Firefighters' Pension Schemes (England)

A guide for fire authorities (in England) when calculating pension forecasts for the Firefighters' Pension Top Up Grant

July 2019

1. Introduction

1.1 The collection of accurate annual pension forecast data is critical to the Home Office (HO) for ensuring sufficient budget cover is secured to make pension top up grant payments to fire authorities each year. Poor quality forecasts represent significant financial risk to HO accounts and it is important that steps are taken to ensure these risks are reduced as much as possible.

1.2 Top up grant pension forecasts, by their very nature, carry an inherent risk due to the uncertainty and volatility of future pension income and expenditure streams. The National Audit Office (NAO) has advised that this uncertainty is exacerbated in the fire sector as fire authorities do not follow a consistent approach to forecasting.

1.3 Following this advice, the HO and Local Government Association (LGA) jointly established a Pension Forecasting Working Group (PFWG) comprising of employer representatives from the Fire and Rescue Service who are directly involved in the top up grant pension forecasting process. The PFWG was asked to:

- consider the different methodologies that fire authorities can use to forecast each pension data set;
- consider the scheme information that is necessary to feed into forecast calculations e.g. scheme membership, retirement dates etc. and the difficulties of obtaining this information; and
- suggest potential actions/approaches to help remove or reduce uncertainties and improve the overall quality of the forecasts.

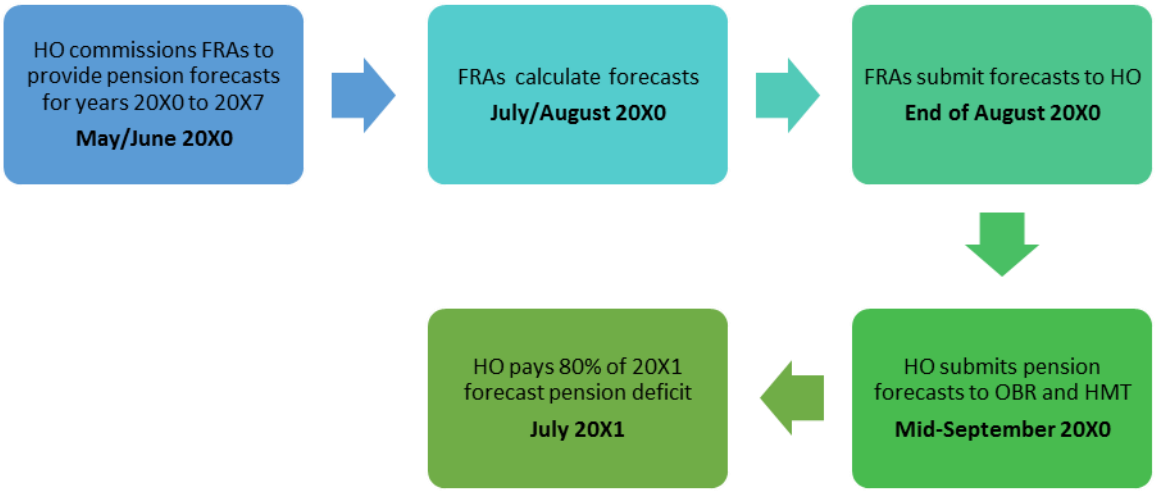
1.4 Following its discussions, the PFWG drafted this sector led guidance to support fire authorities with the top up grant pension forecasting process and to introduce a more consistent approach to pension forecasting within the Fire and Rescue Service.

1.5 The guidance is informal and there is no mandatory requirement to adhere to it. Where the accuracy of forecasts falls outside of the acceptable margins, fire authorities will continue to be asked for mitigation. This may include details of the approach taken.

1.6 This guidance will be reviewed annually by the PFWG to ensure it remains up to date and relevant.

2. Top Up grant pension forecasting process

2.1 The overarching timetable for the top up grant pension forecasting process is set out below.



2.2 Each year the HO commissions fire authorities to submit pension forecasts for the following seven financial years. The pension forecasts for the financial year following the collection are used to make an initial assessment on each fire authority's annual top up grant entitlement for that year**. It is essential that these forecasts are as accurate as possible to ensure that the HO secures sufficient budget cover to make the associated top up grant payments to fire authorities.**

2.3 The pension forecasts for the full forecasting period are also reported back to both HM Treasury and the Office for Budget Responsibility (OBR) to be used for the Autumn Budget considerations.

