FIREFIGHTERS' PENSION COMMITTEE
FIREFIGHTERS' PENSIONS: Budget Notices

Budget 2011

1. At the Budget 2011 on 23 March the Chancellor made two announcements on public service pensions which are discussed in this paper. The full budget document can be found at http://www.hm-treasury.gov.uk/2011budget.htm.

Lord Hutton's Final Report

2. The final report of Lord Hutton's Independent Public Service Pensions Commission was published on 10 March 2011 and set out 27 recommendations for pension reform. Key recommendations include the protection of accrued rights; the retention of a defined benefit; a move to a career average scheme and a fairer sharing of risk between taxpayers and scheme members. The report also recommended a normal pension age of 60 for uniformed services inline with the NFPS, an end to the abatement of pensions and greater choice as to when benefits can be taken.

3. The final report also focused on governance, recommending independent oversight of governance, administration and data transparency, and a proposal that the Government examine closely the potential for shared contracts and combined support services across unfunded schemes. The full recommendations are set out in Annex A.

4. At the Budget the Chancellor accepted Lord Hutton's recommendations as a basis for consultation with public sector workers, trades unions and others, recognising that the position of the uniformed services will require particularly careful consideration. Following this consultation, the Government will set out its proposals for pension reform in the autumn.

SCAPE Discount Rate

5. Lord Hutton's interim report recommended that the SCAPE discount rate be reviewed as it was at the high end of what is appropriate. A discount rate is the rate at which a future payment or stream of payments is converted into a single value today. The SCAPE discount rate is used to set the total contribution rate for the unfunded public service pension schemes, and was set at 3.5% above RPI. As unfunded schemes, the review concerned both of the firefighter pension schemes.

6. The Government carried out a full public consultation on the appropriate discount rate to use; this consultation closed on 3 March 2011. Following this consultation, the Chancellor announced at the Budget that the Government had decided that the appropriate discount rate for calculating unfunded public service pension contribution rates should be based on the long term expectation of Gross Domestic Product growth (GPD). The use of GDP will ensure that employment decisions made today take into account the costs passed to future taxpayers on a fair and sustainable basis.

7. The latest OBR forecast for long-term GDP growth is 2.2% above the assumed GDP deflator, which is equivalent to a discount rate of 2.9% above the Consumer Price Index (CPI). Given the range of uncertainties inherent in these calculations,

the Government has decided that a rounded figure of 3% above CPI will be adopted under this methodology for future valuations.

8. The Government proposes to review the level of the discount rate every five years, and the methodology every ten years, and has also confirmed that this change in the discount rate will not lead to an increase in member contribution rates beyond those already announced at Spending Review 2010.

Conclusion

9. The Committee is invited to note developments and comment.

Department for Communities and Local Government
April 2011

Annex A: Lord Hutton's Recommendations

1. The Government should make clear its assessment of **the role of public service pension schemes**. Based on its framework of principles, the Commission believes that the primary purpose is to ensure adequate levels of retirement income for public service pensioners.

2. Pensions will continue to be an important element of **remuneration**. The Commission recommends that public service employers take greater account of public service pensions when constructing remuneration packages and designing workforce strategies. The Government should make clear in its remits for pay review bodies that they should consider how public service pensions affect total reward when making pay recommendations.

3. The Government should ensure that public service schemes, along with a full state pension, deliver at least **adequate levels of income** (as defined by the Turner Commission benchmark replacement rates) for scheme members who work full careers in public service. Employers should seek to **maximise participation** in the schemes where this is appropriate. Adequate incomes and good participation rates are particularly important below median income levels.

4. The Government must **honour in full the pension promises** that have been accrued by scheme members: their **accrued rights**. In doing so, the Commission recommends **maintaining the final salary link for past service** for current members.

5. As soon as practical, **members of the current defined benefit public service pension schemes should be moved to the new schemes for future service**, but the Government should continue to provide a form of **defined benefit pension** as the core design.

6. All public service pension schemes should **regularly publish data which, as far as possible, is produced to common standards and methodologies and is then collated centrally**. This information should be of a quality that **allows simple comparisons to be made** across Government, between schemes and between individual Local Government Pension Scheme (LGPS) Funds.

7. A new **career average revalued earnings (CARE) scheme** should be adopted for general use in the public service schemes.

8. **Pension benefits should be uprated in line with average earnings during the accrual phase for active scheme members**. Post-retirement, pensions in payment should be indexed in line with prices to maintain their purchasing power and adequacy during retirement.

