

Independent
Public Service

Pensions Commission

Reforming public service pensions in the United Kingdom

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Outline

- The UK Independent Public Service Pensions Commission
- Public Service Pensions in the UK
- The case for further reform
- Interim conclusions and next steps

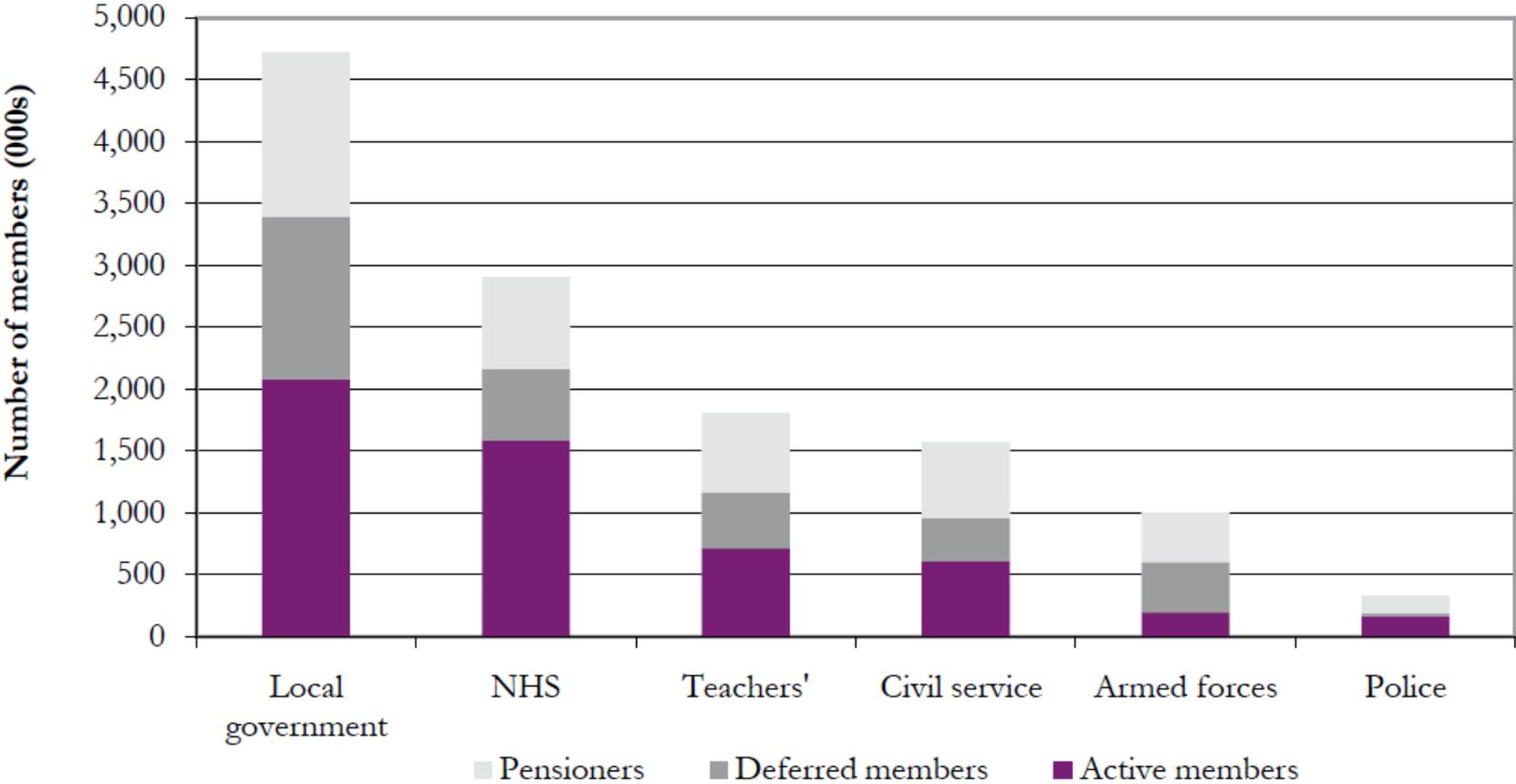
The Independent Public Service Pensions Commission

- New government elected in May 2010
- Coalition agreement: independent review of “long-term affordability of public sector pensions, while protecting accrued rights”
- Lord Hutton appointed in June 2010
- Interim report published in October 2010
- Final report due in March 2011

Public Service Pensions in the UK

Membership of UK Public Pension Schemes

Scheme membership in UK pension schemes



Source: IPSPC analysis of resource accounts and scheme data returns

Public Service Pension payments

The evolution of pension payments from the five largest schemes

	Total Pensions Paid			Average (Mean) Pension		
	1999-2000 (adjusted to 2009- 10 prices) (£bn)	2009-10 (£bn)	% change	1999-2000 (adjusted to 2009-10 prices) (£)	2009-10 (£)	% change
Local government (England)	3.53	4.41	25	4,115	4,052	-2
NHS (England and Wales)	3.13	4.62	47	6,951	7,234	4
Civil service (UK)	2.97	3.67	23	5,626	6,199	10
Teachers (England and Wales)	4.07	5.56	37	9,781	9,806	0
Armed forces	2.40	3.08	28	7,160	7,722	8
Total	16.11	21.34	32	6,222	6,497	4

Source: The Cost of Public Service Pensions, National Audit Office, IPSPC analysis of resource accounts, Local Government Financial Statistics England, 2010.

