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Mr Shane McAteer
Clerk
Committee for Finance and Personnel
Room 419
Parliament Buildings
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Our Ref – CFP191/11-15

25 January 2012

**Dear Shane,**

**Public Sector Pensions Bill**

At the Committee meeting of 9 January 2013 officials agreed to send some additional information to Members in relation to the Public Sector Pensions Bill. This information is included below.

1. **Information on the areas/issues in which there would be scope to vary from the Whitehall approach.**

**<u>Scope for variance in the Bill – Primary Legislation</u>**

Civil Service Pensions, in conjunction with Departments and the Office of Legislative Counsel, is working on the Public Service Pensions Bill to be introduced in the Assembly. This Bill will provide the primary legislation required to enable the implementation of public service pension reforms, as agreed by the Executive on 8 March 2012. This Bill is a framework piece of legislation, which will determine the high level provisions to apply across the public sector in Northern Ireland. The Committee was provided with a written update on 4 January 2013, on plans for the introduction of the Bill, including the detail of the proposed core provisions, the decision by the Executive to adopt these pension reforms and the proposed timetable and policy consultation. In the light of the decision by the Executive, it is anticipated that the core provisions will be adopted in the Bill.

In line with normal Bill procedure, the Public Service Pensions Bill will be debated in the Assembly and will be subject to full Committee scrutiny. Public Service pension policy is devolved. However the approach has been to apply changes to public service pension schemes here in line with policy developed centrally for the equivalent schemes in Great Britain. HM Treasury funding projections are formulated on the presumption that the policy intention contained in the Westminster Public Service Pensions Bill will be applied in Northern Ireland, and on this basis any divergence from the policy contained in the Westminster Bill has potential for a financial impact. This approach across devolved administrations was also recommended by Lord Hutton in his review.

HM Treasury has also made clear that failure to implement the required pension reforms to the timescales outlined in the Westminster Public Service Pensions Bill would have a detrimental financial impact for Northern Ireland funding. The Minister of Finance and Personnel provided figures of the potential cost of non-implementation or delay to the Assembly on 26 November 2012. The cost of diverging from the policies or delaying their implementation could be in excess of £262m per year.

In summary therefore, variations could be made from the core provisions in the Westminster Bill, (detail of these already supplied in earlier written submission). Such variations would however need to be considered in the context of the Executive decision of 8th March, and on the understanding of the financial consequences.

**Scope for variance in scheme design - Secondary Legislation**

Secondary legislation will be required to amend the rules of each devolved public service pension scheme, to give effect to the reform measures carried in the Public Service Pensions Bill. This work will be taken forward by each of the Ministerial Departments which have individual responsibility for pension schemes. The secondary legislation will provide scope for each relevant Minister to consider what variations may be possible and appropriate for each of their schemes. Ministers are likely to give consideration to the approach taken to date in mirroring their comparable scheme in Great Britain when designing their Northern Ireland scheme and its regulations. The Coalition Government set out its preferred design for the schemes in Great Britain in November 2011[1](a copy of the preferred scheme design is attached at Annex A). Scope exists for schemes to vary from the scheme design in scheme regulations to suit the requirements of the individual workforces. Following consultations with scheme representatives and TUS, scheme specific designs were developed for members of the NHS, Civil Service, Teachers and Local Government pension schemes which incorporate variations while remaining based on the principles contained in the Government's preferred design.

Ministers will need to take account of keeping within the parameters of cost, the overall core provisions set out in the primary legislation and the costs of changing their IT systems. It should be noted that the IT systems used by main schemes here are modelled on the IT systems for the Great Britain scheme. Examples of variations at Secondary Legislation stage are set out below.

**Accrual Rate**

The accrual rate is the fractional rate at which benefits build up in the scheme. It is commonly expressed as a fraction of pensionable salary for each year. Example: For a teacher in a CARE scheme with an accrual rate of 1/57th who pays into the

[1] Public Service Pensions; Good pensions that last – published 20 November 2011, http://cdn.hm-treasury.gov.uk/pensions_publicservice_021111.pdf

scheme for 20 years, their pension will be 1/57th of their first year's salary, plus 1/57th of their second year's salary, plus 1/57th of their third year's salary etc, up to and including 1/57th of their final year's salary. Variances in accrual rates exist across schemes; examples of the rates for the Civil Service, NHS, Teachers and Local Government schemes which will be established under the Westminster Bill are set out below. These rates could be varied in their application to Northern Ireland: however, the financial consequences of doing so would need to be considered carefully as this is a key factor in the design of a scheme, in determining the financial viability of a scheme, and subsequent level of employers' and employees' contributions.

