

# Independent Public Service Pensions Commission

## Final Report – 10<sup>th</sup> March, 2011

### Background

Lord Hutton has recently published his final report setting out how he thinks public sector pension schemes should be reformed to make them affordable, sustainable and fair to both scheme members and taxpayers.

The schemes covered by the review are as follows:

- Local Government Pension Scheme,
- Teachers Pension Scheme
- NHS Pension Scheme
- Police and Fire Pension Schemes
- Armed Forces Pension Scheme
- Civil Service Pension Scheme

The report contains 27 specific recommendations and it will now be up to the UK Government to decide the extent and pace of change, including the level of benefits to be provided under any new pension arrangements.

### Recommendations

The main recommendations are as follows:

- the current final salary schemes should be replaced with career average schemes
- the new career average schemes should be put in place by 2015
- current members should be moved to the new schemes in respect of future service
- pension rights built up so far should be protected and their final salary link maintained
- normal pension age (i.e. the age at which benefits can be taken without penalty) should be linked to the State Pension Age and will therefore rise over time. State Pension Age is scheduled to rise to 66 by 2020 and ultimately to age 68 by 2046.
- normal pension age for Police, Fire and Armed Forces should be age 60
- tiered employee contributions should be a feature of the new arrangements (this currently exists in the Local Government Pension Scheme)
- employer contributions should be capped at a level to be decided by Government. Where scheme costs increased beyond this level, higher employee contributions or reduced benefits would be necessary (some schemes already have these “cap and share” arrangements)
- any new arrangements should not be open to non-public service employees
- governance at a local level should be strengthened by the introduction of Pension Boards with member representatives
- governance at a national level should be strengthened and overseen by an independent body such as the Pensions Regulator
- the economic cost of the schemes should be published regularly by the Office of Budget Responsibility

- Consultation on scheme changes should be co-ordinated by Government and conducted on a scheme by scheme basis involving employees and their representatives

The recommendations are in addition to previously stated Government policies to increase future public sector pensions by reference to the Consumer Price Index and to implement increases to employee contributions over the next few years.

### **Final salary versus career average**

One of the key recommendations of Hutton is that the current final salary schemes should be replaced with career average schemes.

Most public sector schemes currently provide retirement benefits on a final salary basis, which means that the pension is guaranteed to be a fixed proportion of earnings on retirement. For example, if you retire after 40 years service on a pay of £20,000, your pension would be 40/60ths of £20,000<sup>1</sup>. The “60ths” component is known as the “accrual rate” and determines the amount of pension provided for each year of service.

Under the career average model, you earn a specific amount of pension each year based on your earnings that year. This amount is then revalued during your career to keep pace with inflation. The pension that you eventually get on retiring is the total of all the individual “years” of pension you have earned, with each year of pension having been suitably revalued. In this way, the pension is based on a person’s average pay over their career rather than being linked to their rate of pay at the end of their career.

### **Summary**

The Hutton report makes far reaching recommendations about the future of public sector pensions.

If implemented, the changes will represent the most fundamental overhaul of the schemes since their inception in the early 20<sup>th</sup> century.

As an employee in the public sector, the recommendations have the potential to significantly affect your future retirement benefits. However, further announcements and detail will be needed from Government before the extent of change can be fully assessed.

Look out for updates about future developments on the Falkirk Council pensions web pages at [www.falkirk.gov.uk/pensions](http://www.falkirk.gov.uk/pensions).

Pensions Section  
Falkirk Council  
12<sup>th</sup> March, 2011

<sup>1</sup> - A “60ths” accrual rate has been assumed for the purposes of the illustration, although it should be noted that prior to 1/4/2009, the Local Government Pension Scheme was based on “80ths” and with the provision of an automatic lump sum of three times the pension. Most members will currently have their benefits based on a mixture of 80ths and 60ths.