Payments and contributions in unfunded schemes

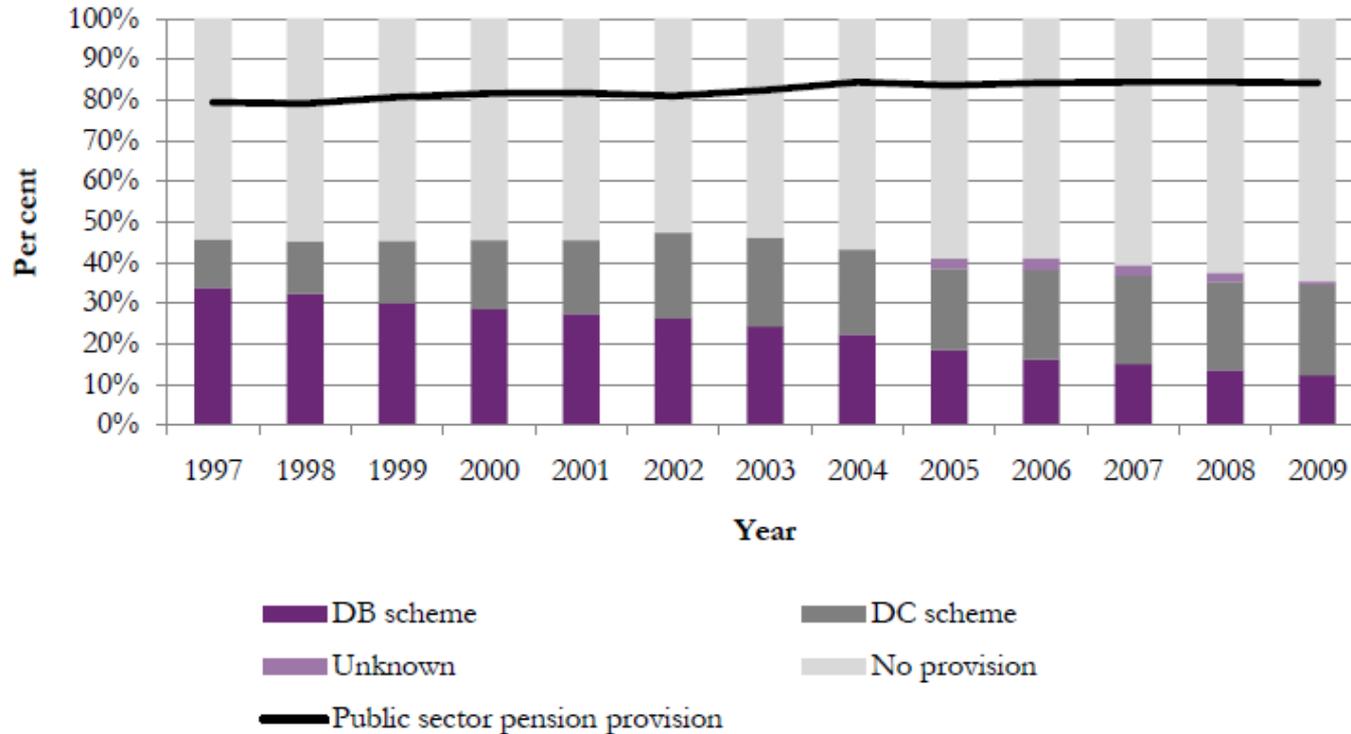
OBR Budget 2010 forecast: net cash expenditure

Year	Net cash expenditure (£bn)	Benefit payments (£bn)	Contributions received (£bn)
2008-09	3.1	22.5	19.4
2009-10 (estimate)	3.1	24.3	21.2
2010-11 (forecast)	4.0	25.4	21.3
2011-12 (forecast)	5.1	26.8	21.6
2012-13 (forecast)	5.8	28.3	21.5
2013-14 (forecast)	7.3	29.9	21.5
2014-15 (forecast)	8.9	31.3	21.4
2015-16 (forecast)	10.3	32.9	21.6

Source: OBR

a Forecasts from 2012-13 onwards include a £1 billion saving from cap and share.

Employer-sponsored pension provision in the UK



Source: *Annual Survey of Hours and Earnings, 2009*

Note: There was a methodological change between 2005 and 2006, which has a marginal impact on results. The 'Unknown' category was introduced in 2005.

Recent Reforms

- Mainly for new entrants
- Increase in pension age (60 to 65 Health, Teachers, Civil Service)
- Modernisation eg. unmarried partners' pension
- Some increase in employee contributions, variation by income in Health and Local Government
- Final Salary scheme remains for most, but Civil Service scheme changed to career average
- Cost sharing introduced in some schemes – “Cap and Share”
- June 2010 – change in indexation measure RPI to CPI
- Recent reforms plus change in indexation lead to around 25% reduction in pension benefits as % of pay