| **Scheme** | **Annual accrual rate** |
|---|---|
| Civil Service | 1/43.1 |
| NHS | 1/54 |
| Teachers | 1/57 |
| Local Government | 1/49 |

**Annual revaluation of pension benefits while in service**

Pension benefits accrued in public service schemes are uprated annually to take account of cost of living increases. Clause 9 of the Westminster Bill deals with the procedure for revaluing the accrued pension rights of active scheme members. This is **not** the uprating or indexation of pensions that are deferred or already in payment. In the Coalition Government's preferred scheme design benefits accrued by members who remain in service would be uprated in line with measured increases in earnings. Clause 9 of the Westminster Bill specifies that revaluation of pension benefits in service must be by reference to a change in prices or earnings (or both) in a given period. The Westminster Bill also contains provisions for HM Treasury to make orders to specify the percentage increase or decrease in prices or earnings for the purposes of this revaluation. Each of the proposed final scheme designs for the four main Great Britain schemes have agreed variances in the revaluation of benefits whilst remaining in service using the relevant HMT Treasury index measuring changes in consumer prices, as outlined in the table below:

| **Scheme** | **Annual rate for Revaluation of accrued benefits (active members)** |
|---|---|
| Civil Service | Consumer Prices Index (CPI) |
| NHS | CPI + 1.5% |
| Teachers | CPI +1.6% |
| Local Government | CPI |

The HM Treasury indices referenced in the Westminster Bill currently apply in the Northern Ireland Schemes and the policy intention is that the draft Public Service Pensions Bill will reflect the current position. However schemes will have autonomy to vary the application of the indices in the same way as has been illustrated for the Great Britain Schemes above.

## Employee contribution rate

The Coalition Government's preferred scheme design sets average member contributions for the unfunded public service pension schemes at the level of the existing schemes. This is after the full increase of 3.2 percentage points from the current programme to increases employee contributions for public service schemes has been applied. The Coalition Government announced at budget 2011 that employee contribution rates for public service pension schemes would be increased by an average 3.2 percentage points over 3 years by 2015. The average employee contribution rates which will apply in the Civil Service, NHS, and Teachers in Great Britain from April 2015 are set out in the proposed final agreements for each scheme and are reproduced below:

| **Scheme** | **Average employee contribution rate in CARE schemes at April 2015** |
|---|---|
| Civil Service | 5.6% |
| NHS | 9.8% |
| Teachers | 9.6% |

The Westminster Bill does not specify employee contribution rates for the schemes. The employee contribution rates will be determined in individual scheme regulations. The average rates specified in the table above are generally in line with the Coalition Government's preferred scheme design i.e. at the level of the existing schemes after the full increase of 3.2 percentage points from the programme to increase employee contributions for public service schemes has been applied, and within revised cost ceilings set by the Coalition Government in November 2011 for the Great Britain schemes.

The Departments which have policy responsibility for the Northern Ireland schemes will retain authority to vary the contribution rates which will apply in the CARE schemes from April 2015. This will be subject to the cost cap limits mechanism and the determination of scheme valuations. The financial consequences of any proposed variance at scheme level in contribution rates after April 2015 will need to be taken into account by each Minister who has responsibility for one of the public service schemes here.

## Lump sum payments

In the Coalition Government's preferred scheme design members would be given the option at retirement to convert £1 of annual pension into a £12 one-off lump sum payment in accordance with HMRC limits and regulations. This is known as commutation. The Westminster Bill does not specify the provisions which must apply in schemes for the provision of lump sum payment. Each of the Great Britain scheme designs offer some variation on the Coalition Government preferred design for optional commutation of pension to lump sum as outlined in the schemes proposed final agreements.

The Northern Ireland schemes currently contain provisions for commutation of pension to lump sum and will retain scope to vary these provisions, within the external limits and regulations imposed by HMRC, in the new schemes established under the proposed Assembly Bill.

**Ancillary benefits**

Ancillary benefits include dependant pensions, ill health benefits and death benefits. In line with the policy intention in the Westminster Bill (stated at clause 3) the proposed Assembly Bill will include provisions which enable Departments with responsibility for public service schemes to make provision in scheme regulations which are designed for different purposes or cases (including different provision for different descriptions of persons) and which take account of existing scheme differences. This scope for variation will extend to ancillary benefits.

However, variations to Northern Ireland scheme designs from their comparable scheme in Great Britain would have to be considered in the context of the overall scheme valuation which will be subject to provisions for the valuation and cost control set out in the Bill.

**Other areas where scope exists to vary from the Westminster approach**

**Re-employment -** Under the Westminster Bill schemes will retain authority in scheme regulations to vary provisions applying in schemes where members leave the scheme and rejoin. The Northern Ireland schemes will retain scope to vary these provisions in scheme regulations; and,

**Staff transfers -** The Westminster Bill contains new provisions which will enable members of public service pension schemes whose employment is subsequently transferred to the private sector to retain membership of the public service scheme operated by their previous employer.

