WIRRAL COUNCIL

PENSIONS COMMITTEE

16 NOVEMBER 2010

REPORT OF THE DIRECTOR OF FINANCE

PUBLIC SERVICE PENSIONS COMMISSION

1. EXECUTIVE SUMMARY

1.1. This report informs Members of the interim report published on 7 October 2010 by the Public Service Pensions Commission headed by Lord Hutton.

2. BACKGROUND

2.1 The Pensions Committee considered the creation of the Public Service Pensions Commission on 27 September 2010 (Minute 29 refers).

2.2 The Public Service Pensions Commission has been tasked with conducting a fundamental review of public sector pension provision and has been asked to make recommendations to the Chancellor and Chief Secretary on pension arrangements. The Commission has been invited to produce a final report in time for the Budget 2011, but was also tasked with producing an interim report. A copy of the Treasury press release for the interim report is attached for information (Appendix 1).

The Public Service Pension Commission Interim Report

2.3 The interim report was published on 7 October 2010. The terms of reference also invited the Commission to consider the case for delivering savings on public service pensions within the spending review period of 2011-15.

2.4 The report states that public service pension schemes are a valuable recruitment and retention instrument, which also provide a reasonable standard of living at retirement without becoming a burden on the welfare state. The report also rejected the claims that public service pensions are “gold plated”. Nonetheless, Lord Hutton points out that the status quo is not tenable. Further reform is necessary in order to strike a fairer balance, not just between current tax payers and public service employees, but also between future and current generations. He does, however reject a “race to the bottom” approach by following the private sector decline in pension provision. The report does state that it would not be desirable to move towards a funded, individual defined contribution model.

Short-term options

2.5 The report considers a range of options for making short-term savings and concludes that the most effective way to do so is to increase member contributions. The Commission believes that it is a matter for the Government to decide the manner and level of any necessary contribution increases but that any increase should provide some measure of protection for the low paid. In the Spending Review on 20 October 2010 the Government indicated that increases to public sector employee pension contribution rates should be phased in over three years from 2012 -13 to 2014 -15.

Long-term

2.6 The report has concluded that the necessary longer term structural reform cannot be achieved via traditional final salary defined benefit (DB) pension schemes, which are considered to primarily reward high earners who may also have a longer life expectancy. It is also suggested that final salary schemes do not provide a robust and fair mechanism for the majority of the public sector workforce.

2.7. The long-term reform recommendations that the Commission will be making in its final report to the Government will be based on the following set of principles: -

- Affordable and sustainable;
- Adequate and fair;
- Support productivity;
- Transparent and simple.

2.8. In the final report the Commission will examine other international public sector pension models but will also look at other pension arrangements which share the risk between employee and employer. These will include:

- Career average defined benefit schemes;
- Notional Defined Contributions (DC) schemes with added protections that, while not being funded, still determine the value of benefits at retirement by an assumed return on contributions and annuity rates.
- Collective DC schemes where all contributions are placed in one fund that is then managed on behalf of members. Members' pensions will vary according to the underlying investment performance. However, this gives an option to use inter-generational sharing to smooth the effects of market conditions;

- Cash balance schemes where the employer puts a notional amount into the member's pot every year, which is then guaranteed. This credit can be expressed as a percentage of salary for each year worked. If cash contributions from the employee and employer, plus investment returns do not match the promised guarantee then the employer will have to meet any shortfall.
- Sequential hybrids (or nursery schemes) which have more than one section or part where a member may earn both a DB pension and DC pension during their career with an employer. Members, would however, be earning either DB or DC benefits at any one time.
- Capped DB schemes, where there is a limit on the amount of salary that counts for pension purposes or on pension payments from the scheme; and
- Combination hybrids, where members simultaneously earn benefits that are part DB and part DC. For example, a capped DB pension, based on earnings up to a certain level and a DC benefit on earnings above this level.

3. OTHER MATTERS

3.1. The Commission has concluded that the LGPS should remain a funded scheme.

3.2 The Commission will in its final report consider pension scheme administration costs and the scope for rationalisation and cost reduction. This will include possible simplification and consolidation of functions across different schemes and units within a scheme.

3.3 Existing rights

As far as the accrued rights of existing members are concerned the Commission will be considering the extent of those accrued rights, their protection and the implications for future pension terms. The Commission is clear that protecting accrued rights does not extend as far as protecting current terms for future pension accrual.

3.4 Fair Deal

The Commission believes the evidence presented to it makes clear that current pension structures, combined with the requirement to provide comparable pension ("Fair Deal") are a barrier to outsourcing public service provision. The Commission does not appear to accept that the LGPS approach to this by offering admitted body status to contractors provides a long-term, sustainable solution for the public sector. The Commission will address this issue in its final report. The Government is to carry out a further consultation on the Fair Deal policy.

3.5 Additionally, the Commission is interested in gathering further views on public service pensions to inform the final report at Budget 2011. The Commission will therefore be issuing a second call for evidence, asking for contributions by early December 2010.

4. FINANCIAL IMPLICATIONS

4.1 The outcome of this review is likely to have significant financial implications for all stakeholders in the Local Government Pension Scheme and other public sector pension schemes should the Government accept and act upon the recommendations.

5. STAFFING IMPLICATIONS

5.1. There are none directly arising from this report.

6. EQUAL OPPORTUNITY /EQUALITY IMPACT ASSESSMENT

6.1. There are none arising from this report.

7. COMMUNITY SAFETY IMPLICATIONS

7.1. There are none arising from this report.

8. HUMAN RIGHTS IMPLICATIONS

8.1. There are none arising from this report.

9. LOCAL AGENDA 21 IMPLICATIONS

9.1. There are none arising from this report.

10. PLANNING IMPLICATIONS

10.1. There are none arising from this report.

11. MEMBER SUPPORT IMPLICATIONS

11.1. There are none arising from this report.

12. BACKGROUND PAPERS

12.1. The interim report of the Public Service Pensions Commission - 7 October 2010.

13. RECOMMENDATION

13.1 That Members note the report.

IAN COLEMAN
DIRECTOR OF FINANCE

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