

STATES OF JERSEY



PUBLIC SECTOR PENSION REFORM (S.R.4/2014): RESPONSE OF THE STATES EMPLOYMENT BOARD

**Presented to the States on 27th May 2014
by the States Employment Board**

STATES GREFFE

**PUBLIC SECTOR PENSION REFORM (S.R.4/2014): RESPONSE OF THE
STATES EMPLOYMENT BOARD**

Ministerial Response to: S.R.4/2014

Ministerial Response required by: 23rd June 2014

Review title: Public Sector Pension Reform

Scrutiny Panel: Corporate Services Scrutiny Panel

INTRODUCTION

The Corporate Services Scrutiny Panel review of the Public Sector Pension Reform is welcomed. It is reassuring that, after a detailed review conducted by Scrutiny's appointed adviser, the Scrutiny Panel has concluded the rationale for a move from a final salary scheme to a Career Average Revalued Earnings (CARE) scheme is compelling. It is also reassuring that the Panel have concluded that the debate on the Law should continue as there is some urgency to deal with the increasing costs that the Scheme is facing due to improving longevity.

The Panel have requested that confirmation is provided that the proposals are affordable in advance of the debate on the Law. The proposals have been developed using prudent assumptions with a view as to what is affordable for the States in the long term. It is proposed that the additional costs will be met from within existing budgets. An employer cost cap will be introduced, giving certainty to the States in terms of future contributions. This cost cap has been proposed at an affordable level with the long-term States income and expenditure projections in mind. The proposed cost cap is expressed as a percentage of pensionable earnings (16.5%) which means that actual costs can be managed by efficiency savings within existing budgets. The introduction of a formal employer cost cap at a level that has been proposed to be affordable in the long term, and the ability to manage actual costs through efficiency savings, provides affordability into the long term.

Many of the Scrutiny recommendations are of a detailed nature relating to the Regulations, and do not affect the debate on the Law which is an enabling Law. This means that the Treasury, on behalf of the States Employment Board, can undertake further detailed work to consider and fully evaluate the proposals made by Scrutiny. The provisions of the enabling Law do not prevent the Scrutiny comments being taken into account. The States Employment Board will be considering these recommendations and will respond formally to Scrutiny by 23rd June 2014. The States will debate the Regulations later this year.

FINDINGS

	Findings	Comments
1	Adoption of the draft Law would effectively provide in-principle approval for the move from a final salary scheme to a Career Average Revalued Earnings (CARE) scheme. The rationale for such a move is compelling and the debate on the draft Law should therefore proceed, albeit with the caveat that the details of how the scheme will operate will not be agreed until the draft Regulations have been finalised.	<p>Agreed. This is a helpful comment and is welcomed. The final salary pension scheme is no longer affordable. Increasing longevity is placing a funding pressure on the Scheme. There is a contribution shortfall for every new member joining the Scheme. The problem is growing and needs to be addressed.</p> <p>The Career Average Revalued Earnings (CARE) Scheme proposed has been developed to address the issues facing the Scheme and provide a Sustainable, Affordable and Fair pension scheme for the future. The rationale for the move to CARE is indeed compelling.</p> <p>The Law is an enabling Law and the details of how the scheme will operate will indeed be contained in Regulations which will be debated by the States later in the year.</p>
2	Further evidence is required in respect of the affordability of the proposed employer's contribution cap in the long term.	The current base budget allocations and departmental efficiency savings will fund the employer contributions required. The provision of an employer cost cap will, for the first time, provide certainty to the States of the costs it could be asked to pay in the future. The employer cost cap has been proposed at a level which is affordable within the Long-Term Revenue Plans for the States.
3	Further clarity is required regarding the manner in which Article 8(1) of the draft Law would be applied.	This Article refers to how retrospective changes can be made, and has been developed to ensure that non-contentious changes to Regulations resulting from other tax or regulatory matters can be dealt with quickly and efficiently, whilst retrospective changes of a contentious nature will require the consent of representative bodies.
4	It would be beneficial for Regulations under the draft Law to include, in respect of the CARE scheme, provisions in relation to investment strategies, prudent and best-estimate funding assumptions; and the declaration of conflicts of interest.	<p>The Regulations will include provisions regarding the investment strategy, funding strategy and declaration of conflicts of interest.</p> <p>Consideration should be given as to whether the level of prudence in the assumptions should be specified in the Regulations, as this may have wider implications in terms of the operation and decision-making around the risk-sharing arrangements.</p>