This measure was recommended by the Public Service Pension Commission to promote increased plurality in the delivery of public services and the principle accepted by the Coalition Government following consultation on the existing Fair Deal mechanism which requires employers in the private sector to provide new employees transferring from public body employers with a broadly comparable pension arrangement. Schemes will be required to implement these provisions of the Westminster Bill in their scheme regulations.

The Assembly Public Service Pension Bill will contain equivalent provisions for the Northern Ireland schemes. Schemes will retain existing scope to vary processes for the transfer of employee benefits between public service schemes, subject to the application of existing statutory regulations for the transfer of pension rights.

In summary, schemes will have considerable scope to vary these factors at secondary legislation stage. In doing so, a key constraint will be any financial consequence.

**2. Information on the revised measures for management, regulation and administration of the various pension schemes.**

The Independent Public Service Pensions Commission identified a great variety of governance arrangements in the public service schemes. They flagged that the position contrasts with that of the trust based schemes in the private and public sector, which are required to have pension boards that are responsible for the operations of the schemes. The Pension regulator in turn plays an active role in overseeing the operation of trust based schemes and ensuring their compliance with pension's legislation.

The Commission recognised that there are valid reasons for the different governance models, but considered that lessons can be learned from the trustee model. They recommended that every public service pension scheme (and individual Local Government Pension Scheme fund) should have a properly constituted, trained and competent Pension Board, with member nominees, responsible for meeting good standards of governance, including effective administration. The Commission also recommended that a framework should be established to ensure independent oversight of governance, administration and data transparency of the public service pension schemes.

The Coalition Government accepted these recommendations. The intention is that every public service pension scheme with two members or more will be required to establish a Pension Board to ensure that the schemes are managed and administered effectively and efficiently. The Pension Regulator will be given a more active role in defining and regulating good standards of governance and administration in the public service pension schemes. Where the Pensions Regulators' existing powers relating to the administration and governance of pensions do not currently apply to the public schemes, they will be given equivalent powers.

The Department does not envisage that the cost of administering the schemes will increase as a result of these changes. Schemes should already be compliant with legislation and achieving good standards of administration. The changes are concerned with providing members and other taxpayers with assurance that those standards are being met across all schemes. There will be new costs for the Pensions regulator's role but the Department expects these to be insignificant.

For further reference, Clauses 4 – 7 of the Westminster Public Service Pensions Bill details the provisions on Governance and Pension Boards. www.publications.parliament.uk/pa/bills/lbill/2012-2013/0077/2013077.pdf

Officials are available and willing to provide further clarification as required.

Yours sincerely,

Ch. Pauley

**CHRISTINE PAULEY**
**Acting Departmental Assembly Liaison Officer**

**ANNEX A**

**Government preferred scheme design for:**

- **Scheme model -** a Career Average Revalued Earnings (CARE) pension scheme;
- **Accrual rate -** Public service workers benefits to be earned at a rate of 1/60ths of pensionable earnings each year;
- **Revaluation of accrued benefits while in service -** Public service workers will have their benefits increased each year they are working in the public services in line with earnings revaluation;
- **Scheme pension age -** a Normal Pension Age linked to State Pension Age (or 65, whichever is higher);
- **Revaluation of pensions in payment -** pensions in payment to increase in line with the Consumer Prices Index (CPI);
- **Revaluation of deferred benefits -** benefits earned by leavers to increase by CPI from the date of leaving until retirement;
- **Employee contribution rate -** average member contributions for the unfunded public service pension schemes set at the level of the existing schemes after the full increase of 3.2 percentage points from the current programme to increases employee contributions for public service schemes has been applied;
- **Additional scope for funded schemes -** in the funded Local Government Pension Scheme both member contributions and other adjustments to benefits would be reflected in cost ceilings following the outcome of the consultations on alternatives to contribution increases.
- **Lump sum payments -** members given the option at retirement to convert £1 of annual pension into a £12 one-off lump sum payment in accordance with HMRC limits and regulations;
- **Ancillary benefits -** ill-health, death and survivors benefits (ancillary benefits) to match those currently provided by schemes that are open to new members;
- **Re-employment -** members who leave the scheme and rejoin within 5 years to be able to link their new service with previous service, as if they had always been an active member;
- **Staff transfers -**members transferring between public service schemes to be treated as having continuous active service (which would include those transferring between schemes who had rejoined public service after a gap of less than 5 years); and,
- **Employer cost cap -** an employer contribution cap to provide backstop protection to the taxpayer against unforeseen costs and risks.