2.4 As part of the top up grant forecasting process, fire authorities apply central assumptions prescribed by the OBR. These are:

i. Consumer Price Index rates to be used when uprating annual pensions in payment during the full forecasting period; and
ii. Wage inflation rates to be used when uprating annual pensionable pay for scheme members.

2.5 Fire authorities apply their own local workforce assumptions relating to expected recruitment, retirement rates, ill-health retirements etc. and consider the impact on their future annual pension income and expenditure streams.

2.6 The HO commissions the forecasts in June/July each year with a deadline for response in late August. The forecast return is submitted on the DELTA online data collection site. It is important that fire authorities plan for this work and allocate sufficient resources to ensure this deadline is met to guarantee a timely top up grant payment.

2.7 On receipt of the returns, the HO scrutinises the data submitted by each fire authority and undertakes cross-reference checks with previous forecast/actual pensions data submitted. Where variances exist that exceed expected tolerance levels, fire authorities will be asked to provide a detailed explanation setting out the underpinning causes.

2.8 All forecast data is also scrutinised in detail by the NAO and OBR. Fire authorities may be asked to attend challenge meetings, chaired

by HO officials, where their forecast returns consistently fall below expected standards.

3. Calculating financial forecasts

3.1 There are currently four fire pension schemes: the 1992, 2006, 2015 and the 2014 Modified Scheme[1]. To provide high quality top up grant forecasts, forecasters will need access to specific workforce data to feed into their pension forecast calculations for each of the pension schemes. Forecasters should work closely with their HR, payroll and pension administration teams to determine future recruitment plans, expected retirement rates, scheme opt-out rates and employee turnover rates etc.

3.2 Whilst not exhaustive, a list of the specific workforce data that forecasters will need to obtain / derive / estimate to feed into their forecast calculations is set out in **Annex A**.

3.3 Fire authorities provide annual forecasts for each individual pension income and expenditure stream for each fire scheme during the forecast period. These have been set out below, along with recommendations made by the PFWG.

3.4 *Pensionable Pay* – As part of any sound forward looking finance plan, fire authorities will be aware of the pensionable pay that they expect to pay in respect of scheme members they employ. The level of total pensionable pay for each scheme will be affected by factors such as the number of annual retirements (both ordinary and ill-health),

[1] *The provisions of the 2014 Modified Scheme are incorporated within the 2006 Firefighters' Pension Scheme's legislation*

membership opt out rates, employee turnover, new recruitment levels, wage inflation and earnings profile of scheme membership. It is necessary for fire authorities to consider the impact of each of these factors on pensionable pay levels each year.

3.5 It is key that fire authorities can identify the number of members in each scheme and the pensionable pay that each member earns for each year of the forecasting period. It is also necessary to consider the annual movement in scheme memberships i.e. the number of employees that exit the schemes each year (by either retiring, opting out or leaving employment) and the net effect of these on pensionable pay levels in each scheme.

