

APPENDIX B

Report to:	Ethics and Audit Working Group
Date:	23 July 2010
Reporting Officer:	Peter Morris, Executive Director of Pensions
Subject:	INDEPENDENT PENSION COMMISSION
Report Summary:	<p>The government has set up an independent pension commission chaired by John Hutton to review the long term affordability and sustainability of public service pensions. This report sets out the terms of reference and a proposed structure for a response from the Fund. There will be a presentation at the Working Group and discussion to help formulate the response.</p>
Recommendations:	<ol style="list-style-type: none">1. That a response be submitted to the Commission in line with the views of the Working Group.2. That the Chair of the Management Panel approve the content and wording of the response.
Financial Implications: (Authorised by the Borough Treasurer)	<p>In reviewing public sector pensions, there are many issues that need to be considered.</p> <p>Clearly, the long term affordability of the LGPS is critical to its sustainability and in making such an assessment a long term view needs to be considered alongside the consequences of changes proposed.</p>
Legal Implications: (Authorised by the Solicitor to the Fund)	<p>The Commission will produce an interim report by the end of September considering the case for short-term savings within the Spending Review 2010 period. Any such changes will need to be implemented through the relevant legislative or regulatory procedures.</p>
Risk Management:	<p>The economic and financial environment has made the last decade a very difficult period for those running and funding pension schemes. The long term nature of pension schemes means that whilst the short term consequences of change should be capable of quantification, the longer term is more difficult and there is a likelihood of unintended consequences. The main purpose of this report and associated presentation is to be informative and flag some of the issues that need to be considered.</p>
ACCESS TO INFORMATION:	<p>NON - CONFIDENTIAL</p> <p>This report does not contain information which warrants its consideration in the absence of the Press or members of the public.</p> <p>For further information please contact Peter Morris, Executive Director of Pensions on 0161 342 2952 or email peter.morris@tameside.gov.uk</p>

1. INTRODUCTION AND BACKGROUND

- 1.1 The last decade has seen significant changes in pension provision. In the private sector, there has been a move away from defined benefit schemes to defined contribution (money purchase). This has been driven by affordability issues (the last decade has been amongst the most challenging for financial markets and interest rates have shrunk to historical lows which drives up the value of liabilities alongside increasing life expectancy projections) and accounting requirements.
- 1.2 In the public sector, schemes have been reviewed to address affordability issues and have generally maintained a defined benefit approach to assessing benefits.
- 1.3 The Government is introducing “NEST” to encourage pension saving amongst those that do not currently save (subject to confirmation by the Government).
- 1.4 The affordability and sustainability of public sector pensions is currently subject to intense scrutiny. The unfunded nature of many public sector schemes, their cost and the scale of liabilities and the impact this has on the national debt has featured regularly in the news with various proposals being put forward. The most recent came from the Institute of Directors and the Institute of Economic Affairs. They have called for an immediate 2% increase in employee contributions as a starting point. It also recommended later pension ages and reduced benefits.
- 1.5 The Government has recently set up an independent pensions commission, chaired by John Hutton, to review the long term affordability and sustainability of public service pensions.
- 1.6 The purpose of this report is to set out the terms of reference for the Commission and provide a framework for discussion to help formulate a response. Responses are sought by the end of July.

2. INDEPENDENT PUBLIC SERVICE PENSIONS COMMISSION - ANNOUNCEMENT

- 2.1 The Government is setting up an Independent Public Service Pensions Commission, chaired by John Hutton, to conduct a fundamental structural review of public service pension provision. John Hutton is a former Labour Minister and held a number of Secretary of State posts including Work and Pensions.
- 2.2 The Commission will produce an interim report by the end of September 2010 considering the case for short-term savings within the Spending Review 2010 period, consistent with the Government’s commitment to protect those on low incomes. Terms of Reference for the review are set out below. A final report is requested to help inform the 2011 Budget.

3. WHICH SCHEMES ARE WITHIN THE SCOPE?

- 3.1 Schemes within the scope of the review are:

- Principal Civil Service Pension Scheme
- Principal Civil Service Pension Scheme (Northern Ireland)
- Armed Forces Pension Scheme
- NHS Pension Scheme
- NHS Superannuation Scheme (Scotland)
- Health and Personal Social Services Northern Ireland Superannuation Scheme
- Teachers’ Pension Scheme (England and Wales)
- Scottish Teachers’ Superannuation Scheme

- Northern Ireland Teachers' Superannuation Scheme
- **Local Government Pension Scheme (England and Wales)**
- Local Government Pension Scheme (Scotland)
- Northern Ireland Local Government Pension Scheme
- Police Pension Scheme (administered locally)
- Firefighters' Pension Scheme (administered locally)
- United Kingdom Atomic Energy Authority Pension Schemes
- Judicial Pension Schemes
- Department for International Development – Overseas Superannuation Scheme
- Research Councils' Pension Schemes

3.2 The Commission will not consider the trust-based funded schemes in the wider public sector, in particular among government owned companies or public corporations, such as those for the BBC, Royal Mail or the Universities Superannuation Scheme.

