Merseyside
PENSION FUND

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LOCAL GOVERNMENT PENSION SCHEME REFORM 2014

Wirral Council is responsible for the administration of the Merseyside Pension Fund which is part of the Local Government Pension Scheme (LGPS). Merseyside Pension Fund deals with the LGPS pension administration and investments on behalf of the five Merseyside District Councils, and over 100 other employers on Merseyside and elsewhere throughout the UK.

The Fund has over 45,000 active contributing members, 44,362 pensioners and just over 33,000 deferred pensioners. It is responsible for the investment and accounting for a pension fund of £5billion.

I refer to the employer consultation issued on 27 June in regard to the proposals for the new LGPS design, to take effect from 1 April 2014. I submit the following response on behalf of Wirral Borough Council in its capacity as the Administering Authority of the Merseyside Pension Fund (MPF). A formal response to the consultation by Wirral Council, in its capacity as an employer, will be made under separate cover.

MPF has, throughout the considerations of a new LGPS, recognised the requirement to ensure the affordability and ongoing viability of the Scheme; specifically the need to calibrate the cost of pension provision between the membership and employers.

Whilst good pension provision should be supported it is imperative that it is sustainable and that any revised package is equitable to all stakeholders.

1/ MEMBER CONTRIBUTION RATES

MPF has conducted numerous surveys of its membership and a clear, consistent preference has been made to increase normal retirement age (by linkage to State Pension Age) rather than any increase to member contributions, which could make the Scheme unaffordable. Consequently, MPF continues to strongly support any future arrangements which would result in fewer members wishing to leave the LGPS, helping to ensure that Funds remain sustainable via a broad active membership base.

The current proposals, if implemented, will see no contribution increases for the vast majority of members (with many low paid and part-time members actually seeing reductions). Furthermore, an improved accrual rate will see many members receiving higher benefits in retirement, which encourages Scheme participation.

2/ CAREER AVERAGE & NORMAL RETIREMENT AGE

The future proposal of Career Average with an accrual rate of 1/49th and CPI indexation has been costed on a broadly equivalent basis to the current 1/60th Final Salary Scheme - the main objective of this change to address the inequalities inherent in final salary arrangements for members with low earnings growth.

It would appear that the significant increase in accrual rates, (with 1/49th being 22.4% larger than 1/60th), combined with CPI revaluation, will be beneficial to certain groups of members, particularly those who tend to see no or only modest real increases in pay (i.e. the majority)

However it is imperative that the alignment of Normal Retirement Age to State Pension Age, with the intended link to longevity, is managed with diligence as it is this link which is the main cost savings emanating from the proposals.

3/ PENSIONABLE PAY

The change to include non-contractual overtime as actual pensionable pay will have a significant impact on budgets for employers where such overtime constitutes a substantial element of the payroll.

4/ THE 50/50 OPTION

This 50/50 proposal is a positive step from the members' perspective as it eases both the contribution burden in the current economic climate and potentially the incidence of optant-outs from the LGPS in the longer term.

This option could initially increase cash requirements for employers due to the improvements in expected Scheme take-up rates. Although the cost is lower for this benefit it is still more than the nil cost that otherwise would have been from the case of non-participation. Conversely, the improvements in the membership profile would result in lower contribution rates at subsequent valuations and would assist in maintaining optimistic funding parameters.

It is evident that this option poses significant administrative issues for Funds and employers. In particular, consideration needs to be given to whether, as part of the actuarial valuation; employers would be offered dual future service rates, split between the main scheme and the 50/50 option. If the current arrangement of a single future service rate is maintained, then any savings would not emerge immediately and would not take effect from the 2013 valuation unless a specific assumption is introduced on the perceived take-up of this option.

The documentation provided suggests that the applicable employer contribution rate is the same irrespective of the differences in the accrual rates. However, the regulations currently provide the actuary with the power to set the rates as appropriate.

It would appear that the low cost option meets the criteria as a qualifying scheme and specific regulatory provision is required to designate the main Scheme arrangement as the default for the purposes of Auto-Enrolment and to legally facilitate the member's re-enrolment in the main Scheme.

5/ COST SAVINGS FROM PROPOSALS

Although the headline savings are stated to be in the order of 2% of pay in comparison to the current Scheme, it is important that employers understand that these savings may not necessarily apply.

Whilst the average trend may apply to councils, some employers with large numbers of older, lower paid members working non contractual overtime may find that the new proposals actually increases employer participation costs.

In managing expectations, it is also important for employers to understand that the contributions required to fund any past service deficits are not included in the overall cost envelope of 19.5% of pay. It is a foregone conclusion that in the current volatile economic environment the impact of deficits could remove or even outweigh any apparent saving from the new Scheme.

6/ FUTURE COST MANAGEMENT

The major focus of reform has been on the initial benefit design; however, future cost management is crucial to the long term sustainability of the Scheme. Theoretically, linking the Normal Retirement Age to State Pension Age will lead to an inbuilt barometer that reacts to emerging changes in longevity.

The cap-and-collar mechanism will influence the cost and structure of the Scheme more readily and will provide the necessary agility in maintaining an equitable calibration of costs between members and employers.

7/ COMMUNICATIONS

It is essential that during this process of reform, due consideration is given to the operational aspects of delivery, in particular the communication and administrative requirements facing both Funds and employers.

Employers need to be engaged and participative in the communication of Scheme reform to their employees. Whilst MPF and other Funds will develop communication strategies and plans over the coming months, any support and direction by the LGA and government departments would be welcomed and appreciated. It is also important that it is recognised that Funds will need to be appropriately resourced to carry out this communication task.

8/ ADMINISTRATION

Migration from one benefit package to another presents a major challenge to the administration of the Fund; both at employer and Fund level. The complexities of the proposals will require a greater number of pay bands for contribution-setting purposes. Furthermore, a mix of final salary and CARE benefits, a change in accrual rate and different pensionable pay definitions, create a number of operational difficulties to overcome and will require an increased level of administrative resource.

It is essential that the detail of the new Scheme is known as soon as possible, in order that software providers and operational processes can be developed to cope with the burden of running the separate benefit structure/calculations. As auto-enrolment responsibilities need also to be addressed and delivered, it is paramount that planning, resourcing and implementation commences upon the general acceptance of the proposals.

9/ COUNCILLOR SCHEME

To avoid further complexity and confusion it would appear opportune to move Councillors within the general scope of the 2014 Scheme. This would be both equitable to the members and to alleviate some of the administrative burden of running two different CARE pension benefit Schemes.

MPF believes the proposed package meets the long standing objective of the government for employers to provide good pension provision, which is valued by the employee and affordable to both.

The general intent to limit member contribution increases in exchange for a later retirement age is reasonable, but it is only through the appropriate application of the cap-and-collar mechanism that future sustainability can be sought. The 50/ 50 option together with the improved accrual rate is attractive to employees and should encourage member participation ensuring continuing financial viability.

Yours sincerely

Tom Sault

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cc. Jeff Houston, Head of Pensions - LGA