without radical restructuring:[85]

> 120. The universal service is a service of general economic interest and indeed one of the most appreciated of such services. The United Kingdom will be taking action to ensure continued provision of that service, and it is taking this action only after it is clear that it is necessary. The majority of the liabilities it assumes will date from before market opening. Royal Mail Group will be left with significant pension liabilities, and will lose the assets underpinning the historic pension scheme. The universal service

---

80 For further information, see Parliament Website – *Postal Services Bill 2008-09*

81 HL Deb, 10 March 2009, c1132

82 HL Deb, 31 March 2009, c985; See also *Government Response to the House of Commons Business and Enterprise Select Committee Report on the Postal Services Bill* (Fifth Report of 2008-09: HC 172-I), Cm 7623, May 2009, para 59

83 HL Deb, 31 March 2009, c1004

84 HL Deb, 10 March 2009, c1071; See also, c1084 [Lord Haskell]

85 BEC, *The Postal Services Bill,* Fifth Report of 2008-09, HC 172-1, 1 April 2009, para 120

> provider will remain subject to regulation to prevent market abuse. In our view, a strong case can be made for state aid clearance for removal of part of [Royal Mail Group's] pension liabilities without radical restructuring or compensating competitors.

Another issue raised by Lord Clarke was whether Royal Mail employees should have their rights accruing from future service protected. He proposed a form of protection like that introduced when the electricity supply and railway industries were privatised, whereby employees with continuity of service retained rights to continue to participate in the scheme.[86] The then Parliamentary Under Secretary of State, Lord McKenzie of Luton, responded that decisions on future pension provisions were "rightfully an operational matter for the Royal Mail board".[87]

Decision not to proceed

On 19 February 2009, Jane Newell, the then chair of the RMPP trustees, warned of "severe" consequences for the RMPP if no action was taken. The deficits resulting from the 2009 valuation were "highly unlikely to be affordable by Royal Mail, with potentially devastating consequences":

> If this were the case, the Plan's financial resources would not be sufficient to provide the full value of benefits, which would need to be very significantly reduced. At present, in a winding-up the Plan would not even be able to provide as much as 50% of members' benefits.[88]

On 1 July 2009, Lord Mandelson announced that the Government had been unable, because of current market conditions, to find an appropriate partner for Royal Mail (see section 2.4 above). Because of this, there was no prospect of achieving the objectives of the Bill. The Government would return to the issue when conditions changed:

> My Lords, market conditions have made it impossible to conclude the process to identify a partner for the Royal Mail on terms that we can be confident would secure value for the taxpayer. There is therefore no prospect in current circumstances of achieving the objectives of the Postal Services Bill. When market conditions change, we will return to the issue. We remain convinced that Hooper's combined package offers the best chance of securing the universal postal service while protecting Royal Mail pensions.[89]

In January 2010, the CWU argued that there were "a number of ways the pension deficit could be dealt with":

> These include, but are not limited to: an extended repayment period; a 'crown guarantee'; or, direct repayments. The deficit can be dealt with under existing legislation. The Postal Services Bill offered only one particular route. Avoiding legislation would mean the deficit could be dealt with quickly.[90]

---

[86] HL Deb, 20 April 2009, c1277

[87] *ibid*., c1279

[88] Jim Pickard, The letter from the chair of the Royal Mail Pensions Trustees, *Financial Times,* 24 February 2009

[89] HL Deb, 1 July 2009, c222-3

[90] CWU, *Time to Deliver*, January 2010

5 Developments from 2010

Following the general election, the new Conservative-Liberal Democrat Coalition Government said it would “seek to ensure an injection of private capital into Royal Mail, including opportunities for employee ownership.”[91]

5.1 Update of the Hooper Report – September 2010

On 24 June 2010, Business Secretary, Vince Cable, announced that Richard Hooper would be updating his December 2008 report (see section 4 above). Mr Hooper was to let Ministers have his initial views in the summer and publish a fuller update by early autumn.[92]

The updated report – *Saving the Royal Mail’s universal postal service in the digital age* – on 10 September 2010.[93] In this report, Richard Hooper argued that “compared with twenty months ago, the pension deficit is an even stronger risk to the Royal Mail’s financial health and therefore to the sustainability of the universal postal service.” The latest triennial valuation showed a deficit of £10.3 billion at 31 March 2008. An agreement had been reached to repay the deficit over 38 years but this was subject to a formal review by the Pensions Regulator:

> The third factor continuing to impact Royal Mail’s financial health, alongside market decline and inadequate levels of modernisation, is the pension deficit. Compared with twenty months ago, the pension deficit is an even stronger risk to Royal Mail’s financial health and therefore to the sustainability of the universal postal service.
>
> The deficit continues to pose a significant constraint on Royal Mail’s business, sapping cash from the company and causing Royal Mail to be balance sheet insolvent. The deficit hampers Royal Mail’s ability to compete with other operators. Customers remain price sensitive; thus the market will not bear the cost of the pension through an increase in prices.
>
> Royal Mail has made, as noted earlier, important changes to the pension scheme thus reducing annual accrual costs. The problems associated with the Royal Mail Pension Plan (RMPP) are well documented, in the 2008 report, and elsewhere.
>
> There are two ways of valuing the pension deficit – accounting and actuarial. Both tell the same story. In March 2008 the accounting deficit was calculated as £2.9bn. Since that point the deficit has nearly trebled in size. The accounting deficit in March 2010 had risen to £8.0bn. The triennial actuarial valuation process reported the deficit to be £3.4bn in 2006. The latest triennial valuation showed a deficit of £10.3bn at 31 March 2009.
>
> This latest triennial valuation has led to an agreement between the Pension Trustees and the company to fund and repay the deficit over 38 years, representing the shortest period of time over which Royal Mail can realistically afford to pay.
>
> Such a long repayment period is quite unprecedented by modern standards and The Pensions Regulator (TPR) has expressed substantial concerns about this and the deficit figure. The agreement is now subject to a formal review by TPR. TPR has wide-ranging powers that could extend to imposing a new and more difficult recovery plan, with unknown consequences for the affordability of the deficit repayments.

---

[91] The Coalition – Our Programme for Government, May 2010

[92] BIS Press Release, 24 June 2010, ‘Government asks Hooper to refresh his Royal Mail report’

[93] ‘Saving the Royal Mail’s universal postal service in the digital age’ – An update of the 2008 Independent Review of the Postal Services Sector. Richard Hooper CBE’, Cm 7937, September 2010

> The review by the TPR compounds the problems already associated with the pension deficit.[94]

Richard Hooper confirmed his earlier view that the Government should take responsibility for Royal Mail's historic deficit as part of a wider range of measures:

> The 2008 report recommended that the Government should relieve the Royal Mail of its pension deficit as part of a wider package of measures. Taking the historic pension deficit away hugely helps Royal Mail's ability to sustain the universal postal service. The need for that action is now greater than ever. Without such action, Royal Mail's pension deficit will continue to threaten the universal postal service and will remain a barrier to the private sector investment and discipline which it desperately needs.
>
> However, it is still difficult to justify to taxpayers that they should take on the deficit if Royal Mail cannot deliver faster modernisation. As set out in the 2008 report, removing the deficit by itself will not solve Royal Mail's problems on a sustainable basis.
>
> **Restructuring Aid**
>
> The 2008 report stated that "doing nothing" on pensions was not a policy option. Inaction could lead to Royal Mail having to approach the Government for emergency financial support in order to continue as a going concern. Any such support, the report noted, would have to be carried out under a "forced restructuring" under EU rules to ensure that Member States do not harm competition.
>
> Royal Mail has made progress on modernisation but the wider reforms proposed for the company in 2008 did not proceed. As a result the situation has got worse since then with faster than anticipated falls in mail volumes and substantially increased pension deficit.
>
> Given this worsening situation, the European Commission may consider any reform of the Royal Mail pension fund under its Restructuring Aid guidelines. As stated in the previous report, the purpose of Restructuring Aid is to restore the long-term commercial viability of a business such that it no longer needs further state support. While the Restructuring Aid route has disadvantages, ultimately, a restructuring of both the pension and the business is what Royal Mail needs, and guidelines are in place at the EU level to manage such situations. Many of the measures that the Commission could ask of Royal Mail as a condition of state aid approval (such as reducing its cost base) are things that must happen and are happening anyway. The onus will be on the Government to demonstrate that its support for the pension (and any other support) does not distort competition. It is, however, important that action is taken now to address the problems to prevent it needing rescue aid in the future.[95]