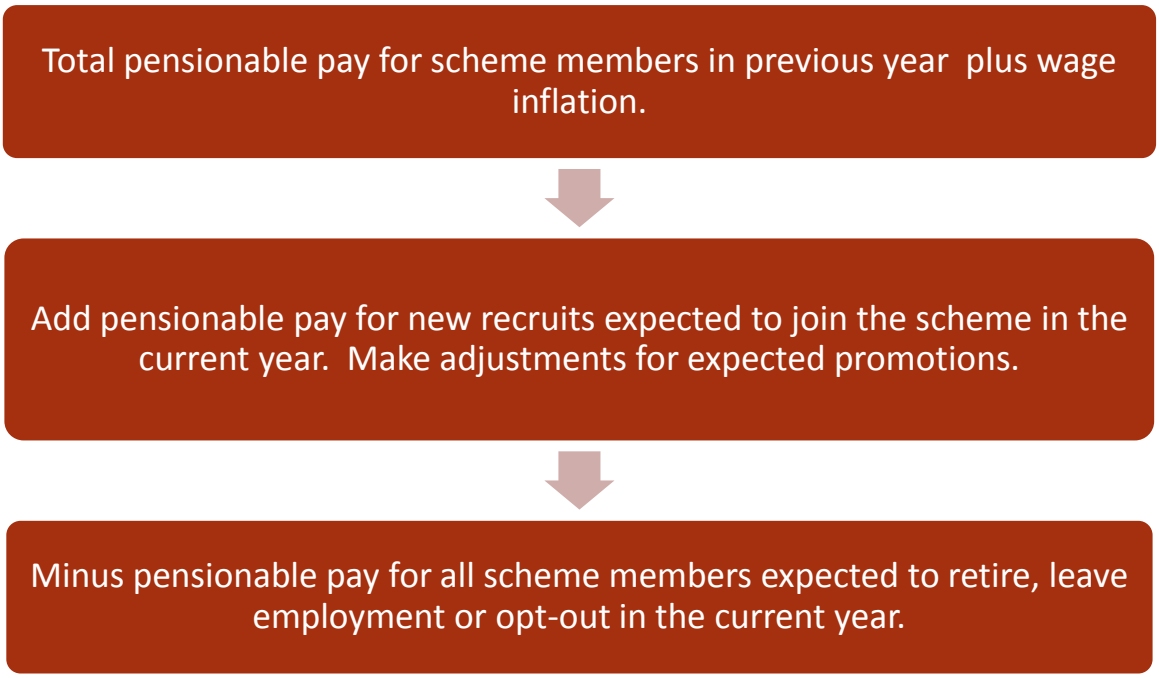
3.6 To estimate the annual pensionable pay levels for each scheme, fire authorities should identify:

- the membership numbers in each scheme throughout the forecasting period (taking account of the aforementioned factors).
- the pensionable pay that each member receives, to include promotions (taking account of the centrally prescribed wage inflation assumptions – see paragraph 2.4).

3.7 To identify the movement of membership numbers as above, the PFWG discussed that smaller fire authorities (less than 1000 employees) would look at experience of individuals, whereas larger fire authorities (more than 1000 employees) would use averaged experience. However, the methodology would depend on the level of

information available to finance. It was considered good practice for fire authorities to involve HR in this process.

3.8 To estimate the annual pensionable pay levels for each scheme during the forecasting period fire authorities should use the following calculation method:



3.9 This pensionable pay calculation can then be repeated for each of the subsequent years of the forecasting period.

Pensions Income

3.10 The elements of pensions income that fire authorities forecast are:

- Employer contributions;
- Employee contributions;
- Ill-Health Charges;
- Transfers In; and

- Other Miscellaneous income.

3.11 *Employer contributions* – This is the amount of employer contributions each fire authority pays in respect of the scheme members that they employ. Each of the four fire pension schemes have bespoke employer rates. The current employer contribution rate for each scheme is as follows:

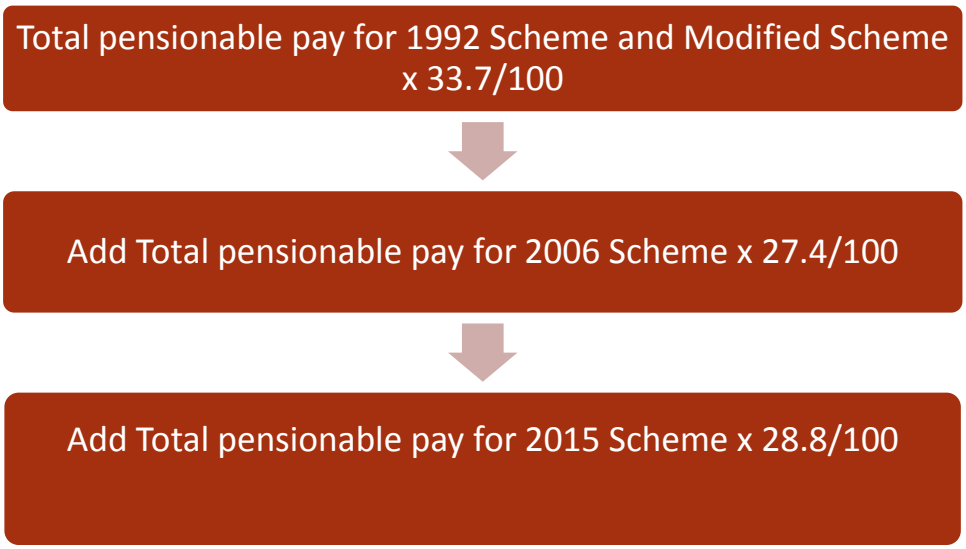
1992 Scheme – 37.3% of member's pensionable pay

2006 Scheme – 27.4% of member's pensionable pay

2015 Scheme – 28.8% of member's pensionable pay

Modified Scheme – 37.3% of member's pensionable pay

3.12 To estimate/forecast the annual income from employer contributions for each scheme during the forecasting period the **PFWG recommends** using the following calculations:

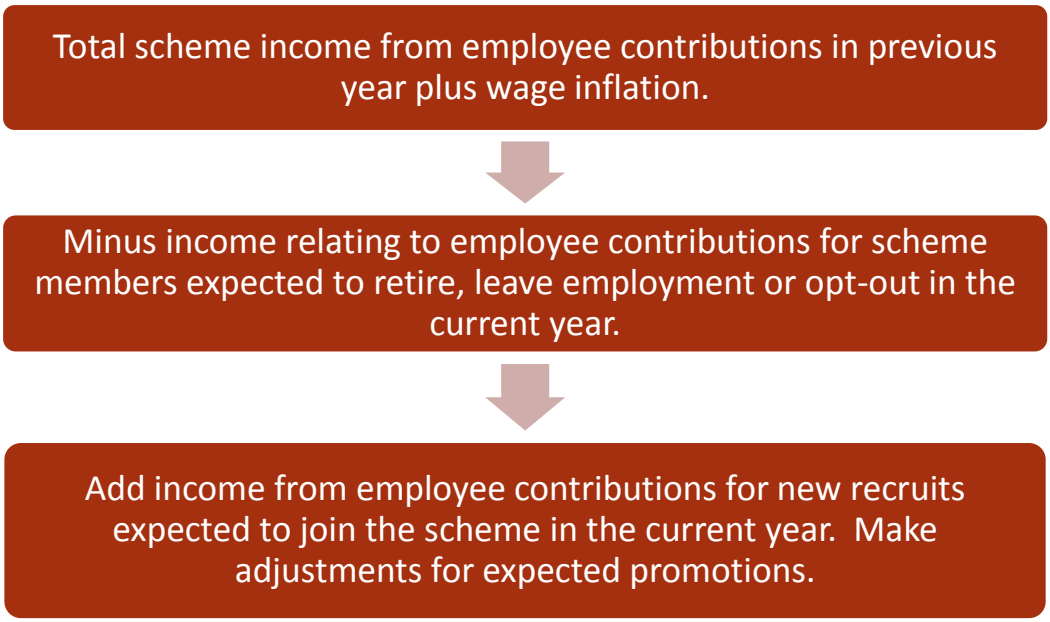


3.13 *Employee contributions* – Each of the four fire pension schemes operates tiered employee contribution rates which means that the contribution rate that an employee pays is determined by the amount of the pensionable pay they receive each year. The current tiered employee contributions rates for each scheme are attached at **Annex B**. The key to accurately estimating employee contributions is forecasting the pensionable pay levels for each member of each scheme.

3.14 To estimate / forecast the annual income from employee contributions for each scheme, fire authorities should identify the fire scheme that each employee is a member of and the pensionable pay that they receive for each year during the forecasting period. This information will allow fire authorities to estimate the total income that they expect to receive from employee contributions by applying the appropriate employee contribution rates.