	Findings	Comments
5	The aim to implement the proposed CARE scheme on 1st January 2015 means that the development and consideration of the draft Regulations will be undertaken within a very tight timescale. Sufficient time must be allowed for those Regulations to be considered.	The drafting of Regulations is well underway, The Pension Review team are supported by a dedicated Law Drafting resource. Regulations will be shared with the Committee of Management, and discussions have taken place in respect of the content of the Regulations. The Committee of Management have committed to reviewing the Regulations promptly.
6	Further information and analysis is required in respect of the cost comparison between PECRS and the proposed CARE scheme; the sensitivity of the results to the assumptions underlying the calculation of the anticipated contribution rates; and the quantification of risks of underfunding within the CARE scheme.	The Scheme Actuary has been requested to provide this analysis, which will be available in advance of a formal response required by 23rd June 2014.
7	The concept of prudence within the funding assumptions to be used under the proposed CARE scheme should be clearly established.	Following receipt of the further analysis being conducted by the Scheme Actuary, consideration will be given as to how this could be clearly established within the Regulations or via alternative mechanisms.
8	Some of the protections which would be afforded to current members of PECRS in the move to a CARE scheme are essentially unfair. They appear to have been included for pragmatic reasons to ensure the proposed reforms would be acceptable to employees.	During negotiations it was clear that offering protection to those closest to retirement was something the trade unions felt very strongly about. The length of protections offered are similar to those offered within UK public sector pension schemes which are also moving to Career Average. Providing protection to those within 7 years of retirement was a pragmatic decision to allow these important changes to be progressed.
9	Appropriate provision needs to be made within the draft Regulations for the circumstances in which Admitted Bodies to the CARE scheme wished to leave the scheme.	The Scheme Actuary would provide advice on the implications of an Admitted Body leaving the Scheme. Advice will be sought from the Scheme Actuary as to whether there is a need to provide for these situations within the Regulations.

	Findings	Comments
10	It is not ideal for both the PECRS and CARE scheme Committee of Management and the States Employment Board (as employer) to receive actuarial advice on the choice and prudence of assumptions from the same actuarial firm, since there is a risk that the advice may not be, or be seen to be, completely independent.	<p>The Committee of Management receive actuarial advice from the Scheme Actuary based in Epsom. The States Employment Board receives actuarial advice from the Employers Actuary based in Bristol. Whilst both are employed by the same actuarial firm, they are different teams separated by Chinese walls.</p> <p>The 2 teams have different roles and provide advice accordingly. The use of the same actuarial firm facilitates the transfer of base data between teams for use in calculations. This also enables actuarial advice to be provided more cost effectively.</p>
11	There needs to be clarity regarding the administration costs arising from implementation of the CARE scheme, and confidence that the staff resources would be sufficient and adequately trained. These are matters which will be pursued during Phase 2 of the Scrutiny Review.	The Committee of Management have agreed to fund additional temporary resources to support the implementation of the CARE Scheme. The Dedicated Pensions Unit has an industry standard pension administration system that is used by many large pension schemes in the UK. The system can be adapted to administer a career average pension schemes. The software supplier is aware of the implementation date and work has commenced on a system specification.
12	Notwithstanding the large amount of communication which has taken place, care should be taken to ensure that communication with members of PECRS is not inadvertently misleading about the status of the proposed reforms.	Agreed. It is important that communications to scheme members are accurate and understandable. The Pension Review team is taking actuarial and legal advice regarding communication materials.

RECOMMENDATIONS

	Recommendations	To	Accept/ Reject	Comments	Target date of action/ completion
1	Prior to the debate on the draft Law (and the accompanying amendments), the States Employment Board should ensure the States Assembly is provided with sufficient evidence on the affordability of the proposed employer's contribution cap.	SEB	Accept	<p>The employer is currently committed to paying 15.6% of pensionable salaries to fund public service pensions. At present, 2% of this is being used to repay the Pre-1987 debt, but the intention has always been that this would go to funding existing benefits once the debt had been repaid. At the time of this agreement, the arrangement was affordable, but that is no longer the case. The full 15.6% of pensionable salaries is now required to fund the benefits package, and in fact 16% is required for the CARE proposals to be sustainable, affordable and fair. That is an additional 0.4% of pensionable salaries (£1 million per annum).</p> <p>A further 2% of pensionable salaries (£5 million per annum) is required to fund the existing States commitment to repay the Pre-1987 debt.</p> <p>Funding for the current level of employer contributions is included within base budgets, and any additional employer costs resulting from the introduction of the CARE Scheme will be met from departmental savings.</p> <p>In total, an additional £6 million per annum is required. This will be funded by corresponding departmental efficiency savings, as highlighted to the Council of Ministers when presented with the draft Law. Departments will make efficiency savings to fund the proposals. The saving requirement will be phased in over 2 years – £2 million in 2015 and a further £4 million in 2016. This phased introduction of the savings will</p>	19/05/15

