

# The Pensions Regulator

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Rt Hon Frank Field MP  
Chair, Work and Pensions Committee  
House of Commons  
London  
SW1A 0AA

26 January 2018

Dear Mr Field

Thank you for your letter of 17 January 2018 regarding the Carillion defined benefit (DB) pension schemes. We note that the Work and Pensions and Business, Energy and Industrial Strategy Committees have announced a joint inquiry into what is clearly a worrying situation for all those affected and we stand ready to assist as required. In the meantime, we continue to work closely with all relevant parties, including the pension scheme trustees, the Pension Protection Fund (PPF), the Official Receiver and the Government to help achieve the best possible outcome for the pension schemes sponsored by Carillion and its subsidiaries. To address your specific questions:

- 1. Is TPR currently engaged in any investigative activity in respect of Carillion?**
- 2. Will TPR open an anti-avoidance case into Carillion?**

This is a complex situation where the scale, timing and impact of the group's profit warnings raise important questions. We are in contact with the FCA, FRC and Insolvency Service to determine what happened and what regulatory action may be appropriate. In relation to the pension schemes, TPR has launched an investigation to determine if there is information that suggests we should use our anti-avoidance powers. We also continue to work to facilitate the smooth transition of the pension schemes into the PPF whilst managing any residual risks to members and the PPF.

- 3. How did TPR react to the profit warning issued by Carillion in July last year?**

We have been involved in discussion with the trustees of a number of Carillion's pension schemes for a number of years as part of our role to review their long term funding.

Before the first profit warning in July 2017, we were already working with the trustee of the six DB schemes which shared a single trustee in relation to the 2016 valuation. These six schemes hold the majority of the DB memberships. In our proactive work of this sort, we typically seek assurances from trustees that they have sought appropriate advice and are adopting a robust negotiating position with the scheme employers on funding the scheme,

and that they are managing any downside risks, such as the risks presented by the scheme's investment strategy or an employer finding itself in financial difficulty.

Since the first profit warning in July 2017, we have had frequent and close contact with the schemes to ensure that members and the PPF are protected to the greatest extent possible. We contacted the trustees of all the thirteen DB schemes which are exclusively reliant on Carillion Group Plc to ensure that they had access to appropriate financial and legal advice given the increased likelihood of a restructuring. We have also had a series of meetings with senior executives from Carillion, their advisers, and major financial creditors. A consistent theme of our engagement in this type of situation is to ensure that the schemes are well prepared in the event of a restructuring proposal being made and, in particular, to ensure that all creditors will be treated equally as events unfold.

***4. Did TPR react to the profit warning about the sponsor's business model and potential material detriment to the pension covenant arising from business transactions?***

Following the profit warning, we urged the trustees to seek additional information as a matter of urgency and prepare themselves for a likely restructuring. In this type of situation, TPR's approach is to challenge trustees to ensure they have access to additional financial and legal advice appropriate to the circumstances, and to review the scheme's investment strategy to take account of the additional risks posed to members' benefits. Where needed, and given the pensions and restructuring expertise we have at our disposal, we will ensure that we provide clear feedback to trustees as to the approach they are taking and our expectations of them.

As explained above, in this particular situation, we have launched an investigation to determine if there is information that suggests we should use our anti-avoidance powers. Whether material detriment has occurred would normally form part of our consideration as to whether it would be appropriate to use our powers. However, the issuing of a profit warning following the payment of dividends does not, of itself, result in use of our anti-avoidance powers being appropriate.

***5. What regulatory contact has TPR had with Carillion pension trustees aside from usual/routine meetings around scheme valuations, a) before the profit warning and b) after the profit warning?***

At the time of the first profit warning in July 2017, we were proactively engaged with the six schemes which shared a single trustee in respect of their next scheme funding valuations (five of which had valuations as at 31 December 2016), in order to make clear our expectations and to influence the outcome ahead of their submission. In respect of our involvement following the profit warning, I would refer you to our responses to questions 3, 4 and 7.

***6. What is TPR's assessment of the reasons for the upsurge in the pension deficit?***

DB schemes are required to submit a valuation and, where the scheme is in deficit, a recovery plan to us every three years. They have up to 15 months from their scheme's valuation date to return this information to us. Valuation dates differ for the various Carillion

schemes. The most recent data returned to us relates to schemes with 2013 valuation dates and it is understood that the aggregate deficit for Carillion's pension schemes has grown since those submissions.

You will have read a variety of deficit figures being quoted in the press. It may be helpful to note that the c.£900m figure that has been quoted is based on the measure of the PPF's liabilities, whilst the figure of £587m is based on the accounting deficit which Carillion were required to reflect in their corporate accounts. These two measures are arrived at using different key financial assumptions and the PPF measure is usually (but not always) higher than the accounting measure. These two measures are therefore not easily comparable.

DB schemes have generally experienced challenging market conditions for several years and many schemes will have experienced an increase in their deficits. Gilt and bond market yields have remained low over a relatively long period in comparison to historical levels. Uncertainty remains around whether and when gilt and bond yields will revert to higher levels. This has generally led to an increase in the value placed on scheme liabilities. Whilst most major asset classes have performed well (which has led to an increase in scheme asset values) returns have not been to a sufficient level to compensate fully for the increase in liabilities. Many schemes are therefore likely to show larger funding deficits than reported at their last valuation.

Schemes (including the various Carillion DB schemes) will also have different investment strategies, benefit structures and membership profiles and hence their funding levels will have performed differently over the last few years. The trustees of each of the Carillion DB schemes will be best placed to provide a more detailed overview of the relative movements in the deficits of these schemes and the main drivers for those movements.

***7. Does TPR have concerns about the trustees' management of the schemes?***

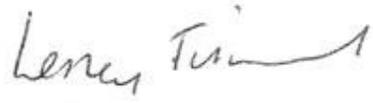
We have been closely engaged with the trustees, in particular of the six DB schemes that shared a single trustee given that they represent a high proportion of the total members. In the sort of circumstances which have arisen with Carillion, it would be usual for TPR to be more prescriptive in relation to our expectations of the trustee; for example, that they should only make decisions with the appropriate information and advice. In particular, we typically challenge trustees to make sure that they understand the risks in relation to the strength of the employer covenant, that any conflicts of interest are appropriately managed and that they and their professional advisers have the necessary experience in these types of situations.

***8. Were you aware of the Pension Ombudsman ruling against Mr Green, and do you have concerns about the extent to which his stewardship of Carillion took into account the interests of its pension scheme?***

We agree that strong corporate governance of sponsor companies is in the best interests of the DB pension schemes they support. However, it is not appropriate for us to comment on the actions of individuals, whilst TPR and a number of other authorities have investigations underway.

I hope this information is helpful to your Committee but please get in touch if we can be of further assistance.

Yours sincerely

A handwritten signature in black ink that reads "Lesley Titcomb". The signature is written in a cursive style with a long, sweeping horizontal line extending to the right from the end of the name.

Lesley Titcomb  
Chief Executive