3.15 Fire authorities should monitor annual changes in the number of members in each scheme taking into consideration retirements (both ordinary and ill-health), opt outs, employee turnover rates, promotions and recruitment; and the pensionable pay that they receive for each year of the forecasting period. This is especially relevant during the period that the 2015 Scheme transitional arrangements are in place as the contribution rate that a member pays will change when they move across to the 2015 Scheme.

3.16 To calculate the annual income from employee contributions for each scheme during the forecasting period the **PFWG recommends** that fire authorities use the following calculation method:



3.17 *Ill-health Charge (IHC)* – Fire authorities make a payment from their operational accounts to their local pension fund account for each employee that they ill-health retire. The payment equates to 2 x member's pensionable pay for a lower tier ill-health retirement; and 4 x member's pensionable pay for a higher tier ill-health retirement. The payment is spread over three years in equal annual instalments.

3.18 To accurately forecast annual income from IHCs, fire authorities need to be able to predict the number of ill-health retirements they expect in each year during the forecasting period, the type of ill-health retirement (i.e. lower or higher tier) and the amount of pensionable pay that each retiree was receiving at the point of ill-health retirement.

3.19 The **PFWG recommends** that in the absence of any robust information to inform forecast ill-health retirements, fire authorities should calculate the average IHC paid over the previous 5 years[2] by using the following calculation method:

[2] At the time of forecasting the IHC for 2020/21, FRAs will not know the actual IHC paid in 2019/20.

$$\text{Forecast IHC in } 2020/21 = \frac{\text{IHC } 2014/15 + \text{IHC } 2015/16 + \text{IHC } 2016/17 + \text{IHC } 2017/18 + \text{IHC } 2018/19}{5}$$

The average estimated IHC for the first year of the forecast period can then be projected forward using an appropriate index e.g. wage growth.

3.20 *Transfer Values In (TVs in)* – Fire authorities may receive a request from existing scheme members to transfer pension benefits from an external pension arrangement into the fire pension schemes. Where such a request is accepted, the fire authority is required to pay the cash received into their local pension fund account. As with ill-health retirements, the number of TVs in can be volatile and difficult to predict in any year.

3.21 The **PFWG recommends** that in the absence of any robust information to inform forecast income from TVs in, fire authorities should calculate the average value of TVs in, received over the previous 5 years[3] by using the following calculation method:

$$\text{Forecast TVs In } 2020/21 = \frac{\text{TVsin}2014/15+\text{TVsin}2015/16+\text{TVsin}2016/17+\text{TVsin}2017/18+\text{TVsin}2018/19}{5}$$

The average estimated TVs in for the first year of the forecast period can then be projected forward using an appropriate index e.g. wage growth.

[3] At the time of forecasting income from TVs in for 2020/21, FRAs will not know the actual income received from TVs during 2019/20.

3.22 *Other miscellaneous Income* – There are other miscellaneous elements of pension income that fire authorities need to forecast for each year of the forecasting period. For example, annual payments made by fire authorities to their local pension fund accounts where they (the employers) have initiated early payment of a 2006 Scheme or 2015 Scheme member's pension; chosen not to abate a 1992 or 2006 scheme members pension on re-employment; or where the fire authority exercises its discretion to allow certain 1992 Scheme members to commute their pension for a lump sum of more than 2.25 x pension. Fire authorities need to have a robust methodology to forecast this income.

3.23 The **PFWG recommends** that in the absence of any robust information to inform forecast miscellaneous income, fire authorities should calculate the average miscellaneous income received over the previous 5 years[4] by using the following calculation method:

$$\text{Forecast MiscInc}20/21 = \frac{\text{MiscInc}14/15+\text{MiscInc}15/16+\text{MiscInc}16/17+\text{MiscInc}17/18+\text{MiscInc}18/19}{5}$$

The average estimated miscellaneous income for the first year of the forecast period can then be projected forward using an appropriate index e.g. wage growth.