9. A single benefit design should apply across the whole income range. The differing characteristics of higher and lower earners should be addressed through **tiered contribution rates**. The Government should consider the trade off between affordability and the impact of opt outs on adequacy when setting member contribution levels.

10. Members should have **greater choice** over when to start drawing their pension benefits, so they can choose to retire earlier or later than their Normal Pension Age and their pension would be adjusted accordingly on an actuarially fair basis. **Flexible**

retirement should be encouraged and abatement of pensions in its current form for those who return to work after drawing their pensions should be eliminated. In addition, caps on pension accrual should be removed or significantly lifted.

11. The Government should **increase the member's Normal Pension Age in the new schemes so that it is in line with their State Pension Age.** The link between the State Pension Age and Normal Pension Age should be regularly reviewed, to make sure it is still appropriate, with a preference for keeping the two pension ages linked.

12. The Government, on behalf of the taxpayer, should set out a **fixed cost ceiling**: the proportion of pensionable pay that they will contribute, on average, to employees' pensions over the long term. If this is exceeded then there should be a consultation process to bring costs back within the ceiling, with an **automatic default** change if agreement cannot be reached.

13. The Commission **is not proposing a single public service pension scheme**, but over time **public service pensions should move towards a common framework** for scheme design as set out in this report. However, in some cases, for example, the uniformed services, there may need to be limited adaptations to this framework.

14. The key design features contained in this report should apply to all public service pension schemes. The **exception is in the case of the uniformed services** where the Normal Pension Age should be set to reflect the unique characteristics of the work involved. The Government should therefore consider setting **a new Normal Pension Age of 60 across the uniformed services**, where the Normal Pension Age is currently below this level in these schemes, and **keep this under regular review.**

15. The **common design features laid out in this report should also apply to the LGPS**. However, it remains appropriate for the Government to **maintain the different financing arrangements for the LGPS** in future, so the LGPS remains funded and the other major schemes remain unfunded.

16. It is in principle **undesirable for future non-public service workers to have access to public service pension schemes**, given the increased long-term risk this places on the Government and taxpayers.

17. Every public service pension scheme (and individual LGPS Fund) should have a **properly constituted, trained and competent Pension Board, with member nominees, responsible for meeting good standards of governance including effective and efficient administration**. There should also be a **pension policy group** for each scheme at national level for considering major changes to scheme rules.

18. **All public service pension schemes should issue regular benefit statements** to active scheme members, at least annually and without being requested and **promote the use of information technology** for providing information to members and employers.

19. Governance and the availability and transparency of information would be improved by government establishing **a framework that ensures independent oversight of the governance, administration and data transparency of public service pension schemes.** Government should consider which body or bodies, including, for example, The Pensions Regulator, is most suitable to undertake this role.

20. When assessing the long term sustainability of the public finances, the **Office for Budget Responsibility should provide a regular published analysis of the long term fiscal impact of the main public service pension schemes** (including the funded LGPS).

21. **Centrally collated comprehensive data, covering all LGPS Funds, should be published including Fund comparisons**, which, for example, clarify and compare key assumptions about investment growth and differences in deficit recovery plans.

22. Government should set **what good standards of administration should consist of in the public service pension schemes based on independent expert advice.** The Pensions Regulator might have a role, building on its objective to promote good administration. **A benchmarking exercise should then be conducted across all the schemes** to assist in the raising of standards where appropriate.

23. Central and local government should **closely monitor the benefits associated with the current co-operative projects within the LGPS, with a view to encouraging the extension of this approach, if appropriate,** across all local authorities. Government should also examine closely the potential for the unfunded public service schemes to **realise greater efficiencies in the administration of pensions** by sharing contracts and combining support services, including considering outsourcing.

24. The Government should introduce **primary legislation to adopt a new common UK legal framework** for public service schemes.

25. The **consultation process itself should be centrally co-ordinated**: to set the cost ceilings and timetables for consultation and overall implementation. However, the **consultation on details should be conducted scheme by scheme involving employees and their representatives**.

26. The Commission's view is that even allowing for the necessary processes it should be possible to **introduce the new schemes before the end of this Parliament** and we would encourage the Government to aim for implementation within this timeframe.

27. **Best practice governance arrangements** should be followed for **both business as usual and the transformation process**, for each scheme. And there will also **need to be the right resource**, on top of business as usual, to drive the reforms; particularly given the challenging timescale and scope of the reforms.