EXPLANATORY MEMORANDUM TO
THE RAILWAY PENSIONS (TRANSFER OF PENSION SCHEMES) ORDER 2007
2007 No: DRAFT

AND

THE RAILWAY PENSIONS GUARANTEE (PRESCRIBED PERSONS) ORDER 2007
2007 No.1595

1. This explanatory memorandum has been prepared by the Department for Transport and is laid before Parliament by Command of Her Majesty.

2. Description

2.1 The Railway Pensions (Transfer of Pension Schemes) Order 2007 (the "Transfer Order") transfers members from seven railway pension schemes (the "transferring schemes") into the 1994 Pensioners Section of the Railways Pension Scheme (the "1994 Pensioners Section") with effect from the effective date. It also transfers all the assets and the liability to pay pensions from the transferring schemes to the 1994 Pensioners Section.

2.2 The Railways Pensions Guarantee (Prescribed Persons) Order 2007 (the "Prescribed Persons Order") prescribes a class of persons whose membership of the 1994 Pensioners Section is to be disregarded for the purpose of determining whether that Section satisfies the conditions in paragraph 11(3) of Schedule 11 to the Railways Act 1993 (the "1993 Act").

2.3 The transferring schemes are as follows:

2.3.1 The London and North Western Railway Provident Society for providing pensions for widows and orphans of the salaried staff;

2.3.2 Great Western Railway Supplemental Pensions Reserve Fund;

2.3.3 The Great Western Railway Salaried Staff Widows' and Orphans' Pension Society;

2.3.4 The Great Northern Railway Superannuation Fund;

2.3.5 The Great Western Railway Inspectors and Foremen's Special Pension Fund;

2.3.6 The Southern Railway (South Eastern and Chatham Section) Enginemen & Motormen's Pension Fund Society; and

2.3.7 The B.R. (1974) Pension Fund (the "1974 Fund"), so far as it relates to persons who have rights under that Fund and at least one of the other transferring schemes, i.e. it is <u>not</u> a general transfer of that pension scheme.

3. Matters of special interest to the Joint Committee on Statutory Instruments

None

4. Legislative Background

4.1 The Transfer Order will be made under the powers in paragraphs 4 and 12 of Schedule 11 to the 1993 Act. The Prescribed Persons Order is made under paragraph 11(5) of Schedule 11 to the 1993 Act.

4.2 Article 4 of the Transfer Order provides for all the assets held by the transferring schemes to be transferred to the 1994 Pensioners Section. Article 5 of the Transfer Order modifies the operation of Articles 6(2) and 7(4) of the Railway Pensions (Protection and Designation of Schemes) Order 1994 (the "Protection Order") so that the Protection Order does not require a payment to the 1994 Pensioners Section in respect of the transfer of the relevant liabilities of the 1974 Fund made by this Order.

4.3 Article 5 of the Transfer Order has been made under paragraph 12 of Schedule 11 to the 1993 Act. The Secretary of State considers it expedient to modify the operation of the Protection Order in relation to the transfer of liabilities of the 1974 Fund. The reason is explained in paragraph 7.10 below.

4.5 The Prescribed Persons Order is made under paragraph 11(5) of Schedule 11 to the 1993 Act. Paragraph 11(5) permits classes or descriptions of person to be prescribed whose membership of, or participation in, a new scheme is to be disregarded for the purpose of determining whether the new scheme (in general terms, a scheme established under the Railways Act 1993) satisfies the conditions under which the Secretary of State shall or may give a guarantee to the trustees of a pension scheme in respect of pension rights under the scheme.

4.6 The guarantee is to be provided under paragraph 11(3) of Schedule 11. The Prescribed Persons Order is necessary in the case of the transfer into the 1994 Pensioners Section because some of the existing members of that Section were transferred into it by way of a deed and not by way of a transfer under paragraph 4 of Schedule 11 to the 1993 Act.

5. Territorial Extent and Application

5.1 This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

Mr Tom Harris, Parliamentary Under-Secretary of State has made the following statement regarding Human Rights:

> "In my view the provisions of the Railway Pensions (Transfer of Pension Schemes) Order 2007 are compatible with the Convention rights."

7. Policy background

7.1 The transfer envisaged by the Transfer Order is for the transfer of pension rights under six very old pension schemes (the "historic funds"), and the assets and liabilities of those schemes, into the 1994 Pensioners Section, and for the winding up of those schemes. The Order also provides that, where a person has rights under one of the historic funds and also has supplementary pension rights under the 1974 Fund, then those rights under the 1974 Fund will also transfer into the 1994 Pensioners' Section.

7.2 Where a surplus arises under the 1994 Pensioners Section, 40% of that surplus is distributed to the scheme members by way of benefit improvements and 60% is directed to a fund known as the Special Reserve Fund (the "SRF"). This fund is used to make up any future shortfall in pension funding under the 1994 Pensioners Section, and when the 1994 Pensioners Section is eventually wound up, any remaining funds will be applied at the discretion of the Secretary of State. At present, the SRF is sufficient to meet any deficit even after the transfer of liabilities effected by the Transfer Order. If in the future the SRF were to be insufficient to meet the liabilities of the 1994 Pensioners Section, then the Secretary of State would meet any shortfall under the guarantee issued by him.