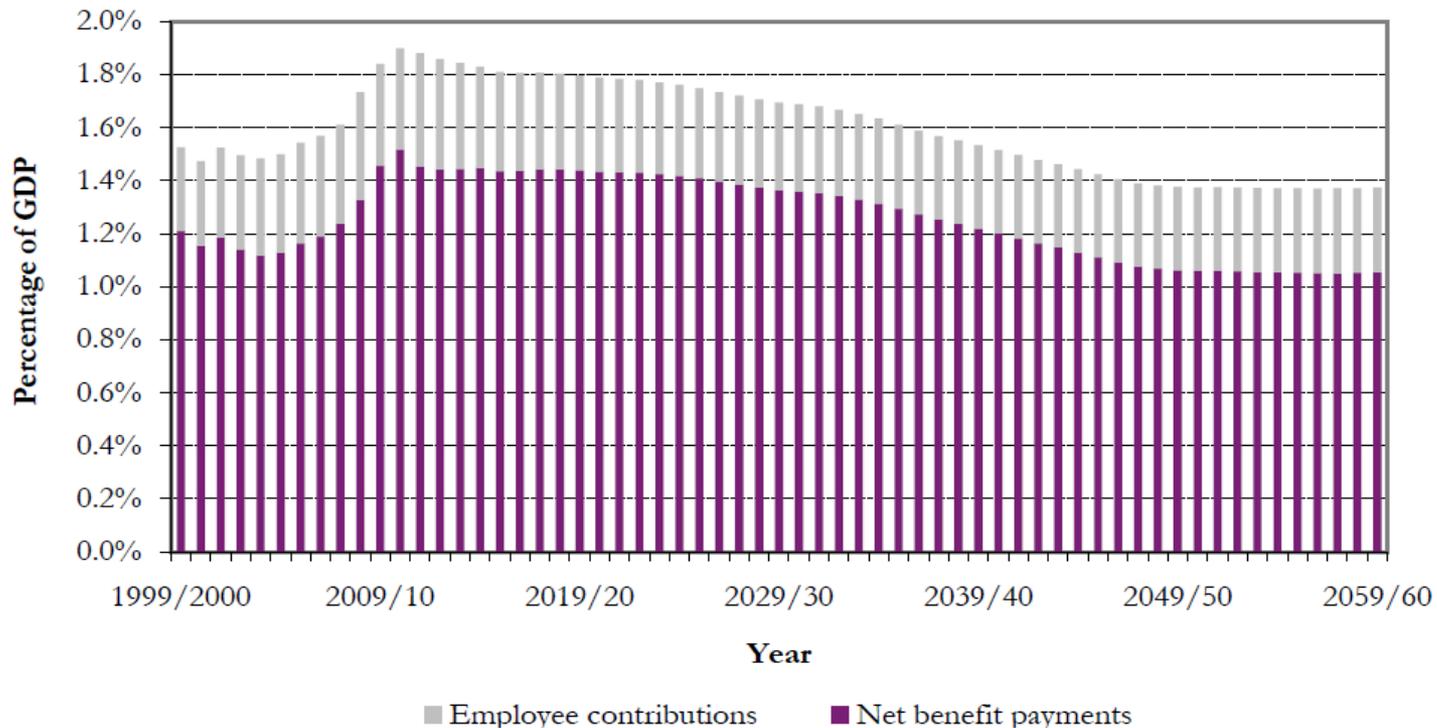
The case for further reform

The framework of principles

- Affordable and sustainable
- Adequate and fair
- Support productivity
- Transparent and simple

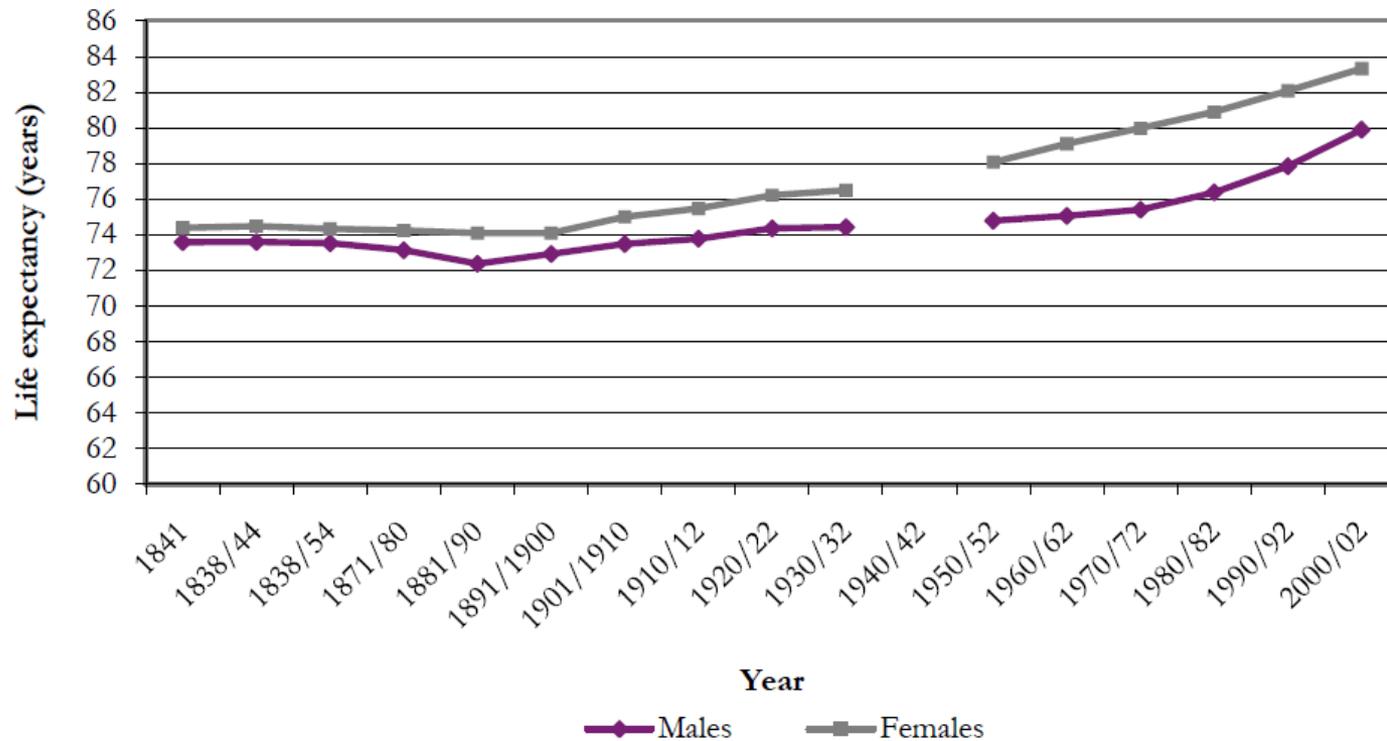
Affordable and sustainable: projected costs