Responding to the report, Business Secretary, Vince Cable, said the Government would come forward with legislation in the autumn:

> This update reaffirms the findings of Richard Hooper's original report and the views he has given me during the course of the summer. He paints a very clear picture - Royal Mail is facing a combination of potentially lethal challenges – falling mail volumes, low investment, not enough efficiency and a dire pension position.
>
> We are determined to safeguard Royal Mail for the future and help it tackle these challenges. We will come forward with new legislation in the autumn. It will draw heavily on Hooper's analysis and recommendations and the Government's wider

[94] Ibid, page 26
[95] Ibid, page 33

objectives, including the need for employees to have a real stake in the future of the business.[96]

The Communication Workers' Union stressed the importance of ensuring that pension scheme assets were used for paying the pensions of scheme members. Deputy General Secretary, Dave Ward said:

> We fear the pensions of our members will be at risk under privatisation. Everyone hears about the deficit, but there's over £26 billion in assets which belongs to the postmen and women who have paid their contributions every week of their working lives. We will never let the government get its hands on that money for anything other than what it's intended - to pay for the retirement of hard-working postal workers.[97]

5.2 Postal Services Act 2011

In the Queen's speech on 25 May 2010, it was announced that a *Postal Services Bill* would include "measures to resolve the problems surrounding Royal Mail's pension deficit."[98] The *Postal Services Bill 2010-11* had its first reading in the House of Commons on 13 October 2010.[99] A discussion of the provisions of the Bill and the issues raised in connection with it can be found in Library Research Paper 10/67 *Postal Services Bill.*

The Bill's Second Reading was on 27 October 2010 and was considered in Public Bill Committee in 20 sittings, between 9 November and 9 December 2010. These debates are covered in Library Research Paper RP 11/01 *Postal Services Bill: Committee Stage Report.* Report stage and third reading were on 12 January 2011.[100]

The Bill had its Second Reading in the House of Lords on 16 February 2011.[101] At Committee Stage, the Government made a number of amendments to the Bill.[102] These were summarised in Explanatory Notes when the Bill returned to the House of Commons, as follows:

> **Lords Amendment 12**
>
> 12. Lords Amendment 12 concerns the transfer of assets from the Royal Mail Pension Plan (RMPP) to the Government. The department expects assets to be transferred under Clause 20 from the RMPP in two tranches: the bulk at the 'relevant time' when liabilities are transferred; followed by a second transfer when actuarial calculations have been finalised. The second transfer will include adjustments to account for investment and market movement in the time since the initial transfer. Lords Amendment 12 ensures that these adjustments are disregarded when assessing the asset/liability ratio within the RMPP immediately before and immediately after the transfer.
>
> **Lords Amendment 13**
>
> 13. Lords Amendment 13 would ensure that information relating to pensions or other benefits under the RMPP or the new public scheme could be shared between the Secretary of State, the administrators of the new public scheme, the Trustees of the

[96] BIS Press Release, Government publishes Hooper Royal Mail update, 10 September 201-
[97] CWU Press Release, 'Privatisation is politically motivated', 10 September 2010
[98] 10 Downing Street website – Queen's speech – postal services bill
[99] *Postal Services Bill 2010 – Bill 78*
[100] HC Deb, 12 January 2011, c293-400
[101] HL Deb, 16 February 2011, c699-778
[102] HL Deb, 6 April 2011, c1723-46

RMPP (and any of the Trustees' administrators), and the employer. New subsection (4) would ensure that these information sharing arrangements would also apply to any section of the RMPP that is constituted as a separate pension scheme.

Lords Amendment 14

14. Lords Amendment 14 would allow the Secretary of State to commence any Order (or any provision of any Order) made under Part 2 of the Bill on a specified day by means of a commencement order.[103]

These amendments were debated in the House of Lords on 6 April 2011 and in the House of Commons on 9 June 2011.[104]

The *Postal Services Act 2011* received Royal Assent on 13 June 2011. The provisions regarding the pension scheme are in Part 2. The orders transferring the historic liabilities and assets to the Government took effect on 1 April 2012. The BIS website said:

> On the 9 March 2012 the Department laid the *Postal Services Act 2011 (Transfer of Accrued Pension Rights) Order 2012 - S.I. 2012/687* - in Parliament (http://www.legislation.gov.uk/uksi/2012/687/contents/made). This Order established a new government pension scheme (the RMSPS), provided for the rules of that scheme and amended the RMPP via a "Statement of Amendments". The Statement of Amendments is included in the related links section on the right. The operative provisions of the Order came into force on 1 April 2012 - the date designated by the *Postal Services Act 2011 (Specified Day) Order 2012 - S.I. 2012/966* - http://www.legislation.gov.uk/uksi/2012/966/contents/made.[105]

5.3 State Aid Approval

The Department for Business explained:

> During the final debate in the House of Commons today the Minister for Postal Affairs Edward Davey set out the next two crucial steps that need to be taken to secure the future of Royal Mail: obtaining state aid approval from the European Commission and changing the regulatory regime.
>
> The Minister confirmed that the Government intends to take on Royal Mail's historic pension deficit with effect from March 2012 as part of the preparations for a sale of the company. It also intends to restructure the company's balance sheet in due course. Royal Mail currently has around £1.7 billion of debt facilities with the Government. Ministers believe that for Royal Mail to be on a sustainable commercial footing going forward this will need to be restructured and Royal Mail's level of debt will need to be reduced substantially.
>
> The Government needs approval from the European Commission to provide this financial support and informal discussions have now begun with the Commission. The Government will submit a formal state aid notification in the next few days. It hopes that the process will be completed by March 2012.[106]

In July, the European Commission announced the opening of an in-depth investigation into state aid to UK postal operator Royal Mail:

---

[103] Bill 196 EN 2010-12
[104] HL Deb, 6 April 2011, c1723-46; HC Deb, 9 June 2011, c337-339
[105] BIS website – Royal Mail Pension Plan
[106] BIS Press release, Postal Services Bill agreed by Government, 9 June 2011

Brussels, 29 July 2011 - The European Commission has opened an in-depth investigation to ascertain whether UK plans to restructure the postal incumbent Royal Mail, by relieving it of its *'pension deficit'* and strengthening its balance sheet, are in line with EU state aid rules. At this stage, the Commission has doubts that Royal Mail's restructuring plan foresees adequate measures to mitigate any distortions of competition brought about by the state intervention and to ensure a sufficient own contribution to the cost of restructuring. The opening of an in-depth investigation gives interested third parties the possibility to comment on the measures under examination. It does not prejudge the outcome of the investigation.

Commission Vice President in charge of competition policy Joaquín Almunia said: "*The Commission acknowledges the importance of the reform of the postal market in the UK. However, we must ensure that the state measures do not provide undue advantages to Royal Mail as this would distort the conditions of competition among postal operators in the Internal Market*."

In June 2011, in the context of the reform of the postal services sector, the UK notified the Commission of its intention to relieve Royal Mail of its obligation to fund the accrued deficit of the pension fund that the UK claims is due to Royal Mail's status as public sector monopoly before 2006. The so-called pension deficit relief is estimated by the UK authorities at up to £8bn (around €9 billion). In addition the UK notified measures to strengthen Royal Mail’s balance sheet, including restructuring of the company’s £1.7 billion debt (around €1.9 billion) and the provision of a revolving credit facility.

The UK contends that the notified measures are in line with the EU Guidelines on state aid for rescuing and restructuring firms in difficulty (see MEMO/04/172). Alternatively, the pension relief could also be found compatible as legacy costs from the pre-liberalisation period, based on recent Commission practice.

However, at this stage, the UK authorities have not convincingly demonstrated that the submitted restructuring plan would comply with the guidelines. In particular, the Commission has doubts that Royal Mail’s role as the sole universal service provider and the liabilities resulting from its public sector monopoly legacy would justify mitigating the guidelines and notably the conditions ensuring that competition distortions are limited and that the cost of restructuring is shared by shareholders.

Moreover, the Commission has doubts whether the pension relief could be found compatible as compensation for an exceptional burden resulting from Royal Mail's past status as public sector monopoly. In 2007, the Commission indeed approved a French reform regarding the financing of the current and future pensions of the employees of La Poste with a civil servant status (see IP/07/1465). However, while the 2007 decision ensured that La Poste's effective social security costs were comparable to those of competitors, it seems at this stage that a large share of Royal Mail's pension deficit is due to the adverse conditions on the stock markets which have affected all UK undertakings alike. Furthermore, the Commission already approved measures to address Royal Mail's pension deficit, e.g. the creation of an escrow account which allowed Royal Mail to extend the period over which to fund its pension deficit (see IP/09/556).

