

Report of the Treasurer to the Chair and Members of the Policy and Resources Panel.

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Status: For Noting

The Public Sector Pensions Debate

1. Purpose

- 1.1 To outline some of the key issues in the current debate around the future of public sector pensions, with particular reference to funding issues, which has a direct impact on the cost of policing.

2. Recommendations

- 2.1 That members note this report.

3. Reasons

Public Sector Pensions Debate - Background and Context

- 3.1 In June 2010 the Government commissioned former Work and Pensions Secretary, Lord Hutton, to chair the Independent Public Service Pensions Commission's review into the long term future of public service pensions. In his final report Lord Hutton set out his recommendations on how these can be made sustainable and affordable in the long-term, whilst at the same time being fair to both public sector workers and the taxpayer. Lord Hutton concluded that reform was needed.
- 3.2 The Government accepted his recommendations as a basis for consultation with public sector workers, trade unions and other interested parties about the need for long term reform. The

Government intends to introduce changes from 2015 and has confirmed that all pension benefits earned up to that point will be protected. The reforms will ensure that all public service pensions, including the Local Government Pension Scheme (LGPS), will continue to be amongst the best pensions available.

- 3.3 Before making his recommendations for wider reform, Lord Hutton published his interim report. This recommended that if the Government wished to make short term savings to meet current cost pressures, then raising contribution rates would be the most effective way to achieve that objective.
- 3.4 Lord Hutton set out the following rationale for increasing member contributions to public service pension schemes:
- People are living much longer than previous generations – the average 60 year old is living ten years longer now than they did in the 1970s.
 - More of people's lives are now being spent in retirement – between 40 per cent to 45 per cent of adult life compared with around 30 per cent for pensioners in the 1950s
 - As people are living longer in retirement, the cost of providing pensions is increasing; annual expenditure on public service pensions over the last decade has increased by a third to £32bn. And in the case of the LGPS, expenditure on benefits has increased from £1.8bn to £6bn since 1997.
 - Taxpayers can't be expected to bear all the cost of increased longevity. There needs to be a fairer balance between what employees pay and what other taxpayers contribute towards a public service pension.
- 3.5 At the Spending Review, the Chancellor acted upon the rationale Lord Hutton set out by announcing that employee contributions would be increased by an average of 3.2 percentage points in the unfunded public service pension schemes (The Police Officer Pension Fund falls into the category of an 'unfunded scheme'). This will make savings of £2.8bn a year by 2014-15, to be phased in from April 2012.
- 3.6 The Chief Secretary to the Treasury's statement to the House of Commons on 19 July 2011 confirmed that the unfunded schemes would begin formal consultations on the proposed increases in employee contribution rates for 2012-13. In recognition of the funded nature of the LGPS, the Government accepted that separate discussions should take place to see whether alternative ways to deliver some or all of the savings could be found. The equivalent savings in the LGPS are £900m in England and Wales.

Local Government Pension Scheme: Consultation on Proposals for Short-Term Savings

- 3.7 On 7 October 2011 DCLG published consultation proposals to achieve the savings of £900m by 2014/15 from the Local Government Pension Scheme (LGPS). This is equivalent to the 3.2% contribution increase required from unfunded public service pension schemes by the Spending Review.
- 3.8 The proposals consist of two main elements:
- An increase in the employees' contribution tariff from April 2012, to raise an additional £450m (1.5% of pensionable paybill), *and*
 - A change in the scheme's accrual rate from April 2013, to raise an additional £450m (1.5% of pensionable paybill).
- 3.9 The consultation paper states the Government's desire to protect low earners, which means high earners will pay more as a proportion of their salary in contributions than those in lower salary bands, reflecting their more generous pension. There will be no increase in contributions for LGPS members earning less than £15,000 and no more than a 0.6% increase for those earning up to £21,000 in 2012/13. It is proposed that the 31% of local government staff who earn between £21,101 and £32,400 would see their contribution rates increase from 6.5% of pay to 8.3%.
- 3.10 The consultation closes on 6 January 2012 and DCLG's intention is that the proposed amendments to the Scheme's regulatory framework, will take effect on 1 April 2012, subject to the outcome of the consultation exercise. DCLG is expected to announce the final design in February 2012.

Local Government Pension Scheme: Post-2015 Reforms

- 3.11 On 2 November 2011 HM Treasury published a paper, 'Public Service Pensions: good pensions that last', outlining proposals on pension reforms from 2015 onwards. It proposes a Career Average Revalued Earnings scheme for the LGPS, with benefits earned at an accrual rate of 1/60th of pensionable earnings per year. Following discussion with trades unions the paper proposes that the LGPS will have a gross cost ceiling of 20.4% of which 10.9% will be borne by the taxpayer and 9.5% by employees. This cost ceiling is based on the assumption that members' contributions will be increased by an average of 3.0% by 2014/15.
- 3.12 The paper proposes that benefits already earned are protected and for those in final salary schemes, past benefits will be linked to their final salary when they leave the scheme or retire. It also proposes for those workers who, as of 1 April 2012, have ten years or less until their

current pension age, that there will be no change in the retirement age or the amount of pension they receive at the normal retirement age.

- 3.13 According to the paper, the Government's offer is conditional on the trades unions and the Government reaching agreement on the reforms. It states that 'if agreement has not been reached by the end of the year, the Government may need to revisit its current proposals'. The paper states costs ceilings for the police pension scheme will be set in the first few months of 2012.

Police Pension Scheme: Proposed Increase to Contribution Rates 2012/13 to 2014/15

- 3.14 On 29 July 2011 the Home Secretary wrote to members of the Police Negotiating Board (PNB) setting out proposals to increase Police Pension Scheme members' contributions over a three-year period between 2012/13 and 2014/15. The proposals are designed to deliver savings equivalent to an average 3.2% increase in employee contributions by 2014/15, as required by the Spending Review 2010. The consultation with the PNB on the proposals ended on 27 October 2011 and the Government's response is currently awaited.
- 3.15 The proposals are designed to protect lowest-paid scheme members, require higher earners to pay more and minimise any increase in members opting out. Current employee rates are 11.0% for 1987 Scheme members and 9.5% for 2006 Scheme members. In summary the Government proposals would result in the following member contribution rates by 2014/15:
- Officers earning up to £26,999: 2006 Scheme 11.0%
 - Officers earning £27,000 to £59,000: 1987 Scheme 14.2%, 2006 Scheme 12.0%
 - Officers earning £60,000 and above: 1987 Scheme 15.0%, 2006 Scheme 12.7%
- 3.16 The future arrangements for the Police Pension Scheme from 2015 onwards are currently being considered by the second stage of the Winsor Review, as part of the review of pay and conditions of service for police officers.

4 IMPLICATIONS

4.1 Diversity and Equal Opportunity

There are no implications arising from this report.

4.2 Finance

The proposed increases in employee pension contribution rates should result in a reduction in the employer pension contribution rates paid by Cleveland Police Authority. These reductions would be subject to actuarial calculations however only those relating to the LGPS are expected to flow through as savings to the Authority.

4.3 Risk Assessment and Sustainability

The main risk for the employer is the reaction of public sector employees to any proposed increases in their pension contributions at the same time as there is a pay freeze in operation and other terms and conditions are under review.

4.4 Human Rights

There are no human rights implications within this report.

5. Conclusion

- 5.1 The public sector pensions debate revolves around future liabilities and the balance of contributions between the employer (and therefore the tax payer) and the employee.

Michael Porter
Treasurer