Pensions expenditure

3.24 The elements of pensions expenditure that fire authorities are required to forecast are:

[4] At the time of forecasting miscellaneous income for 2020/21, FRAs will not know the actual miscellaneous income received during 2019/20.

- Annual recurring pension payments;
- Commutation lump sum payments;
- Transfers Out; and
- Other miscellaneous expenditure.

3.25 *Annual recurring pension payments* – Fire authorities make recurring pension payments in respect of retired scheme members from their local pension fund account. This represents a significant proportion of the fund's annual expenditure and, as such, it is important that fire authorities forecast this accurately.

3.26 To accurately forecast expenditure on annual recurring pension payments it is key that fire authorities determine the number of pensioners (including survivor pensioners) and the value of their annual pensions for each year during the forecast period – this includes the number of deferred pensions that are due to come into payment each year. It is also important to forecast the number and value of pensions in payment that will cease due to death and how many of these deaths will generate additional survivor pensions.

3.27 To estimate the number of new retirements each year, fire authorities need to engage with their HR/pension administration teams to identify those scheme members that have or will have an entitlement[5] to retire with immediate access to a pension during each year of the forecasting period. It is recognised that those members who have an entitlement to retire will not necessarily retire in the year that their entitlement arises and that this creates uncertainty.

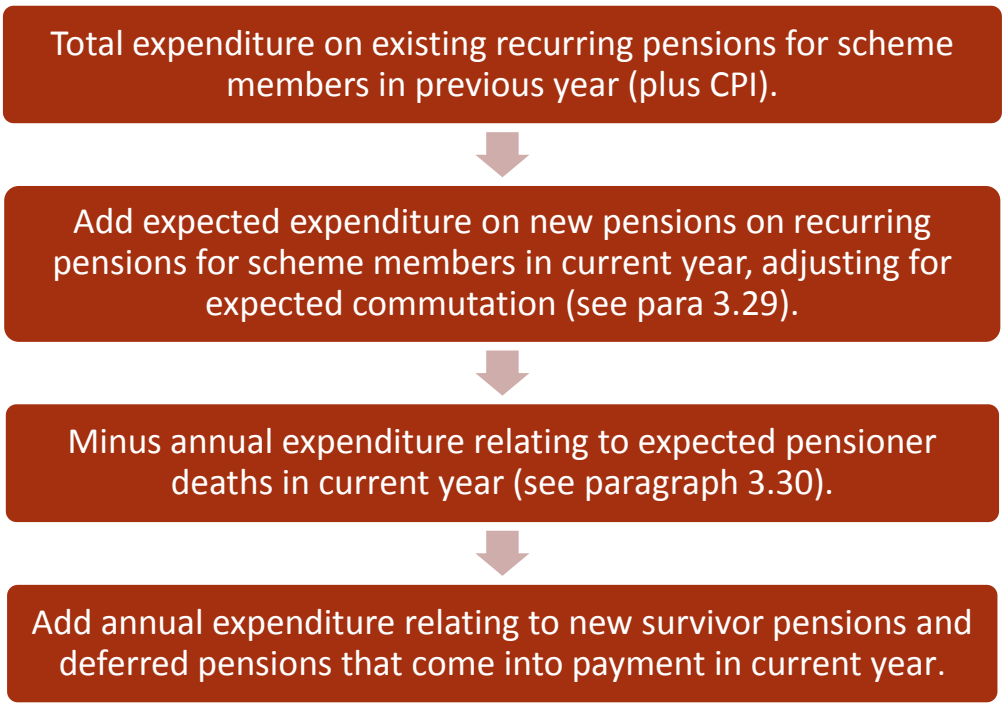
[5] Retirement from the 2015 Scheme Factsheet - http://www.fpsregs.org/images/admin/RetirementFPS2015v1.pdf

3.28 In the absence of robust retirement data being available, the **PFWG recommends** that fire authorities should consider their scheme retirement experience over the previous 5 years to assess the proportion of members who retired in the year that their entitlement arose and the proportions that retired in subsequent years.

