FIREFIGHTERS' PENSION COMMITTEE

CAP AND SHARE

What is Cap and Share?

1. Cap and share is a policy to limit the cost of public sector pensions to the taxpayer

2. The 2009 Pre-Budget-Report expands on this stating:

   "Cap and share reforms to the Teachers, Local Government, NHS and Civil Service pension schemes will cap the contribution to pensions made by employers, thereby limiting the liability of the taxpayer as pensions become more valuable. Cost increases below the cap will be shared equally between employers and employees, and those above the cap met solely by employees."

3. This is developed in the Long-term public finance report: an analysis of fiscal sustainability which was published at the time of the Pre-Budget Report and states:

   "6.26 The main Pay-As-You-Go (PAYG) public service pension schemes covered …are those for the NHS, teachers, the civil service, the armed forces, the police, firefighters, the judiciary and the UK atomic energy authority. To manage increasing pension costs, these schemes (along with the Local Government Pension Scheme and the Parliamentary Contributory Pension Scheme) have already undergone reforms, such as the introduction of higher pension ages for new entrants, the reform of ill-health benefits. In addition, the introduction of cap and share mechanisms will control the increasing cost pressures arising from such things as improving life expectancy."

How and when will cap and share be introduced?

4. There will need to be amendments to the rules of the Fire Fighters' Pension Scheme and the New Firefighters' Pension Scheme.

5. The policy will be implemented when the next valuation is completed. The next valuation will be as at 31st March 2011.

What is the basis for cap and share

6. The PBR 2009 refers to "pensions becoming more valuable". In the context of cap and share "value" is measured within the framework of funding valuations.

7. Unfunded schemes use "SCAPE" mechanism for funding valuations. (SCAPE - Superannuation Charge Adjusted for Past Experience).

8. The output of the valuation will be a Recommended Contribution Rate (RCR) which, broadly, is the % of payroll payable each year so that the scheme can pay for benefits that will fall due in the future

9. In a cap and share valuation the emerging RCR will be compared with
    - the RCR from the previous valuation
    - the scheme cap (in schemes' rules)

10. The difference between old and new RCRs will be broken down. Some differences will not be in the cap and share regime (e.g. change in discount rate), and the cap and the employer rate will be adjusted. All other differences will be shared 50/ 50 between members and employers until employer rate reaches the cap.

11. Any new costs over employer cap will be met by members.

What is the basis for calculating RCR?

12. RCR = future service ± past experience

13. The RCR can be changed by:

- Inter-valuation one-off (e.g. pay increase)
- Inter-valuation experience - change future assumptions, e.g. longevity or ill health
- No inter-valuation experience but change in future assumptions e.g. retirement pattern
- longevity evidence
- future improvements in longevity
- pay scales
- staff withdrawal rates
- retirement patterns
- ill-health retirements
- overall membership base (age or take-up rate)

How are increases in cost paid for?

14. The Employers pay through an increase in the contribution rate.

15. Employees pay through:
    - Increase in contribution rate OR
    - Reduction in benefits.

16. If benefits are reduced cap and share constraints are effectively met by lowering RCR.

An example of cap and share

17. Following the XYZ pension scheme's last valuation, employers pay 13%, employees pay 6% and the cap is 14%.

    - The latest funding valuation reveals that costs (the RCR) have risen by 4% from 19% to 23%. This change has been caused by:
        - 3% cost pressure caused by increasing life expectancy
        - 2% cost pressure caused by lower staff turnover
        - 1% reduction in costs caused by lower than expected pay rises over the inter-valuation period
    - These causes are all within 'cap and share' framework.
    - Sharing half of the 4% cost pressure 50:50 brings the employer rate to the cap of 14%. Members pay the rest of the costs so their rate increases to 9%.

The Committee is invited to discuss.

Communities and Local Government
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