7.3 As part of the transfer, the Secretary of State will also be entering into a transfer deed. This deed will extend the guarantee (referred to above) to cover the liabilities relating to all of the transferring schemes. Therefore, after the transfer, any shortfall in the funds which are being transferred will initially be met by the SRF and thereafter by a guarantee issued by the Secretary of State.

7.4 The main purpose of the proposed transfer is to achieve more efficient administration of the pension arrangements for railway pensioners. When pension schemes become very mature and the number of pensioners falls towards zero, the costs of managing those schemes become disproportionate to the assets of the scheme. In such circumstances it is prudent to take measures (either by amalgamation or by buyout) to simplify administration of the scheme and reduce its costs. For example the separate costs of producing annual reports and valuations will be saved.

7.5 In the case of the historic funds, the aim of the merger is to transfer all of the assets and liabilities of the historic funds, and the relevant liabilities of the 1974 Fund, to the 1994 Pensioners Section in order to improve the efficient administration of railway pensions. Furthermore, the 1994 Pensioners Section is a much larger scheme. It is therefore able to adopt an investment strategy which aims to achieve a better return on its investments (which in turn could result in improved benefits for members), and invest on terms that take advantage of its considerable economies of scale.

7.6 From the point of view of the 1994 Pensioners Section members, the transfer makes little difference. There are currently (as of early May) 2,942 members in the minor funds and 152,592 members in the 1999 Pensioners Section. The liabilities transferred represent about only 1% of the current 1994 Pensioners Section liabilities. In addition, the transferring liabilities, including the minor extra administrative cost, are more than covered by the transferring assets.

7.7 From the point of view of the members of the transferring schemes, the cost of administering the 1994 Pensioners Section will be much lower. There is also an improved prospect of enhanced benefits because the 1994 Pensioners' Section is not restricted to a cautious investment strategy and its rules permit a distribution of 40% of the surplus amongst members. The transfer will not affect the security of their benefits as all but one of the schemes has a Government guarantee. In the case of the Southern Railway (South East & Chatham) Enginemen & Motormen's Society, their members will have greater security as they do not currently benefit from a Government guarantee. Two of the historic funds currently have a surplus of assets over liabilities (The Great Western Railway Supplemental Pensions Reserve Fund and the Great Western Railway Inspectors and Foremen's Special Pension Fund) and, although there is little likelihood of any benefit improvements to the members of these funds if they remain as separate funds, the Secretary of State has agreed that these members should benefit from a one-off 4 percent

increase in their benefits on transfer to the 1994 Pensioners Section. The schemes' trustees are content that no prejudice to the members results from the transfer.

7.8 The transferring members are "protected persons". Where insufficient assets are transferred to meet the anticipated pension liabilities, the Protection Order requires that a payments be made (in this case by the Secretary of State and Stagecoach South Western Trains Limited) which are sufficient to cover the shortfall. This is calculated in accordance with requirements prescribed in Articles 6 and 7 of the Protection Order. “Top up” payments are expected to be made in respect of two of the historic funds which are not fully funded (the Great Western Railway Salaried Staff Widows' and Orphans' Pension Society and the Southern Railway (South East & Chatham) Enginemen & Motormen's Society).

7.9 The Secretary of State (with the agreement of the trustees of the 1994 Pensioners Section) considers it expedient to modify the operation of the Protection Order in relation to the transfer of liabilities of the 1974 Fund. The 1974 Fund is financed on a “pay as you go” basis”. If the operation of articles 6(2) and 7(4) of the Protection Order is not amended, it would require payment to be made to the trustees of approximately £7.4 million in respect of the transfer effected by Articles 3 and 4 of the Transfer Order. Such a payment is not considered necessary because the assets which are being transferred are more than sufficient to cover all the liabilities, including the liabilities in the 1974 Fund. In addition, there is considerable security available for members as a result of (i) the SRF (which is currently more than sufficient to cover any likely future shortfall even after the transfer) and (ii) the guarantee issued by the Secretary of State, which would be available to meet any shortfall in pension funding in excess of the SRF which might arise at a future date.

7.10 The Secretary of State is the Designated Employer of all the schemes involved, with the exception of the Southern Railway (South East & Chatham) Enginemen & Motormen's Society, where Stagecoach South Western Trains Limited is the employer by virtue of having the last active member in the Society. Currently, any costs which would be associated with this scheme would be reflected in the premium paid by a franchisee. The result of the transfer is that the future premium paid for the franchise should no longer reflect any expenses incurred in relation to that scheme.

7.11 The Railways Pension Trustee Company Limited is the trustee of all the schemes other than the Southern Railway (South East & Chatham) Enginemen & Motormen's Society, where Messrs TO Fielding, GW Lemar and RS Wilks are the current trustees.

7.12 In accordance with paragraph 4 of Schedule 11, the trustee of the 1994 Pensioners Section, the trustee of all the transferring schemes and the Pensions Committee of 1994 Pensioners Section have been consulted about and consented to the proposed transfer.

8. Impact

8.1 A Regulatory Impact Assessment has not been prepared for this instrument as it has no impact on business, charities or voluntary bodies.

9. Contact

Sue Waring at the Department for Transport (tel: 020 7944 3946 or e-mail: sue.waring@dft.gsi.gov.uk can answer any queries regarding the instruments.