3.29 For example, a fire authority may assess from its retirement experience that 60% of a scheme's members will retire in the year that the entitlement first arises, with 10% retiring for each of the following four years. With this information, fire authorities can estimate the total new annual pension that would be paid in accordance with their experience i.e. if they expect an additional £1m of new pension entitlement in any one year they can break this down to £600,000 of pension coming into payment in the year that the entitlement arises, and £100,000 of pension coming into payment for each of the following four years. This retirement profiling can be repeated for each year of the forecasting period. Fire authorities should also reflect prescribed CPI assumptions to take account of annual increases in the value of pensions in payment (see paragraph 2.4).

3.30 The **PFWG recommends** that fire authorities should calculate the average value of pensions expenditure that has ceased over the previous 5 years relating to the death of pensioners. Fire authorities will also have records showing whether, on the death of the pensioner, a survivor pension (at the rate of half the pensioner's pension) will come into payment.

3.31 To calculate the annual expenditure on recurring pensions for each scheme during the forecasting period the **PFWG recommends** using the following calculation method:



3.32 *Commutation lump sum payments* – When a scheme member retires they have an option to commute part of their annual pension for a retirement lump sum. Expenditure on retirement lump sums represents a significant proportion of the fund's annual expenditure and, as it relates to the number of retirements in each year, is the most volatile of all the pension expenditure streams.

3.33 Forecasting annual expenditure on retirement lump sums can be difficult as it is not always easy to predict in advance when a scheme member will choose to retire.

3.34 By using the schemes' retirement experience to forecast the amount of new pension payments to come into payment each year during the

forecasting period (see paragraph 3.29), fire authorities can determine the total value of new annual pension that is expected to be paid from each Fire scheme. In the absence of robust information to inform forecast commutation expenditure, the **PFWG recommends** that fire authorities should consider the average proportion of total new pension expenditure that is commuted in respect of each scheme over the previous 5 years. This average commutation rate for each scheme can be applied to the forecast new recurring pension expenditure that has been calculated for each of the years in the forecast period (see paragraph 3.29).

3.35 *Transfers Out (TVs out)* – Fire authorities may receive a request from existing scheme members to transfer their pension benefits from the fire pension schemes to an external pension arrangement. Where such a request is accepted, the fire authority is required to pay a cash payment out of their local pension fund account to the receiving pension arrangement.

3.36 The **PFWG recommends** that fire authorities should calculate the average cash TVs out paid over the previous 5 years[6] by using the following calculation method:

$$\text{Forecast TVs out}2020/21 = \frac{\text{TVs out}14/15 + \text{TVs out}15/16 + \text{TVs out}16/17 + \text{TVs out}17/18 + \text{TVsout}18/19}{5}$$

The average estimated TVs out for the first year of the forecast period can then be projected forward using an appropriate index e.g. wage growth.

[6] *At the time of forecasting expenditure on TVs out for 2020/21, FRAs will not know the actual expenditure on TVs out during 2019/20.*

3.37 *Other miscellaneous Expenditure* – There are other elements of pension expenditure that fire authorities need to forecast for each year of the forecasting period. For example, annual payments made to HMRC where a scheme member has elected to use Scheme Pays to pay an AA tax charge or LTA tax charge.

3.38 The **PFWG recommends** that fire authorities should calculate the average miscellaneous expenditure paid out of their pension accounts over the previous 5 years[7] by using the following calculation method:

$$\text{Forecast MiscExp2020/21} = \frac{\text{MiscExp14/15}+\text{MiscExp15/16}+\text{MiscExp16/17}+\text{MiscExp17/18}+\text{MiscExp18/19}}{5}$$

The average estimated miscellaneous expenditure for the first year of the forecast period can then be projected forward using an appropriate index e.g. wage growth.

[7] At the time of forecasting miscellaneous expenditure for 2020/21, FRAs will not know the actual miscellaneous expenditure paid out during 2019/20.