	Recommendations	To	Accept/ Reject	Comments	Target date of action/ completion
				<p>enable Departments to plan ahead the efficiency measures required and make the proposals affordable.</p> <p>A greater concern would be if these changes are not made. There is currently insufficient funding going into the scheme to fund the benefits being promised. There is no formal employer cost cap within the current Regulations and the States could be asked to pay more. The employer cost cap proposed will provide certainty to the States and be expressed as a percentage of pensionable earnings. So, if the States makes efficiencies in the future, the cost of providing pensions will be less.</p> <p>Employer contributions at the level proposed will be included within the States' Long-Term Revenue Plans.</p>	
2	The States Employment Board should clarify the policy that would be followed in the application of Article 8(1) of the draft Law.	SEB	Accept	<p>This has been included to allow non-contentious retrospective changes of a technical nature to be implemented without the need for the consent of scheme members. The wording followed is similar to adopted in UK. The administration of pension schemes is complex, and sometimes it is necessary to make changes retrospectively as a result of tax or other regulatory changes. These provisions allow for these changes to be made by the Chief Minister, following consultation and after receipt of the necessary actuarial and legal advice.</p> <p>The States Employment Board will consider whether a policy on the application of Article 8(1) is required in advance of making a formal response by 23rd June.</p>	23/06/14

	Recommendations	To	Accept/ Reject	Comments	Target date of action/ completion
3	The States Employment Board should clarify whether and how provision will be made in Regulations for the matters identified by Scrutiny's expert advisor.	SEB	Accept	The States Employment Board will consider whether/how the provisions identified should be contained in the Regulations and a response will be provided by 23rd June.	23/06/14
4	The States Employment Board should take appropriate steps to ensure that additional information and analysis identified by Scrutiny's expert advisor is made available before the draft Regulations are debated.	SEB	Accept	The States Employment Board will consider the additional analysis being completed by the Scheme Actuary in advance of making a formal response by 23rd June.	23/06/14
5	The States Employment Board should ensure that the Regulations underpinning the proposed CARE scheme incorporate the concept of prudence being used within the funding assumptions.	SEB	Accept	The States Employment Board will consider the impact of including the level of prudence in the Regulations in advance of making a formal response by 23rd June.	23/06/14
6	The States Employment Board should ensure that the draft Regulations make appropriate provision for the mechanism which would apply if one of the Admitted Bodies to the CARE scheme wished to leave the scheme.	SEB	Accept	Under the current Regulations there are provisions for an Admitted Body leaving the Scheme, and there will be similar provisions applied in the new Regulations. The States Employment Board will consider if further provision is required.	23/06/14

	Recommendations	To	Accept/ Reject	Comments	Target date of action/ completion
7	The States Employment Board should take appropriate steps to ensure that, from 1st January 2015, actuarial advice to the Board and to the PECRS Committee of Management on the choice and prudence of assumptions, is provided by separate actuarial firms.	SEB	Accept	The States Employment Board will consider the recommendation regarding future actuarial advice in advance of making a formal response by 23rd June.	23/06/14

CONCLUSION

The Corporate Services Scrutiny Panel review of the Public Sector Pension Reform provides a welcome review of proposals that are of long-term significance to the Island. Adoption of the draft Law will provide an in-principle approval for a move from a final salary scheme to a Career Average Revalued Earnings (CARE) Scheme. It is reassuring that Scrutiny have concluded that “the rationale for such a move is compelling and that the debate on the Law should therefore proceed”.

The Panel have requested confirmation that the proposals are affordable in advance of the debate on the Law. The proposals have been developed using prudent assumptions with a view as to what is affordable for the States in the long term. A cost cap has been proposed at an affordable level with the long-term States income and expenditure projections in mind. The proposed cost cap is expressed as a percentage of pensionable earnings (16.5%) which means that actual costs can be managed by making efficiencies. The introduction of a formal employer cost cap and the ability to manage actual costs through efficiency savings provides reassurance on affordability into the long term.

Many of the Scrutiny recommendations are of a detailed nature relating to the Regulations and do not impact on the debate on the Law, which is an enabling Law. The States Employment Board will be considering these recommendations and respond formally to Scrutiny by 23rd June 2014. Any changes resulting from States Employment Board consideration of these recommendations will be included in the Regulations to be debated in the States later this year.