Projected benefit payments as a percentage of GDP – central projection



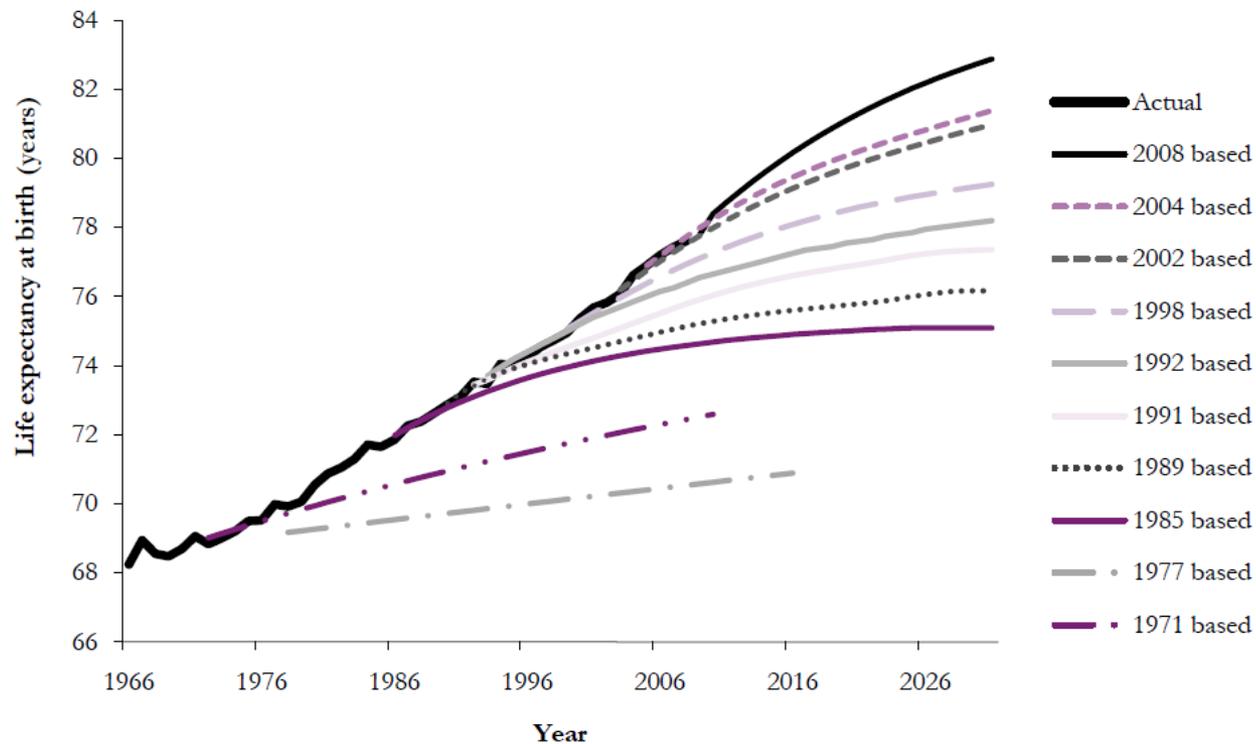
Affordable and sustainable: life expectancy

Period life expectancies for those reaching age 60 – general population



Affordable and sustainable: projected life expectancy

Actual and projected period life expectancy at birth for UK males



Source: IPSPC analysis drawing on C Shaw, 2007 and ONS, 2008 population projections.

Affordable and sustainable: life in retirement

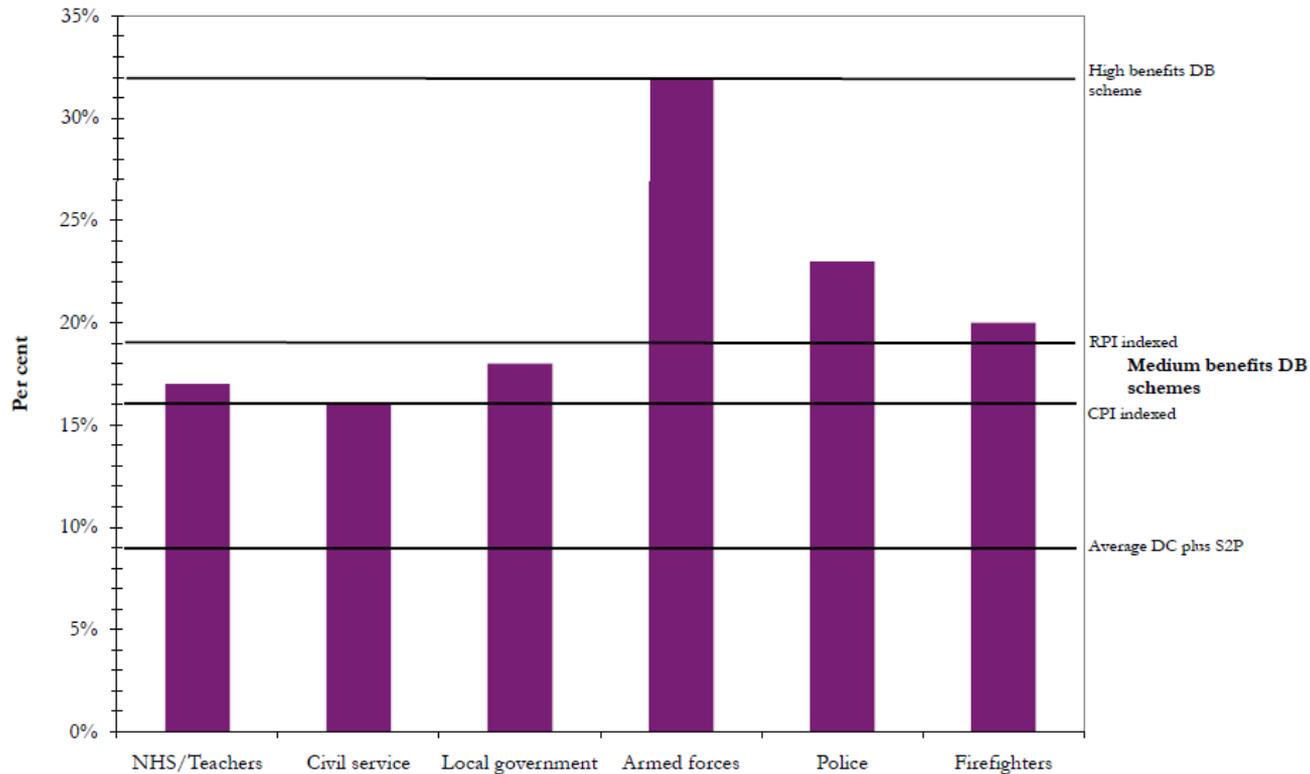
Assumed proportion of adult life in retirement, NHS Pension Scheme



Source: IPSPC analysis of GAD valuation reports.