The Commission is currently also examining measures in favour of the Belgian post incumbent bpost (see IP/09/1133) and the German postal incumbent Deutsche Post (see IP/07/1312). The scope of the investigation on Deutsche Post has recently been extended to cover the financing of certain pension costs (see IP/11/554).

> The non-confidential version of the decision will be made available under the case number SA.31479 in the State Aid Register on the DG Competition website once any confidentiality issues have been resolved. New publications of state aid decisions on the internet and in the Official Journal are listed in the State Aid Weekly e-News.[107]

On 9 September, the Commission gave interested parties one month to submit views.[108] The Communication Workers Union made a submission, explaining that it supported government intervention on the pension deficit and supported the application for state aid to allow this policy to be implemented.[109]

On 21 March 2012, the European Commission announced that it had approved UK plans to relieve the Royal Mail Group (RMG) from excessive pension costs relating to its past monopoly position and to provide RMG with restructuring aid

> **State aid: Commission approves pension relief and restructuring aid in favour of the Royal Mail Group**
>
> Brussels, 21 March 2012 - The European Commission has approved UK plans to relieve the Royal Mail Group (RMG) from excessive pension costs relating to its past monopoly position and to provide RMG with restructuring aid consisting of a debt reduction of £1089 million (around €1311 million). RMG's revised restructuring plan will ensure a sustainable future for the group in its twofold function of providing universal postal services and of granting access to its delivery network to other providers in the UK. Moreover, the plan negotiated with the Commission includes appropriate measures to minimise distortions of competition induced by the aid.
>
> Commission Vice President in charge of competition policy Joaquín Almunia said: "*In order to achieve a level playing field in postal markets, it is crucial that incumbent operators neither enjoy undue advantages, nor suffer from structural disadvantages in comparison with competitors. The relief of excessive pension costs and the restructuring aid approved today will help ensure this balance for Royal Mail and its competitors.*"
>
> The Commission's investigation found that RMG was liable for higher pension costs than its private competitors, as a consequence of legacy costs originating in the pre-liberalisation period, when RMG held a legal monopoly. The Commission therefore authorised the pension measure, under the condition that it only relieves RMG of costs which are in excess of the level of pension payments made by comparable companies in the UK. This will ensure that the pension relief does not place RMG in a better position than competitors. This decision is in line with the Commission's conclusions in previous postal cases (e.g. French Post, seeIP/07/1465, BPost, see MEMO/12/38 and Deutsche Post, see MEMO/12/37).
>
> The UK also plans to grant RMG a debt reduction amounting to £1 089 million in the context of a broad restructuring plan, aimed at ensuring the sustained viability of RMG. The revised restructuring plan, taking into account the Commission's concerns, will be implemented over 2010-1015. It foresees an improved business model for RMG which will better address its weaknesses and ensure its future viability. It builds on the significant restructuring that Royal Mail has already undertaken since 2002 to

[107] EC Press release, State Aid: Commission opens in-depth investigation into state aid to UK postal operator Royal Mail; Further information on State Aid can be found on the European Commission website. The Department for Business, Innovation and Skills has also produced a leaflet: *State Aid – a beginners' guide (June 2010)*.
[108] STATE AID — UNITED KINGDOM, State aid SA.31479 (11/C — ex 11/N) — State aid measures to Royal Mail. Invitation to submit comments pursuant to Article 108(2) of the Treaty on the Functioning of the European Union, (Text with EEA relevance), (2011/C 265/02)
[109] CWU Submission to the European Commission. UK – State Aid Measures to Royal Mail (SA 31479)

modernise its business and drive costs down. The plan includes operational modernisation, the offset of the remaining pension deficit of the RMG pension plan, which falls outside the legacy costs relief, and a structural reduction of mail centres. RMG will finance 50% of the restructuring costs through several measures, such as asset divestments.

The Commission therefore concluded that RMG's restructuring plan is in line with the 2004 EU Rescue and Restructuring Guidelines (see IP/04/856 andMEMO/04/172).

Background

RMG, 100% state-owned through the Royal Mail Holdings, provides the universal postal service in the UK and had a legal monopoly over certain basic letter services until the end of 2005 when the postal markets in the UK were fully liberalised.

