# Unite submission to H M Treasury consultation on the Reform to Retail Prices Index (RPI) Methodology

**This submission is made by Unite, the UK and Ireland's largest trade union with over one million members across all sectors of the economy including manufacturing, financial services, transport, food and agriculture, construction, energy and utilities, information technology, service industries, health, local government and the not for profit sector. Unite also organises in the community, enabling those who are not in employment to be part of our union.**

In November 2019 Unite warned of a 'new wages crisis' and pensioners facing losing out on hundreds of pounds a year following the government's decision to scrap the Retail Prices Index[1]. We highlighted that one of the key differences between RPI and CPIH is which people they use to calculate expenditure. Inflation and how it is calculated matters to workers because it helps decide many aspects of our standard of living including wage increases. Unite will not let employers use this as an opportunity to short change our members and CPIH will not be an option for our collective bargaining.

In Unite's response to the ONS consultation on 'Measuring Consumer Prices' in September 2015 we pointed out why the RPI and CPI are different measures of inflation and why there are valid reasons for them to be different.[2]

We outlined why we believe the RPI is a better measure of the increase in prices and the reasons why it should be retained as the main uprating index, including consideration that it is currently by far the most used index by the private sector for uprating purposes and has a degree of familiarity and trust. The RPI is used in most wage negotiations in both the private and public sector.

This current consultation is the latest episode in a disgraceful and confused catalogue of initiatives to sabotage the RPI and impose the CPIH measure.

Unite concurs with the warning of the respected House of Lords Economic Affairs Committee that the UK Statistics Authority is at risk of being in breach of its statutory duties on the publication of statistics, by refusing to correct an error that it openly admits exists in the Retail Prices Index (RPI) and the Committee's call for the Authority to follow the procedure for

[1] https://unitetheunion.org/news-events/news/2019/september/unite-vows-to-fight-government-plans-to-scrap-rpi-and-stop-employers-cutting-pay-and-pensions/
[2] https://www.politicshome.com/ugc-1/1/4/0/unite_.pdf

correcting the error and, given that RPI remains in widespread use, resume a programme of regular methodological improvements[3].

Unite agrees with the TUC's view expressed in its evidence to the Lords Committee rejecting the charge that the RPI is fundamentally flawed, calling for an end to the constant attacks on the integrity of the RPI, and instead for the implementation of a positive initiative to renew the measure so that national statistic status can be restored.[4]

Serious damage has been done to the credibility of inflation measurements and the integrity of the institutions involved; this comes at a delicate time for the reputation of official bodies. In gaming the inflation measures used for uprating purposes the Government, and some companies, have exacerbated this situation and disadvantaged different sections of the public.

Over time the greatest disadvantage will be to wage earners, who are being inadequately compensated for changes in the cost of living. Even the process of wage negotiation is distorted with discussion side-tracked into the relevant measure of inflation rather than the appropriate increase relative to inflation.

The Lords Committee were unequivocal in their call for the clothing problem to be repaired:

> *"Fixing RPI: The present position of the Authority is untenable. Rather than pre-empting the decision of the Chancellor, it should fulfil its statutory duty to promote and safeguard the quality of official statistics and to do that, it should request a fix to the clothing problem."*

This proposal was supported by the Advisory Panel on Consumer Prices but rejected by UKSA and the National Statistician; the latter's reasoning for rejecting a fix is almost meaningless.

Unite contributed to and supports the submission made by the TUC to this latest consultation.

In the longer-term we support an upgrade to bring the RPI up to date. The developments associated with the RSS's preferred household cost index (HCI) – which is designed explicitly as an uprating rather than macroeconomic measure – provide an appropriate template (including, for example, more appropriate measures for owner occupiers' housing costs and student loan repayments).

Before this could happen, there should be a programme of work to ensure the HCI addresses the formula issue in an unbiased (or least bad) way. This process might be led by the RSS, who have offered valuable advice throughout the process and as an institution have emerged with their credibility and reputation enhanced.