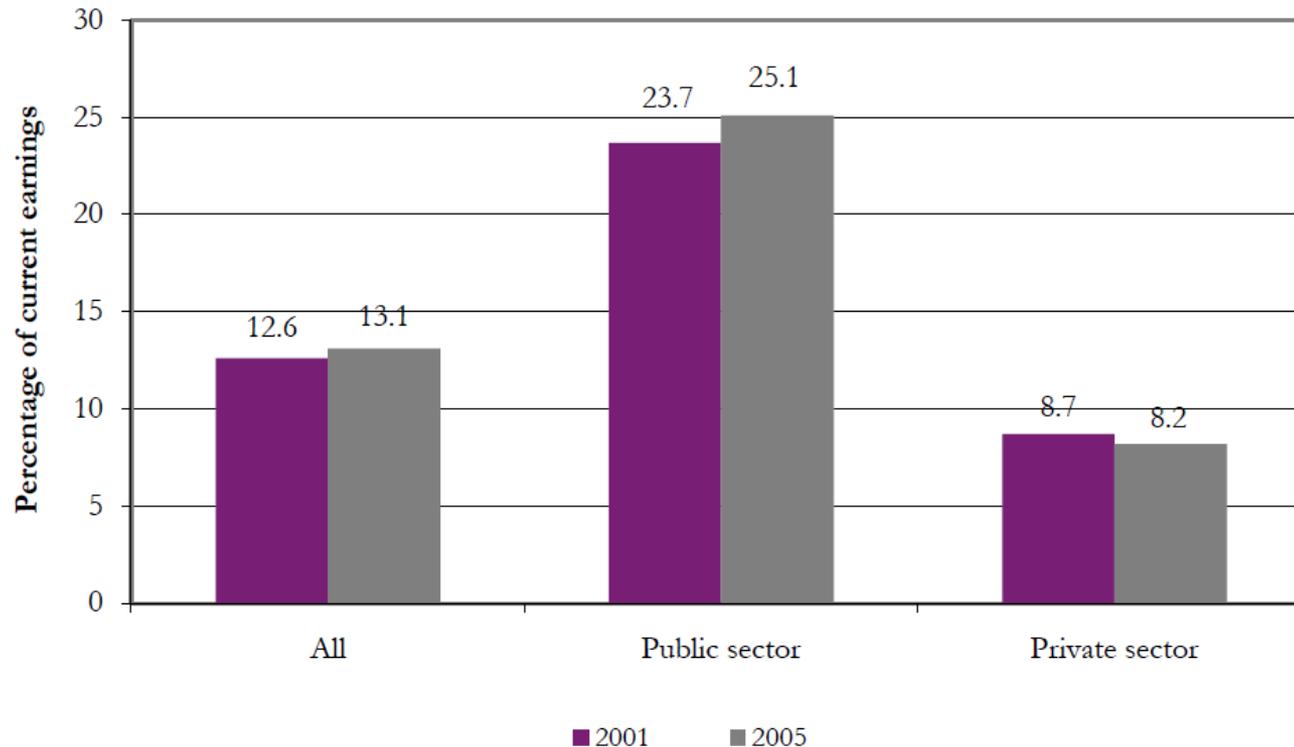
Adequate and fair: between types of worker

Average effective employee benefit rates for reformed public service pension schemes new entrants



Adequate and fair: between sectors

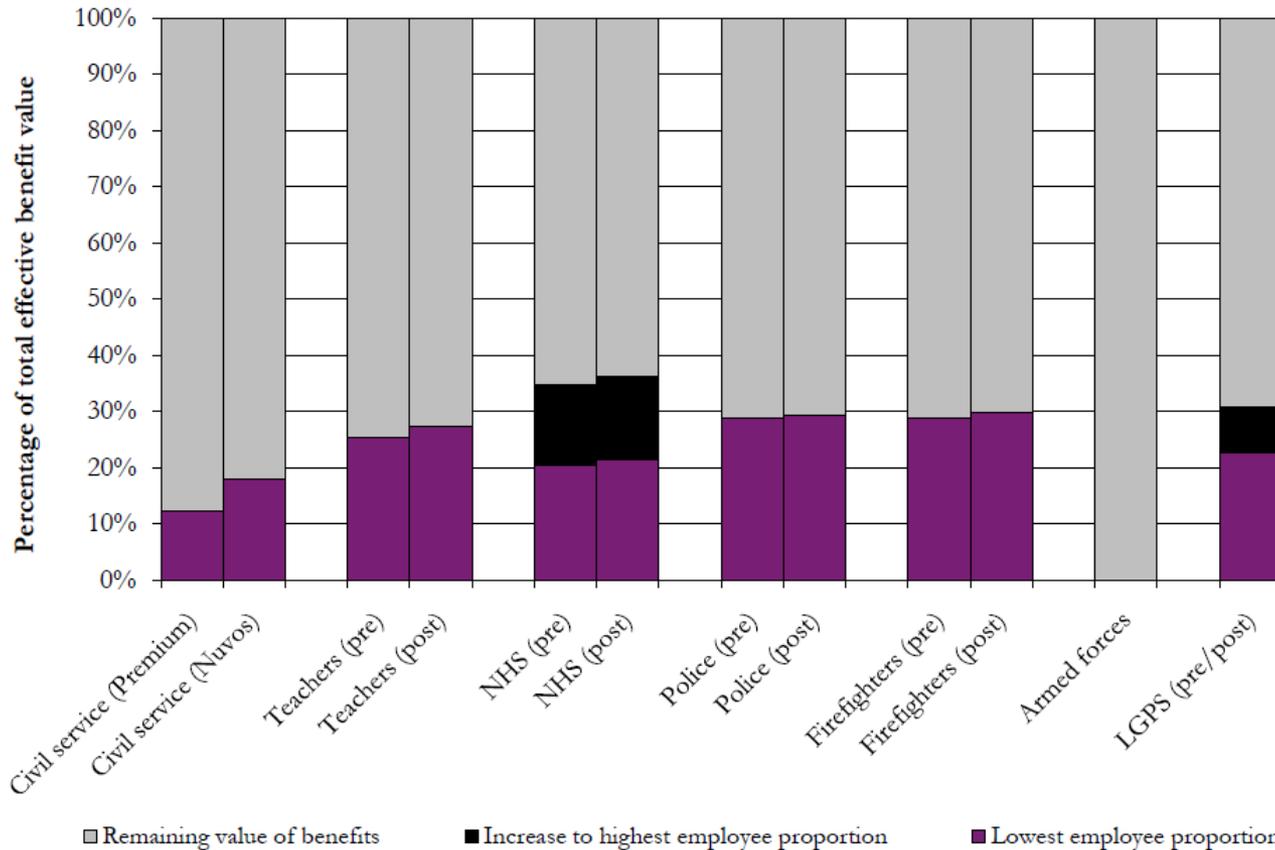
Mean value of total benefits as a percentage of pay across all employees