RMG is the only licensee in the UK postal market with universal service obligations and is required by its license to allow customers and other postal companies access to its national network on a non-discriminatory basis.

In July 2011, the Commission opened an investigation on the proposed measures in favour of Royal Mail Group (see IP/11/936). Today's decision closes this investigation.

The non-confidential version of the decision will be made available under the case number SA.31479 in the State Aid Register on the DG Competition website once any confidentiality issues have been resolved. New publications of state aid decisions on the internet and in the Official Journal are listed in the State Aid Weekly e-News.[110]

5.4 Transfer of historic liabilities and assets to the Government

In its November 2011 *Economic and Fiscal Outlook report,* the Office for Budget Responsibility gave its view of the implications of transferring the historic deficit to the government.[111]

In the Budget 2012, the Government announced that it would transfer historic liabilities of around £37.5 billion to the Government and assets of £28 billion:

> **2.21 Royal Mail Pension Plan (RMPP)** – On 1 April 2012 the Government intends, subject to State aid approval, to transfer the historic liabilities of around £37.5 billion from the RMPP, a private sector pension scheme, to a newly established unfunded public pension scheme, the Royal Mail Statutory Pension Scheme. The liabilities will be treated as contingent in the National Accounts, but will feature in Whole of Government Accounts. An estimated £28 billion of assets will also be transferred to Government. These assets will be disposed of in a measured fashion, subject to achieving value for money for the taxpayer. The Government intends that the gilt holdings will be cancelled in 2012–13. The proceeds from sale of other assets will be transferred to the Consolidated Fund. (iii)[112]

The historic liabilities were transferred to a new public sector scheme (the Royal Mail Statutory Pension Scheme, RMSPS) to be administered by the government.[113]

[110] European Commission, State aid: Commission approves pension relief and restructuring aid in favour of the Royal Mail Group, 21 March 2012

[111] HC Deb, 19 Jan 2012, c923W; Office for Budget Responsibility, Economic and fiscal outlook, November 2011, Box 4.2

[112] HM Treasury, Budget 2012, para 2.21

[113] BIS website, Ensuring the future of the universal postal service and Post Office network services (viewed 18 July 2013)

The transfer had the effect of leaving the RMPP fully funded effect of leaving the RMPP fully funded as at 1 April 2012, i.e. at that date the assets held were sufficient to cover the liabilities.[114] The RMPP Trustee explained what this meant for scheme members:

> **RMPP benefits were split at the end of March 2012:**
>
> > **Benefits for pensioners, dependants and deferred members earned up to 31 March 2012 are now provided by the Royal Mail Statutory Pension Scheme (RMSPS)** which is a Government scheme. The RMSPS is not supported by a fund of assets but is backed by the Government. [...]
> >
> > **Employee members continue to be members of the Royal Mail Pension Plan. Benefits you have earned up until 31 March 2012 have been moved to the RMSPS.** We, as the Trustee for the RMPP, remain responsible for the pension benefits earned after 31 March 2012. [...]
> >
> > The Government has given the following commitments which we believe protect members' benefits:
> >
> > - your benefits have not been adversely affected by the transfer to the RMSPS;
> > - your benefits will be legally protected from future changes to the same degree as now;
> > - The Government will stand behind the transferred benefits; and
> > - The employee member benefits that the RMPP retained were fully funded at the time of the transfer.[115]

The Communication Workers' Union described it as "good news". General Secretary, Billy Hayes, said:

> - Today's announcement will protect the pensions of postal workers who have faithfully paid contributions for decades. We've consistently argued that the government has a moral obligation to take on the pension deficit, partly as owner of the company and for allowing Royal Mail to take a 13 year contributions holiday.
> - We remain strongly opposed to privatisation. Nationalising the debt and privatising the profit doesn't make sense. It's not in the interests of customers, workers or the taxpayer. Royal Mail is now £8.4bn better off and the case for privatisation weaker still.[116]

5.5 May 2013 - consultation on reforms to RMPP

In May 2013, Royal Mail Group (RMG) launched a consultation with members on a proposal to reform the RMPP. The proposal involved limiting the extent to which pay future increases would be pensionable. RMG said this would allow it to "commit to keep the Plan open to future accrual, subject to certain conditions, at least until the company concludes its next periodic review in March 2018." It said that although the transfer of historic liabilities and assets to Government had made members' past pensions considerably more secure, it had not addressed the cost of members' pension benefits from 1 April 2012 onwards:

[114] RMPP Summary Report and Accounts 2012
[115] RMPP Summary Report and Accounts 2012
[116] CWU Press Release, 'Good news for Royal Mail pensions' says CWU

Royal Mail has launched a consultation with Royal Mail Pension Plan members on a proposal which could allow it to commit to keep the Plan open to future accrual, subject to certain conditions, at least until the company concludes its next periodic review in March 2018. During that time there would be no changes to members' contribution rates, retirement age or accrual rates. Royal Mail would continue to make significant, annual contributions to the Plan of around £400 million every year.

Consultation

Royal Mail has been discussing its proposal with CWU and Unite on an informal basis. The company is now consulting its employees to gather Plan members' views on the proposals and help it to meet its legal requirement to complete the triennial actuarial valuation as soon as possible. The company sought to reach agreement with its trade unions on the pension proposal before beginning its employee consultation. Royal Mail will continue to seek agreement with both unions while the consultation is underway and will continue to listen to their feedback both during and after the consultation process. The company wants to reach agreement and strongly believes this proposal is the best option to protect members' pension benefits. The consultation is due to run until 25 August 2013.

The Royal Mail Pension Plan

Royal Mail is in a much better position than many other companies with regard to its Plan. At a time when other companies are closing their defined benefit schemes, the Plan has approximately £2 billion of assets which were left in the Plan following last year's transfer of the majority of the Plan's liabilities and assets to Government. The company understands how important the Plan is to its 112,000 active members. Defined benefit pensions are becoming increasingly costly for all the remaining employers who offer such a scheme because of conditions in the financial markets, including very low gilt yields. In fact the proportion of companies that closed their defined benefit schemes to existing employees climbed to 31 per cent in 2012. This is an increase of more than a third from 23 per cent in 2011.

The Proposal

Under the proposal, increases in the basic pay elements of member's pensionable pay under the Plan would (after accounting for the Lower Earnings Deduction for certain members) match RPI (up to five per cent) every year for Plan benefit purposes, regardless of whether members' actual basic pay goes up by more or less. This would allow the £2 billion of assets left in the Plan following the pension transfer last year to be used to help fund the gap between the company's contributions and the amount now required, because of increased costs, to keep the Plan open, at least until the company concludes its next periodic review. If Royal Mail can reach an agreement with the unions on its proposal then its intention is that this agreement would, subject to its conditions, be legally binding on the company regardless of any change of ownership, meaning that it would give members comfort in the event that Royal Mail is sold. This has been confirmed by Government and would be reconfirmed by Government at the time of any sale. In addition, if agreement can be reached with the unions, the company's intention is that it would (subject to the conditions of the agreement) absorb the estimated £75 million of additional annual employer's National Insurance contributions which would arise when 'contracting out' of the State pension scheme ceases in 2016, at least until the company concludes its next periodic review in 2018.

Why the proposed change is necessary

The transfer of almost all of the Plan's liabilities and assets to Government in April 2012 made members' past pensions considerably more secure. Unfortunately it could

> not address the cost of members' pension benefits from 1 April 2012 onwards. As part of the triennial actuarial valuation of the Plan, the trustee and the company are currently reviewing the cost of the pension members earn. This review could lead to the cost to the company of the Plan increasing by about £300 million each year from current levels. This is simply not affordable. It would effectively reverse the cash benefits to the company of the pension transfer. This action would be necessary irrespective of whether Royal Mail is sold or not - See more at: http://www.royalmailgroup.com/sale-royal-mail/pensions#sthash.ruGCFZeS.dpuf[117]

The Trustee wrote to plan members to explain that, faced with any proposal from the employer regarding benefit changes it would "consider what it believes is the best outcome for the membership as a whole in the circumstances."[118]

Deputy General Secretary of the Communication Workers' Union, Dave Ward said members were "entitled to be confused disappointed and angry" at the news and that the union would oppose any further attempt to change pensions arrangements by executive action.[119]

---

[117] Royal Mail Group website – Pensions (viewed 18 July 2013)
[118] RMPP letter to scheme members, The Trustee's role and approach to consultation, June 2013
[119] CWU Pension changes ring alarm bells, 30 May 2013