Annex A

Fire authorities will need to identify / estimate / derive the following information for each year during the forecasting period:

i. Scheme membership numbers - the number of members in each of the four fire pension schemes taking account of transitioning to the 2015 scheme, the numbers of new members joining through new recruitment; and the numbers of members leaving each scheme through retirement, opting out and employee turnover.

ii. Pensionable Pay levels – the annual pensionable pay that each scheme member receives. For new recruits and promotions, fire authorities should also be mindful of the recruitment date/date of promotion and prorate any annual pensionable pay to reflect the number of months remaining in the financial year.

ii. Ordinary retirements –the number of WTE [8]members that are expected to retire from each scheme with an ordinary pension and the pension that each retiring member is expected to receive. Fire authorities will also need to make an appropriate adjustment to reflect the value of the commutation lump sum that each new retiree is expected to receive.

iii. Ill-health retirements - the number of WTE scheme members that are expected to retire with an ill-health pension. It is also important that fire authorities can split total expected ill-health retirements into lower tier and higher tier as this will affect the amount of ill-health charge[9] that they will have to pay into their local pension account.

[8] Retained firefighters generally work between 25% to 35% of the hours of a WTE regular firefighter. Whilst this can be used as means to convert data relating to retained to WTE, fire authorities should also consider whether this conversion rate is representative of their workforce experience.

[9] Fire authorities will pay an ill-health charge to their local pension account equating to 2 x pensionable pay for lower tier ill-health retirements; and 4 x pensionable for higher tier ill-health retirements.

iv. New recruits - the annual number of new WTE scheme members that are expected to be recruited and the date that they are expected to start their employment.

v. Pensioner deaths - the number of pensioners that are expected to become deceased and, where applicable, the value of the survivor's pension that subsequently comes into payment.

vi. Transfers out - the total transfer values paid out of the fire pension schemes to external pension arrangements.

vii. Transfers in - the total transfer values paid into the fire pension schemes from external pension arrangements.

viii. Opt-outs –the annual number of WTE scheme members that will elect to opt-out of fire pension schemes.

Whilst this list is not exhaustive, fire authorities should ensure that they work closely with their human resource, payroll and pension administrations teams so that they can obtain the necessary information in a timely manner to feed into their forecast calculations.

Annex B

(i) Employee contribution rates for the 2015 Scheme:

Pensionable pay range for an employment	*Contribution rate from 1st April 2018*
Up to £27,818	11.0% of pensionable pay
£27,819 to £51,515	12.9% of pensionable pay
£51,516 to £142,500	13.5% of pensionable pay
£142,501 or more	14.5% of pensionable pay

(ii) Employee contribution rates for the 2006 Scheme:

Pensionable pay	*Contribution rate from 1st April 2015*
Up to and including £15,150	8.5% of pensionable pay
More than £15,150 and up to and including £21,210	9.4% of pensionable pay
More than £21,210 and up to and including £30,300	10.4% of pensionable pay
More than £30,300 and up to and including £40,400	10.9% of pensionable pay
More than £40,400 and up to and including £50,500	11.2% of pensionable pay
More than £50,500 and up to and including £60,600	11.3% of pensionable pay
More than £60,600 and up to and including £101,000	11.7% of pensionable pay
More than £101,000 and up to and including £121,200	12.1% of pensionable pay

More than £121,200	12.5% of pensionable pay

(iii) Employee contribution rates for the 1992 Scheme and Modified Scheme:

Pensionable pay	*Contribution rate from 1st April 2015*
Up to and including £15,150	11.0 % of pensionable pay
More than £15,150 and up to and including £21,210	12.2 % of pensionable pay
More than £21,210 and up to and including £30,300	14.2 % of pensionable pay
More than £30,300 and up to and including £40,400	14.7 % of pensionable pay
More than £40,400 and up to and including £50,500	15.2 % of pensionable pay
More than £50,500 and up to and including £60,600	15.5 % of pensionable pay
More than £60,600 and up to and including £101,000	16.0 % of pensionable pay
More than £101,000 and up to and including £121,200	16.5 % of pensionable pay
More than £121,200	17.0% of pensionable pay