**Pensions**

In respect of pensions, a pension scheme holds assets as collateral for pension promises. A pension promise may be inflation related or a fixed amount. If inflation related, there may be an explicit linkage to the RPI, the CPI, or to some other index (such as a sub-index of RPI or

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[3] https://www.parliament.uk/business/committees/committees-a-z/lords-select/economic-affairs-committee/news-parliament-2017/measuring-inflation-report-publication/

[4] http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/economic-affairs-committee/the-use-of-rpi/written/86883.html

Average Weekly Earnings). In a final salary scheme, the linkage to inflation while in service is to the personal salary growth of an active member.

A pension scheme may hold index linked gilts, which deliver an income stream growing in line with RPI, to support the payment of pensions with a variety of linkages to inflation. A switch of linkage from RPI to CPIH will result in a reduction in the annual increases applied to interest and capital payments. Pension schemes typically hold long dated gilts. A reduction in increases of 1% pa could result in a loss of index linked gilt asset value of around 20%.

Pension schemes own inflation related liability driven investment (LDI). LDI can involve a geared up exposure to index linked gilts. The loss of value on a LDI contract may be particularly severe.

Pension schemes have RPI linked liabilities. A switch of linkage from RPI to CPIH will result in a reduction in the annual increases applied to pensions. A reduction in increases of 1% pa could result in a decrease in the value placed on inflation related liabilities of around 20% (if there is linkage to RPI both before and after retirement). From the member's point of view, this is a 20% cut in the value of their pension.

Pension schemes have CPI linked liabilities, salary linked liabilities, fixed amount liabilities. A switch of linkage from RPI to CPIH has no primary effect.

A pension scheme may end up better off or worse off from the substitution of CPIH for RPI, depending on the nature of its assets and liabilities.

So the sponsoring employer may be made better or worse off, with positive or negative impacts for its business. If a pension scheme deficit does increase, this may lead to larger immediate cash contributions being required from employers in the short term.

In addition, a worsening of pension scheme funding may trigger a decision to increase the active members' contributions. It is increasingly common for an increase in the contribution rate to be shared between the employer and active members. This is an established process in some schemes. Such a decision has the potential to be intergenerationally unfair.

Pension schemes are hugely varied:

- there are schemes in which the pensions are almost wholly indexed to CPI, before and after retirement.
- there are schemes in which the deferred pensions and pensions in payment are almost wholly indexed to RPI.
- there are schemes in which the majority of the liabilities are of fixed amounts.

It would be unwise to attempt to summarise the position of a "typical" pension scheme – any one scheme may be very untypical. One point can however be made with confidence. For any scheme which holds any index linked gilts, the effect of a reduction in the inflation index used is a redistribution of wealth to Government and away from some combination of pension scheme sponsors and members. This is particularly of note given that regulation has increasingly encouraged pension schemes to hold (and leverage up) inflation linked gilts due to the need to "hedge their balance sheets" from valuation date to valuation date. Without that regulatory pressure, it is likely that pension schemes would use other assets that provide more general protection against inflation such as property, commodities and equities.

In combination the ONS and regulation have, in effect, caused pension schemes to buy something from Government that was, in hindsight, overpriced. The loss to pension schemes and their members is Government's gain. The reduction in the value of the UK government borrowing is around £100 billion, assuming that the impact is to reduce the rate of growth on the inflation measure used by 1% pa beyond 2030.

We must state very clearly the effect on pension scheme members with RPI linked benefits. The substitution of CPIH for RPI is a cut in their benefits. Over a lifetime, the cut may compound to be very substantial.

The proposed approach of simply substituting CPIH for RPI is not "fixing the flaws in RPI". "Fixing the flaws" would result in a continuing RPI, perhaps including reformed data collection processes. What is being proposed is the abandonment of RPI: the "new" RPI is a relabelled CPIH.

Simply substituting CPIH for RPI results in a discontinuous RPI index. This is statistically unsatisfactory. A significant merit of RPI for research purposes is its continuity for a long period of time.

It also results in a contractual sleight of hand. Any contract referencing RPI is materially altered by the substitution of CPIH for RPI, changing the balance of financial interests between the parties. Pension promises made based on RPI have been altered for the worse. The consultation document refers to the fact that a previous Chancellor noted that "the Authority's proposal to address the shortcomings in the RPI in this way "may be a more efficient approach then continuing to ask users to stop using it and rewriting existing contracts" ". Whilst this approach may be "efficient" it is unlikely to increase public trust or confidence in either Government or the UKSA.

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