

The Actuarial Profession
making financial sense of the future

Pensions Conference 2011
John Livesey



Public Sector Schemes Funded Arrangements

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Agenda

Overview of LGPS

Hutton

Discount Rate

Other factors

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Overview of LGPS

Legal Structure

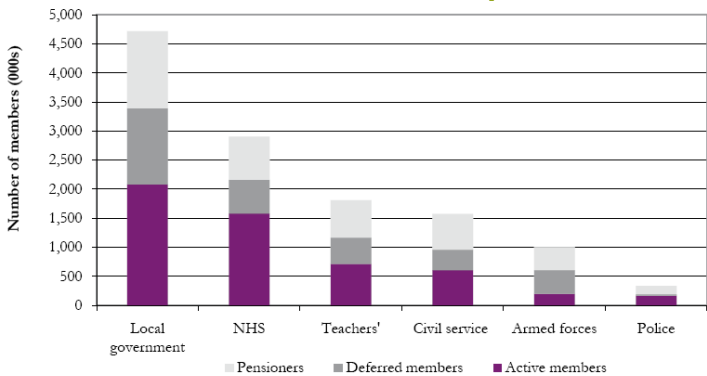
- Statutory
- Legally three schemes
 - split into 100 sub-funds
- Open to local authorities and “related”
- Currently final salary 1/60ths
- Benefits last reviewed w.e.f. 2008
- About 5 million members
- Assets over £150 billion.

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Overview of LGPS

Public service scheme membership



Source: IPSPC analysis of resource accounts and scheme data returns

Note: Police data and local government data in England and Wales are from 2008-09, all others 2009-10.

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Overview of LGPS

Employers

- Local authorities
- Other public sector
 - colleges/academies/universities/fire/police.....
- “Community of Interest”
- Contractors.

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Overview of LGPS

Distinguishing features

- Funded
- Transparency
- Accountability
- Local determination
- Governance.

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Overview of LGPS

Actuarial issues

- Statutory regulation (no tPR)
- Each employer typically responsible for own experience
- Employers normally required to meet debt on exit
- No scheme winding-up provisions
- GAD statutory/advisory role for overall Scheme
- Four firms advising individual funds
- Common actuarial valuation dates.

