Pensions Committee

2pm, Tuesday, 18 December 2012

Regulatory Update including Public Service Pensions Bill

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Executive summary

Regulatory Update including Public Service Pensions Bill

Summary

This report provides an update on pensions regulations:-

- The draft Public Service Pensions Bill is making its way through the UK Parliament. It could have significant implications for Lothian Pension Fund.
- Scottish Government has consulted on changes to the regulations affecting the administration of Lothian Pension Fund.

Recommendations

Pensions Committee should note the regulatory update in this report, the significant implications for Lothian Pension Fund of the Public Service Pensions Bill and the tight timescales for implementation of a new LGPS in Scotland.

Measures of success

This report is purely advisory at this stage.

Financial impact

There are no financial implications arising directly from this report. Future legislative change to the design of the Local Government Pension Scheme, however, will have financial consequences for Lothian Pension Fund and participating employers. These are currently unknown and will be addressed in future reports to the Pensions Committee.

Equalities impact

There are no adverse equalities impacts arising from this report. Changes to the LGPS would be expected to be equalities tested by the Scottish Government.

Sustainability impact

There are no adverse sustainability impacts arising from this report. The Public Service Pensions Bill aims to make pensions more sustainable.

Consultation and engagement

Lothian Pension Fund is committed, on an ongoing basis, to keeping its employers and members fully informed of all the key developments on reform of the LGPS in Scotland. Regular bulletins have been issued to all employers, supplemented by meetings with senior management of certain larger employers. Pension reform also featured prominently as a topic in the Fund's Annual Employer Seminar, which was held on 6 December 2012.

Background reading / external references

The Public Service Pensions Bill and its progress through Parliament to eventual enactment can be viewed at http://services.parliament.uk/bills/2012-13/publicservicepensions.html.

Proposals for a new LGPS design in England and Wales can be viewed at http://www.lgps.org.uk/lge/core/page.do?pageId=15431012.

The response from the Scottish Pensions Liaison Group to the consultation on the draft Local Government Pension Scheme (Miscellaneous Amendments) (Scotland) Regulations 2013 is provided at http://www.lpf.org.uk/regs2013.

Report

Regulatory Update including Public Service Pensions Bill

1. Background

1.1 The Independent Public Sector Pensions Commission, chaired by Lord Hutton, published its report in March 2011. This report (the "Hutton Review") made a number of recommendations for fundamental change to UK public service pension provision.

2. Main report

2.1 The Public Service Pensions Bill ("the Bill") was published by the UK Government on 13 September 2012. The Bill passed its second reading on 29 October 2012. Should this Bill be enacted, then there would be significant changes required to the design and governance of the Local Government Pension Scheme (LGPS) in Scotland.

2.2 Specifically, the Public Service Pension Bill embodies the key recommendations of Lord Hutton's Independent Public Sector Pensions Commission, published in March 2011, namely:

- The end of final salary benefit arrangements;
- Retirement age linked to State Pension Age (SPA);
- Cost control system to provide affordability and sustainability;
- Measures to strengthen governance.

What does the Bill cover?

2.3 The Bill sets out a common framework for pension arrangements for the civil service, judiciary, local government, teachers, NHS, fire services, armed forces and members of the police.

Further detail as to the scope and provisions of the Bill is provided below:

Future service benefit structure

2.4 Although the actual design and benefit structure applicable to the individual public service schemes will be set out in regulations, the Bill confirms that any defined benefits under the new schemes must be provided on a Career Average Revalued Earnings (CARE) basis, a more detailed description from The Pensions Advisory Service is below from 2.5 to 2.7. Schemes (other than fire, police and armed forces), must also provide members with a normal pension age which is aligned to their state pension age or age 65 (whichever is higher). How the increase to members’ state pension age is reflected in the individual schemes remains a matter for scheme regulations.

2.5 A career average revalued earnings (CARE) scheme is a type of defined benefit arrangement. It is set up by an employer to provide income in retirement for its employees.

2.6 Although the employer is responsible for sponsoring the scheme, it is run by a board of trustees (with the exception of most public sector schemes). The Trustees are responsible for paying retirement and death benefits.

2.7 Members contribute to the scheme with the promise of a certain level of pension. The amount of pension payable is dependent upon:

- the length of time served in the scheme (known as pensionable service);
- career averaged earnings [* see below]; and
- the scheme's accrual rate. The accrual rate is the proportion of salary that is received for each year of service.

  * A career average scheme matches each year's benefit accrual to earnings in each year rather than the final years' earnings. The earnings figure will be uprated in line with prices rather than the actual increase in earnings.

  For example, if the scheme provides a pension calculated as 1/60 of pay for each year of service and the member retires in 2010 with 30 years' service, then to calculate pension, each year's pay will be uprated with inflation and then aggregated. It will then be divided by 30 to provide the "average" pay, which in the example would be multiplied by 30/60 to arrive at the pension.

Closure of current schemes

2.8 The Bill provides that the existing schemes will be closed to future accrual with effect from 5 April 2015 (or 1 April 2014 in the case of the LGPS in England and Wales). It also addresses certain transitional issues.