Source: Occupational pension value in the public and private sectors, Crawford, Emmerson and Tetlow (IFS).

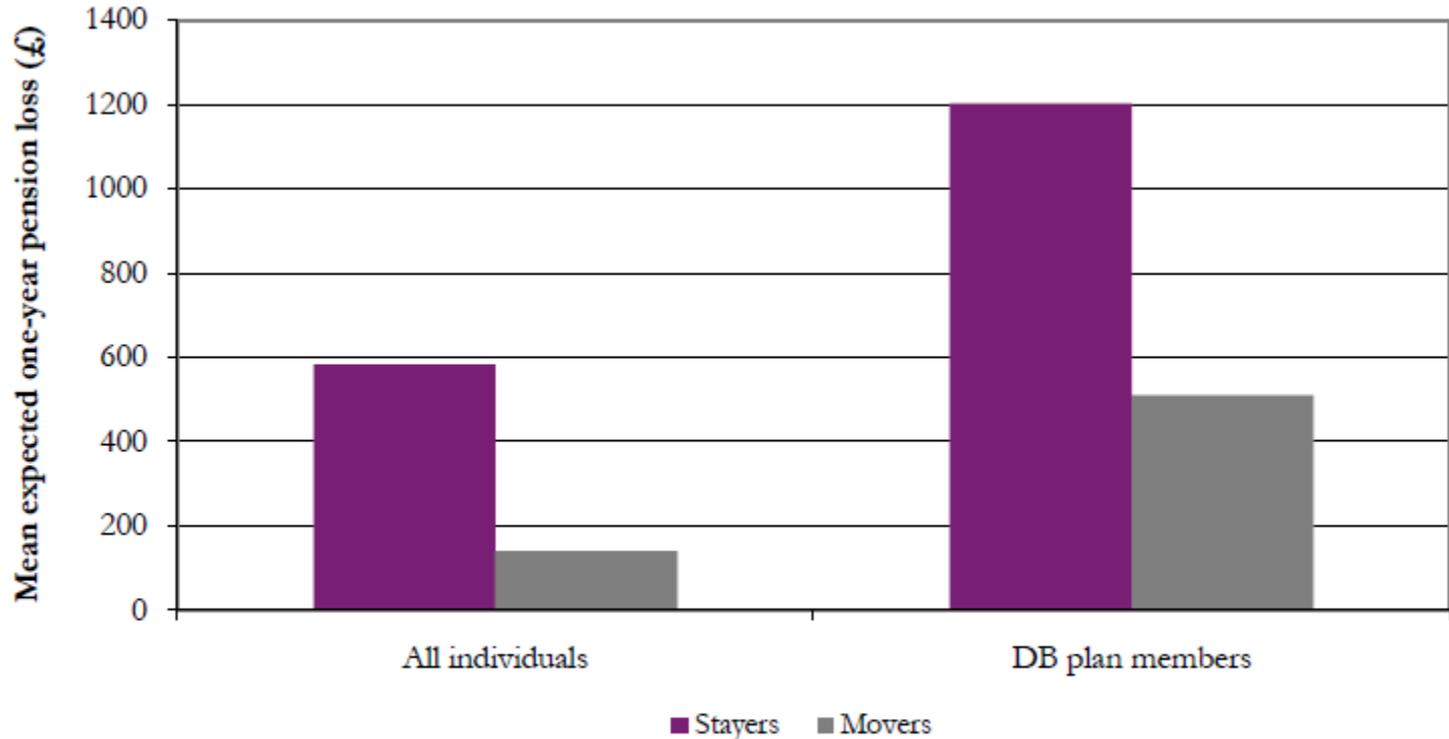
Adequate and fair: between employee and taxpayer

Employee contributions as a proportion of the value of the accrual – pre and post reform



Support productivity: labour mobility

Mean pension loss among stayers and movers



Source: *Pension Rights, Choice of Pension Plan and Job Mobility in Britain*, Disney, Emmerson and Tetlow, mimeo, Institute for Fiscal Studies, 2007.

