JOHN RALFE CONSULTING

Ms Lesley Titcomb
Chief Executive
The Pensions Regulator
Napier House
Trafalgar Place
Brighton BN1 4DW

4th June 2015

Dear Ms Titcomb

Trafalgar House Pension Trust

I am writing to you, as the new Chief Executive of the Pensions Regulator, to ask that the Regulator formally examine the position of Trafalgar House Pension Trust (see appendix for legal structure etc).

Like many UK schemes, THPT, with 25,000 members, is in deficit; around £300m at March 2014 - £1.56bn of assets and around £1.9bn of FRS17 liabilities. But, unlike other schemes it is a "zombie scheme", with no employer standing behind making cash contributions to plug the deficit.

The sponsor, legally responsible for meeting its pension obligations, is Trafalgar House Trustees Limited, the pension trustee company, which is in turn owned by THPT. However, Trafalgar House Trustees Limited, has no operations, income or cash flow and there is no recovery plan for employer contributions.

With no employer contributions, THPT's trustees are betting on "investment outperformance" in high risk assets to plug the £300m deficit. Although 40 per cent of assets are in bonds and swaps to match liabilities, 60 per cent are in equities, private equity, hedge funds and property. The trustees plan to plug the deficit by 2024 by making an average annual return of gilts plus an astonishing 6 per cent on its high risk assets.

John Ralfe Consulting Limited
24 Devonshire Road, West Bridgford, Nottingham NG2 6EU
Tel: 0115 982 1911 07779 574193 JohnRalfe@JohnRalfe.com
www.JohnRalfe.com
Registered in England and Wales: Number 04724749

This extraordinary arrangement was approved by the Pensions Regulator in 2006, as its first major decision and allowed the sponsor, TH Global, to abandon its pension obligations, by agreeing to pay £101m into the scheme by 2012 – around £200m less than the FRS17 deficit at the time.

TH Global was the rump of the engineering group, Trafalgar House, bought by the Norwegian company, Kvaerner in 1996 and then sold in 2005 to an MBO. Since 2006, TH Global has paid £89m of the £101m, but the balance – which depended on a "work out"– was not paid.

The 2006 THPT deal seemed to take us back to the bad old days, when a company could just walk away from its pension scheme without ensuring it had enough assets to pay all its promised pensions. It prompted a series of questions in Parliament.

The Trustees' 2006 plan was to clear the deficit through "asset outperformance" by June 2014, but actual performance has been unimpressive – THPT would have done better simply holding all its assets in passive long dated index linked gilts.

Meanwhile, in the 8 years from 2006 to 2014 it has paid more than £100m in fees to 50 investment managers.

In 2006 THPT held 50/50 matching assets/high risk assets, but in 2009, after poor performance, it reduced matching assets to just 40 per cent and increased high risk assets to 60 per cent, in a desperate game of "double-or-quits".

Despite the absence of a real sponsor to underwrite the scheme, THPT is eligible for the Pension Protection Fund and when it (inevitably) enters the PPF, its deficit will be paid by other companies through a higher PPF levy. Meanwhile, it continues to pay pensions in line with its rules, not at the lower PPF level, so the PPF's losses increase the longer THPT continues. To add insult to injury THPT's PPF levy for 2014 is just £200,000 down from £1.2m in 2012.

I should also point out that THPT has an actuarial valuation as of March 2015.

In 2006 the architect and public face of this reckless game of "heads we win, tails the PPF loses" was Baroness Altmann, [1] now the new Pensions Minister; from being investment advisor she was then a Trafalgar House trustee from 2007 to 2010 and again from 2014.

In 2006, the Pensions Regulator also approved a "zombie" deal for Polestar Pension Scheme - the trustee company became the sponsor, with a similar plan to plug its deficit through high risk investment bets. In 2011, however, the trustees wound this up after the Regulator had told them to "*crystallise the position*" and warned it would use its powers to wind up the scheme if the trustees did not.[2]

The Regulator's subsequent Section 89 report on Polestar concluded that "*under any reasonable scenario the Scheme could never expect to pay the benefits promised to its membership [and] in the absence of an employer which could make payments to the Scheme, the PPF was ... exposed to a growing deficit"* [3] More generally *"the regulator would not expect any scheme to take excessive investment risk, unsupported by the employer covenant, and to the detriment of younger scheme members and the PPF*."

All of these comments apply verbatim to THPT- it is inconceivable it will be able to pay its pension promises, it has no sponsoring employer, it is taking huge investment risk and, meanwhile, the eventual hit to the PPF is increasing. As with Polestar, I believe the Pensions Regulator should tell the THPT Trustees to "*crystallise the position*" and warn it will wind it up if it does not. If the Regulator chooses not to do this it should produce a detailed public explanation of why not.

[1] http://www.ft.com/cms/s/1/71c0449e-1530-11db-b391-0000779e2340.html#axzz3aewV3RXj
[2] http://www.ft.com/cms/s/0/e43b2d74-8450-11e0-afcb-00144feabdc0.html#axzz3JzNWDlqc
[3] http://www.thepensionsregulator.gov.uk/docs/section-89-polestar.pdf

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sitate to ask any questions and I look forward to hearing

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in, PPF

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Appendix

1 **Trafalgar House Pensions Trust** (Reg No 101290901 "THPT") has around 25,000 members. At March 2014 it had assets of £1.56bn and FRS17 liabilities of around £1.86bn, so a deficit of c£300m.

2 Until 2006 THPT's legal sponsor was **Kvaerner plc** and its accounts showed the required FRS17 disclosures – a £250m deficit for 2004.

3 In 2006 THPT's legal sponsorship was transferred to **Trafalgar House Trustees Limited** (No 1604930 "THTL"), which became the Principal Employer. THTL is owned by THTP and is the Trustee of THTP.

4 Under the 2006 agreement, TH Global has made a series of cash payments to THPT, but there are no further cash payments to be made.

5 THTL has no operations or cash flow and minimal net assets and no ability to make deficit cash contributions. The intention is to plug the £300m deficit through superior investment returns. This arrangement was approved by the Pensions Regulator.

6 Since it became the Principal Employer in 2006 the accounts of THTL have made no reference to its pension obligations, although it is legally obliged to make good the pension shortfalls in THPT.

7 **Trafalgar House Pensions Administration Limited** (No 02997636) is owned by THTL, beneficially on behalf of THPT. It is "the current participating employer" in THPT.

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