2.9 In particular, the Bill enables schemes to provide that members who are a certain number of years from their normal pension age on 1 April 2012 will not see any change to their retirement age, or any decrease in the amount of pension they receive on retirement. In addition, the benefits which will have accrued in the current scheme will continue to be linked to his/her final salary when they eventually leave continuous service.

Capping costs

2.10 One of Lord Hutton's key recommendations was a scheme-specific mechanism to ensure costs are kept below specified levels. The basis for such an "employer cost cap" is set out in the Bill, with the intention being that HM Treasury will make regulations to amend schemes where necessary to keep costs within the set margins.

2.11 The Bill further envisages HM Treasury issuing directions as to how valuations are undertaken by the schemes, including when setting the employer cost cap. LGPS funds have not previously had such oversight from HM Treasury when completing their triennial actuarial valuations. CIPFA has already expressed its criticism of this specific proposal.

Governance

2.12 The Bill also sets out new provisions for the overall governance and regulation of the public service pension schemes.

2.13 Each scheme will have its own 'manager' with responsibility for scheme administration, together with a pension board to assist the manager. The remit of the pension boards will be to ensure compliance with legislation, codes of practice and regulatory issues.

2.14 Until now, there has not been a body responsible for the overall regulation of all public service pension schemes. The Bill, however, extends the Pension Regulator's remit to all public service schemes. Accordingly, the Pensions Regulator will be able to issue codes of practice in respect of the public service schemes and require scheme managers to implement internal control procedures in respect of the administration and management of the schemes.

Access to public service pension schemes

2.15 The Bill contains provision which will enable public service pension schemes to allow non-public service workers to participate in the scheme. This reflects the scope for private sector contractors to be admitted to the public service schemes. Again, the detail and terms on which this will be permitted will be a matter for individual scheme regulations.

Timescales

2.16 The Government has indicated that the reforms to public service pension schemes constitute a settlement for a generation. As a result there is a protected period of 25 years from 1 April 2015 during which changes cannot be made, for example, to benefit accrual or contribution rates unless there is consultation with affected persons with a view to reaching agreement on the changes. Importantly, this procedure does not apply where changes are needed to keep the schemes within the employer cost cap.

2.17 This is a very significant Bill which will put Lord Hutton's recommendations onto a statutory footing. The Bill is expected to work its way through the UK Parliament before being enacted sometime during 2013. Individual schemes will then issue the regulations specifying benefit structures and governance arrangements ahead of the latest commencement date for the new schemes – being 6 April 2015 (or 1 April 2014 for the LGPS in England and Wales).

Reform of the LGPS in England and Wales

2.18 Proposals for a new LGPS design in England and Wales have already been published. Consultation responses from the Local Government Association (LGA), UNISON, GMB and Unite have endorsed the proposals for a reformed LGPS and approval by the Government is expected shortly.

LGPS in Scotland

2.19 Pensions policy is a reserved matter for the five main public sector pension schemes, including the LGPS in Scotland. Once enacted, the Public Service Pensions Bill would become primary legislation. Scottish Ministers have been given 'executive devolved competence' to determine scheme specific regulations for the LGPS in Scotland. These regulations, however, must comply with UK legislation.

2.20 Initial meetings of the Scottish Local Government Pensions Advisory Group (SLOGPAG) have been held to consider the implications of the Bill and address future reform requirements. SLOGPAG has tripartite representation from the Scottish Government, Trade Unions and CoSLA, supplemented by pension manager support.

2.21 Unison has stated that it has obtained legal advice that the Bill would require a Legislative Consent Motion (LCM) in the Scottish Parliament in order to change the LGPS. Scottish Government officials have asserted that this is not the case.

2.22 The timeframe for implementation of a new scheme design by the Bill deadline of April 2015 is extremely tight. The Scottish Government has indicated that it is hopeful that the requisite negotiation, regulation writing and pre-implementation preparation phases could run concurrently, to a certain degree, but this is by no means guaranteed.

Regulatory Update – General

2.23 In October 2012, the Scottish Public Pensions Agency (SPPA) issued for consultation the draft Local Government Pension Scheme (Miscellaneous Amendments)(Scotland) Regulations 2013. The main changes relate to the Annual Allowance (Scheme Pays option) and to the alignment of the LGPS regulations with Auto-Enrolment pension legislation. Other proposed amendments should serve to clarify the interpretation of existing provisions.

2.24 A response to the consultation, on behalf of all the LGPS administering authorities in Scotland, has been submitted by the Scottish Pensions Liaison Group. This is available on the Lothian Pension Fund web-site, through the hyperlink provided below at “Background reading / external references”.

3. Recommendations

1. Pensions Committee should note the regulatory update in this report, the significant implications for Lothian Pension Fund of the Public Service Pensions Bill and the tight timescales for implementation of a new LGPS in Scotland.

4. Background reading / external references

The Public Sector Pensions Bill and its progress through Parliament to eventual enactment can be viewed at http://services.parliament.uk/bills/2012-13/publicservicepensions.html.

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Single Outcome Agreement	
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