Interim conclusions

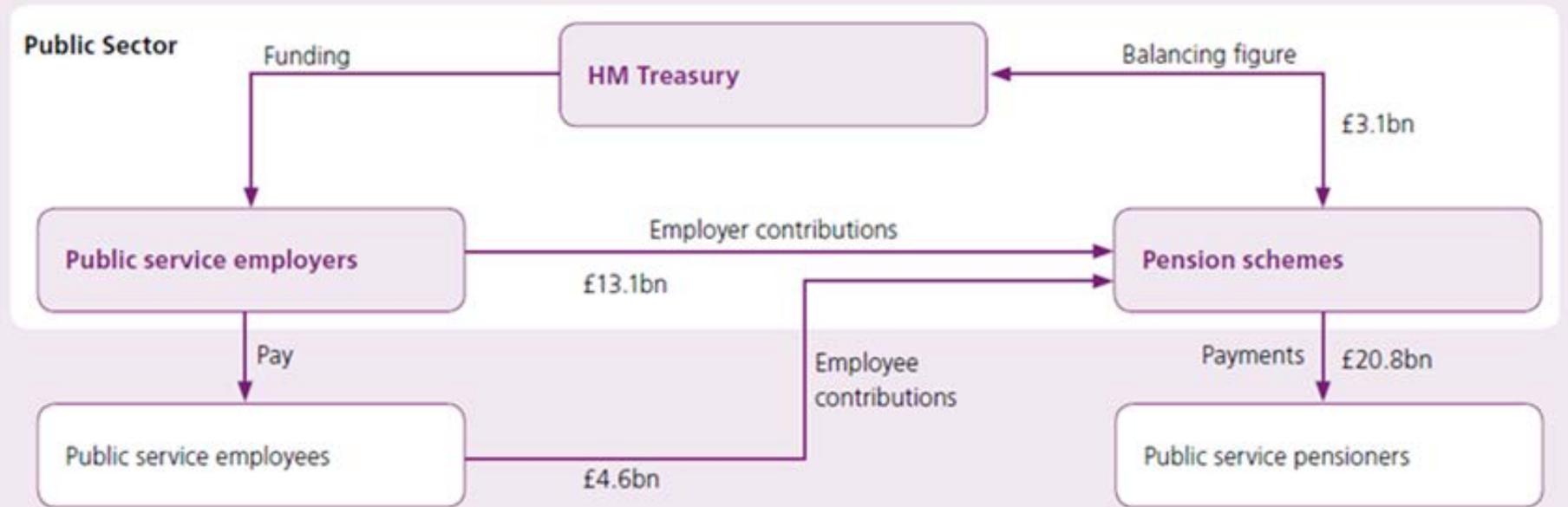
- Need for reform but not a “race for the bottom”
- Case for short term change: raising employee contributions only effective option
- Long term direction:
 - Rule out continuation of final salary scheme and funded individual account DC
 - Consider a wide range of options: career average DB, notional DC, collective DC, cash balance, capped DB, combination hybrids
 - Draw on international and private sector experience
- Transition: must protect accrued rights of existing members but not their future accrual

Next Steps

- Interim report available at www.hm-treasury.gov.uk/indreview_johnhutton_pensions.htm
- Final report will be published in March 2011
- Contact us at: pensions.commission@hmtreasury.gsi.gov.uk

Annex

Diagram: Payments and contributions in pay-as-you-go pension schemes

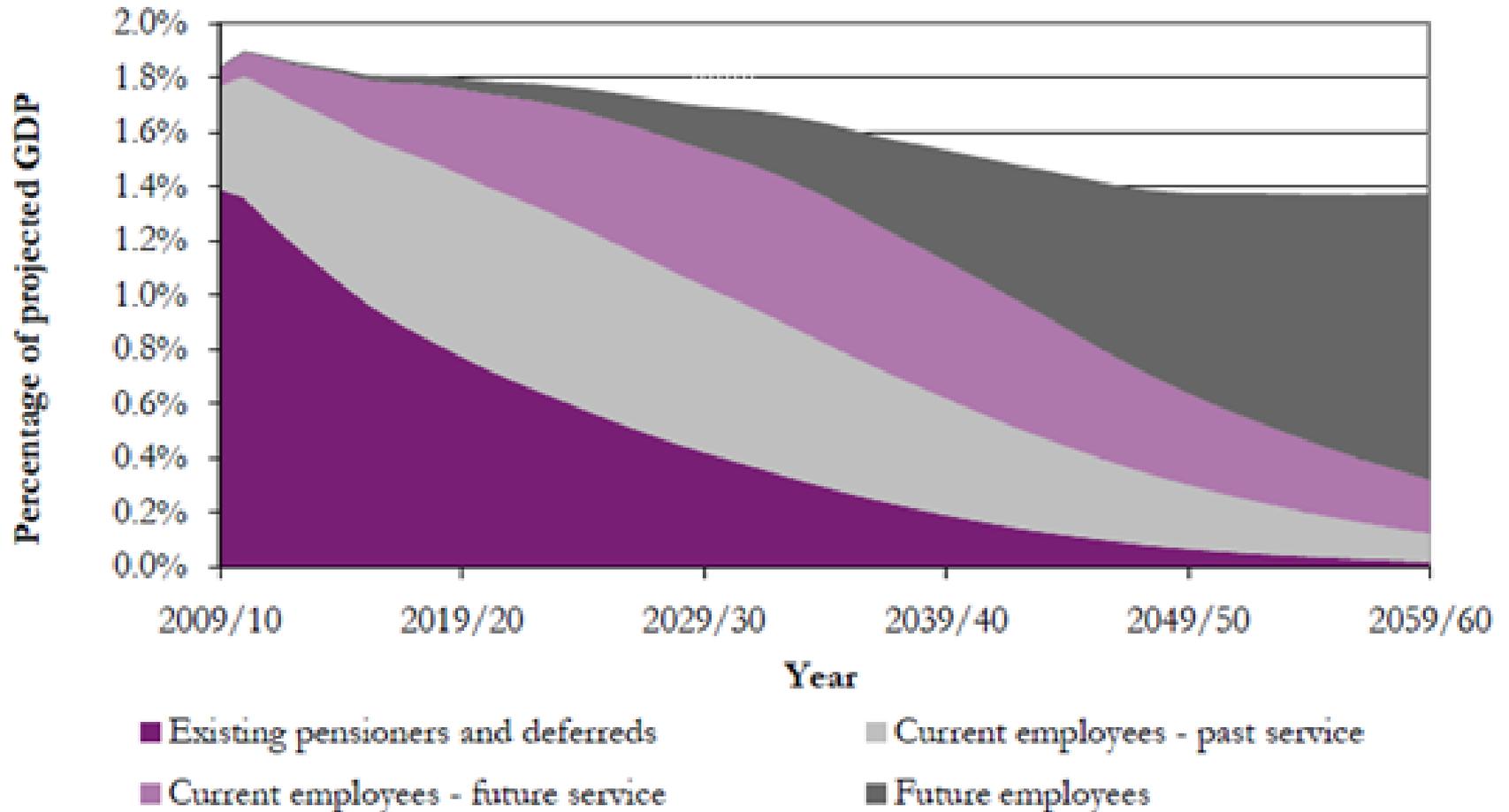


Source: *The cost of public service pensions*, National Audit Office. Figures from Resource Accounts 2009-10.

