

FALKIRK COUNCIL

Subject: AUDIT SCOTLAND REPORT – THE COST OF PUBLIC SECTOR PENSIONS IN SCOTLAND
Meeting: AUDIT COMMITTEE
Date: 21 March 2011
Author: DIRECTOR OF FINANCE

1. INTRODUCTION

- 1.1 This report outlines the findings of an Audit Scotland review of Public Sector Pensions in Scotland and places it in the context of a range of developments that are impacting on the Local Government Pension Scheme [LGPS].

2. BACKGROUND

- 2.1 The report covers the six main public sector schemes:-

- LGPS
- Teachers (STSS)
- NHS
- Civil Service
- Police
- Firefighters

Around one million people in Scotland have a direct interest in one of the schemes, either as members, pensioners or dependents.

[A copy of the full report may be obtained by contacting the Director of Finance]

- 2.2 The LGPS is unique in so far as it is the only scheme which is funded – the others are all “pay-as-you-go” with no fund built up to cover future pension payments.
- 2.3 In 2009/10 the six schemes paid out £2.8B to pensioners whilst public bodies contributed £2.2B and employees £814M to meet the cost of benefits. These costs are significant in terms of both the Scottish budget and the budgets of individual public bodies and in consequence it is important the schemes are well managed and controlled.

3. REPORT CONTENT

- 3.1 The report makes a number of observations based on the statistical data gathered. However, all of the trends revealed are already well known and considered in greater depth in the Hutton review [see section 4]:-

- There is a disparity of pension provision between the public and private sectors
- The fragmented nature of female career patterns mean that the average pension for women is half that of men;
- The average annual teacher's pension is £10,200, whereas the average LGPS pension is £4,750, reflecting the fact that many LGPS members are part time with shorter service.
- There is evidence of improved longevity amongst pensioners - there has been a 12% rise in the number of pensioners in the past 5 years
- The report notes the financial pressures on schemes in terms of improvements in longevity and falling gilt yields, but recognises that the indexation of pensions according to CPI rather than RPI will offer some financial easement.
- The report acknowledges the scheme reforms of recent years
- There is recognition that a Career Average Scheme would be fairer to all members than a final salary arrangement
- Of particular concern are cost pressures impacting on the unfunded schemes. Pension payments from these schemes (i.e. not the LGPS) have increased by 32% in real terms in the past 5 years and the gap between income and expenditure is continuing to grow.
- The schemes were generally well administered, but governance arrangements in the smaller LGPS could be improved

3.2 The report notes that whilst pensions policy is generally reserved to Westminster, the Scottish Government retains some influence and jurisdiction over the process including the power to make secondary legislation. The key recommendations from the report are that the Scottish Government:

- Provide a clear statement on aims and objectives of the schemes in Scotland
- Provide improved scrutiny of pension provision through the use of experts
- Investigate whether differences in contribution rates between the schemes are justified
- Ensure UK scheme changes are incorporated into Scottish schemes
- Have a clear policy on setting a cap on employer contributions
- Decide the extent and pace of reform of LGPS

3.3 There are some areas where the report could have extended its content to provide a more rounded view:-

- It offers no comment on the impact of contributions increases on employee relations, including the potential for significant opting-out which could have a negative effect on scheme liabilities
- It does not consider the impact of a shrinking of scheme membership on cashflow and employer contributions through the current round of severances
- It does not acknowledge that LGPS members are the only public sector members to have suffered an adverse change in their ongoing benefit entitlement. All other schemes applied their reforms to new members.
- The statement that the Scottish Public Pensions Agency (SPPA) has a much lower administration cost than local authority funds should have been balanced by a statement that the local authorities undertake a wider range of activities (e.g. support to employers, etc).

4. CONTEXT

- 4.1 There are a number of developments which are impacting on the LGPS and in consequence on the workload of the Pensions and Payroll Division. They are touched upon in this and in the following paragraphs. The first, and most significant, is the Hutton review of public sector pensions at the UK level. The publication of the Hutton report is concurrent with this report and is expected to recommend changes including a move away from a final salary to a career average scheme and increased contributions from employees.
- 4.2 The Pathfinder review is sponsored by the Scottish Government, the Improvement Service and COSLA and is assessing the merits of consolidating the 11 existing Scottish LGPS's into between one and three schemes. This may apply to the Administration or Investment responsibilities, or both. The findings are expected in the summer.
- 4.3 The SPPA are expected to issue Regulations shortly which will revise the corporate governance arrangements for the LGPS funds and is likely to require greater engagement and communication with stakeholders.
- 4.4 LGPS funds with effect from 2010/11 are now required to produce separate annual reports and financial statements which will be subject to separate audit.
- 4.5 Employers in the Falkirk Fund are now placing significant demands on the Payroll and Pensions Division to process voluntary severance calculations and this is likely to continue into the future.

5. CONCLUSIONS

The report is a useful commentary on the current standing of the six schemes in Scotland and makes several recommendations to the Scottish Government to improve the cost, scrutiny and governance of the schemes. The report, however, is likely to be overtaken by the structural reforms being proposed by Hutton and potential changes flowing from the Pathfinder review.

6. RECOMMENDATION

The Audit Committee is invited to note the report.

pp Director of Finance

Date: 9 March 2011

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LIST OF BACKGROUND PAPERS

NIL