4. TERMS OF REFERENCE

4.1 To conduct a fundamental structural review of public service pension provision and to make recommendations to the Chancellor and Chief Secretary on pension arrangements that are sustainable and affordable in the long term, fair to both the public service workforce and the taxpayer and consistent with the fiscal challenges ahead, while protecting accrued rights.

4.2 In reaching its recommendations, the Commission is to have regard to:

- the growing disparity between public service and private sector pension provision, in the context of the overall reward package – including the impact on labour market mobility between public and private sectors and pensions as a barrier to greater plurality of provision of public services;
- the needs of public service employers in terms of recruitment and retention;
- the need to ensure that future provision is fair across the workforce;
- how risk should be shared between the taxpayer and employee;
- which organisations should have access to public service schemes;
- implementation and transitional arrangements for any recommendations; and
- wider Government policy to encourage adequate saving for retirement and longer working lives.

5. TIMING

5.1 As part of the review, the Commission is invited to produce an interim report by the end of September 2010 This should consider the case for delivering savings on public service pensions within the spending review period – (consistent with the Government's commitment to protect those on low incomes) – to contribute towards the reduction of the structural deficit.

5.2 The commission is invited to produce the final report in time for the 2011 Budget.

6. GMPF

6.1 At the March Panel, consideration was given to potential scheme developments. The Panel minute concluded that "work be undertaken in conjunction with Hymans Robertson

on a potential scheme design based on a hybrid option with Pension Build Up (Career Averaging) being the default option and final salary available to those members who were prepared to pay the extra costs”.

6.2 A suggested format for the Fund’s response is set out below. The aim is to inform the debate and put forward the Panel’s preferred approach, whilst recognising that the cost of the Scheme and how it is shared is primarily an issue for Government, employers and Scheme members.

- (i) Short profile on GMPF
 - part of LGPS/our scale
 - funding position
 - response as an administering authority
- (ii) GMPF – vital statistics
 - average pension
 - pension profile
 - duration on pension
- (iii) Context – where does 2nd pension fit within system
 - NAPF 7 principles
 - preferred starting point – core pension, not adversely affected by saving
 - current position, for many members LGPS pension replaces means tested benefits – who pays for those that do not save?
- (iv) What has caused the problem?
 - returns 75-99, enabled everything that was thrown at a pension scheme to be delivered at no or reducing cost to employer
 - returns 2000-2009, as bad a decade as it gets
- (v) Looking forward, what type of returns can we expect in the long term? Very small changes can have a material impact on liability values and funding position. The change to CPI from RPI is expected to reduce liabilities by 10%; public sector pay constraints will have a beneficial effect. For GMPF, 1% on investment returns equals 5%+ of payroll. LGPS will be around for many decades to come, decisions should not be based on the experience of the last, exceptional decade. How do we deal with changes in mortality?
- (vi) Administering authority role is to administer the LGPS; it is not our norm to comment on the benefit package and how the cost is met.
- (vii) Framework for going forward:-
 - agreement on what is affordable (to all parties) and sustainable cost of the scheme
 - strong preference for defined benefit because of 1) risk aversion in DC and 2) higher cost of admin and thus worse value – complex other impacts that others can consider and comment on
 - if DB, what level of volatility of cost is acceptable, and how will it be managed, risk sharing, cap and share, discretionary benefits
 - how do we distribute the benefits – career averaging (CARE) favoured
- (viii) Analysis of options for benefits package – provide benefits that members value (and reflect any wider aims that are agreed – e.g. case for widows/widowers benefits).
- (ix) To assist with the detail of the Fund’s submission the Actuary has been asked to provide the following information:-

- (a) Analyse the cost of the various components of the Scheme - picking up the particular items identified and an understanding of the implications of changing the assumptions
- (b) Sensitivity analysis v assumptions, e.g real rate of return of 2%, 2.5%, 3%, 3.5% and 4%
- (c) Indicative comparison of final salary v CARE
- (d) Indicative cost comparison of changing rate of accrual
- (e) Impact of increasing retirement age
- (f) Final Salary option - is there a fair way of assessing the extra cost, bearing in mind those that take this option will think that they will benefit.

6.3 A presentation and discussion at the Working Group will help develop the response to the Commission.

6.4 Attached at **Appendix 1** is Hymans initial response to John Hutton. This provides some alternative views on the way forward.

7. RECOMMENDATIONS

7.1 The Director of Pensions draft a response on behalf of the Panel reflecting the views of the Working Group.

7.2 The Director of Pensions consult with the Chairman on the final submission.