Summary of public service pension scheme reforms 2005-08

	NHS ^a	Teachers	Civil service ^b	LGPS (reformed for all members)	Armed forces	Police	Fire
Normal Pension Age (NPA)	60 → 65	60 → 65	60 → 65	Remains 65; Rule of 85 abolished for new service with transitional protection	No change from 55	50 with 25y service (below 50 with 30y); 55 (57 or 60 for higher ranks) → 55	55 (from 50 after 25y service) → 60
NPA for early leavers	Same as NPA	Same as NPA	Same as NPA	Same as NPA	60 → 65 (all members)	60 → 65	60 → 65
Basic design	Remains final salary	Remains final salary	Final salary → Career average	Remains final salary	Remains final salary	Remains final salary	Remains final salary
Accrual rate	80ths → 60ths	80ths → 60ths	60ths → 2.3%	80ths → 60ths	69ths (91ths after 22y ^c → 70ths)	60ths (30ths after 20y → 70ths)	60ths (30ths after 20y → 70ths)
Additional lump sum?	3x pension → commutation	3x pension → commutation	Commutation only	3x pension → commutation	No change from 3x pension	Commutation 4x pension	Commutation only
Late retirement enhancement?	No → Yes	No → Yes	No → Yes	No → Yes	No	No	No
Draw-down option	Yes	Yes (all members)	Yes (all members)	Yes	No	No	No
Rate of employee contributions ^d	6% (5%) → 5-8.5% (for all members)	6% → 6.4% (for all members)	No change from 3.5%	6% (5%) → 5.5%-7.5%	Remains non-contributory	11% → 9.5%	11% → 8.5%
Cost sharing?	Yes	Yes	Yes	Yes	No	No	No
Eligibility for survivor's pension	Now includes non-legal partners and payable for life (but only for new joiners in the police and fire schemes)						
Survivor's pension on death in retirement	Remains a 160ths pension	Remains a 160ths pension	160ths → 3/8ths of member's pension	Remains a 160ths pension	50% → 62.5% of member's pension	Remains a 50% of member's pension	Remains a 50% of member's pension
Ill-health benefit	1-tier → 2-tier	1-tier → 2-tier	Remains 2-tier	1-tier → 3-tier (proposed)	1-tier → 2-tier	1-tier → 2-tier	Remains 2-tier
Timescale	1 Apr 2008	1 Jan 2007	30 Jul 2007	1 April 2008	6 April 2005	6 April 2006	6 April 2006

Gross benefit expenditure by type of member



Source: GAD modelling for IPSPC.

Table B.1: Overview of the main public service pension schemes

Scheme	Name	Normal Pension Age	Min Pension Age	Members Contribution Rate	Employer Contribution Rate	Pension Basis	Accrual Rate	Lump Sum	Status
Principal Civil Service Pension Scheme	Classic (pre October 2002)	60	55 (50 prior to Apr 06)	1.5%	18.9% ¹	Final Salary	1/80	3 x annual pension	Closed
	Premium	60	55 (50 prior to Apr 06)	3.5%		Final Salary	1/60	Optional in exchange for reduced pension	Closed
	Partnership	55-75 ²		0 upwards ³	Minimum of 3%-12.5% depending on age ⁴	Annuity		Optional in exchange for reduced 'pot'	Open
	Nuvos (from July 2007)	65	55	3.5%		Career Average Earnings	1/43 ⁵	Optional in exchange for reduced pension	Open
Armed Forces	Armed Forces Pension Scheme 1975	55	38	Nil	29.4%	Final Salary	1/69-(1/91 for years 22+)	3 x annual pension	Closed
	Armed Forces Pension Scheme 2005	55	40	Nil		Final Salary	1/70	3 x annual pension	Open
Judges⁶	Judicial Pension Scheme 1981	65	Min 5 years service	1.8 – 2.4%	32.15%	Final Salary	1/40 or 1/80	2 x annual pension	Closed
	Judicial Pension Scheme 1993	65	Min 5 years service	1.8 %		Final Salary	1/40	2.25 x annual pension	Open
Police (England and Wales)	Police Pension Scheme 1987	55	48.5 (after 30 yrs)	11%	24.2%	Final Salary	1/60 (2/60 after 20 yrs capped at 40/60)	Optional in exchange for reduced pension	Closed
	Police Pension Scheme 2006	55	55	9.5%		Final Salary	1/70 (max 35/70)	4 x annual pension	Open

Firefighters (England and Wales)	Firefighters' Pension Scheme 1992	55	50	11%	26.5%	Final Salary	1/60-(2/60 after 20 yrs capped at 40/60)	Optional in exchange for reduced pension	Closed
	New Firefighters' Pension Scheme 2006	60	55	8.5%	14.2%	Final Salary	1/60 capped at 45/60	Optional in exchange for reduced pension	Open
National Health Service (England and Wales)	National Health Service Pension Scheme 1995	60	50	5-8.5% dependent on pay range	14.0%	Final Salary ⁷	1/80	3 x annual pension	Closed
	National Health Service Pension Scheme 2008	65	55	5-8.5% dependent on pay range		Final Salary	1/60	Optional in exchange for reduced pension	Open
Local Government Pension Scheme (England and Wales)	Local Government Pension Scheme 1997 ⁸	65	50 with 25 yrs service	5-6%	13.2% ⁹	Final Salary	1/80	3 x annual pension	Closed
	Local Government Pension Scheme 1 April 2008	65	55	5.5-7.5%		Final salary	1/60	Optional in exchange for reduced pension	Open
Teachers (England and Wales)	Teachers' Pension Scheme Before January 2007	60	55	6.4%	14.1%	Final Salary	1/80	3 x annual pension	Closed
	Teachers' Pension Scheme 2007	65	55	6.4%		Final Salary	1/60	Optional in exchange for reduced pension	Open