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Overview of LGPS

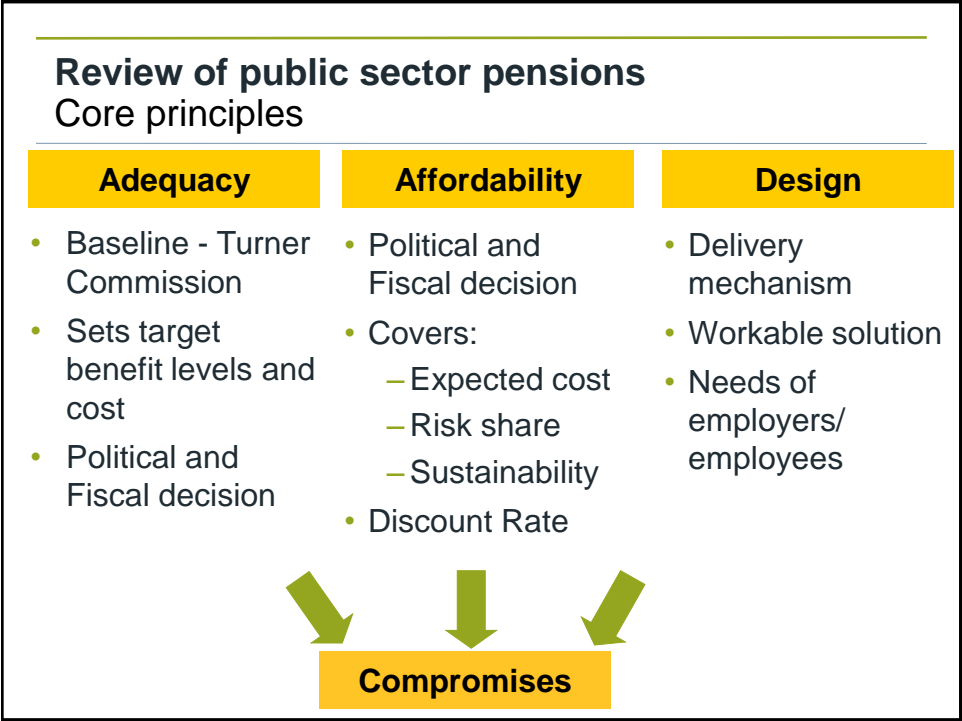
Hutton

Discount Rate

Other factors

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Public service pensions review

Some specific issues for the LGPS

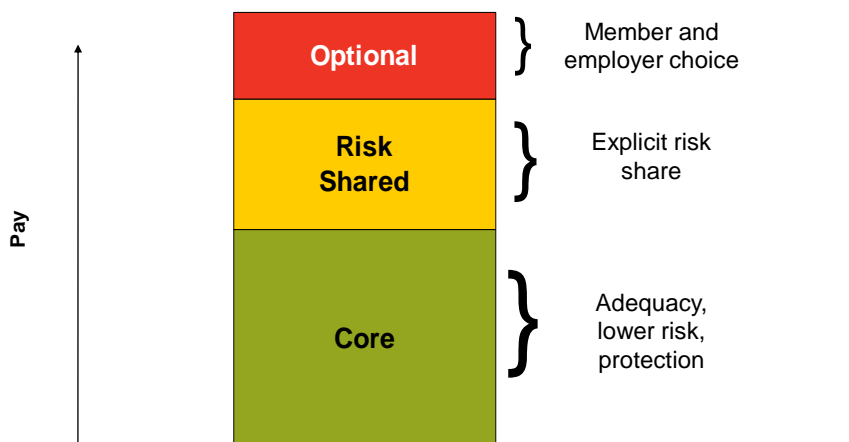
Fit for purpose

- Multi employer issues
- Employer risk management
- Transparency / cross-subsidy
- Benefits strategy and objectives
- Public service delivery – Fair Deal / TUPE
- Adequate and appropriate.

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Ideal LGPS Design Model



Hutton Final Report

Core recommendations

- “CARE” to replace final salary for future service
- Tiered member contributions based on earnings
- Protection of Accrued Rights/link to final salary
- Risk sharing if costs exceed a specified ‘fixed cost cap’
- More flexibility on timing of retirement benefits
- Normal Retirement Age to link to SPA with NRA 65 immediately

Hutton Final Report

Surprises?

- Protection of Final Salary link for accrued benefits
- Revaluation link to National Average Earnings
- Future accruals linked to changes in SPA.

Hutton Final Report

Unknowns

- Member contributions
- Accrual rate.

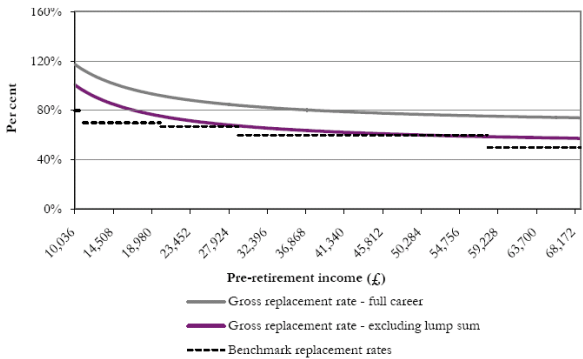
Missed opportunities?

- Risk sharing.

Hutton Final Report

Adequacy

Chart 2.A: Gross replacement rates delivered by typical current public service pension schemes and state pension system



Source: IPSPC analysis.

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Transparency and effectiveness

Governance

- LGPS in general ahead of the game
- Some inconsistencies
- Lack of formal member representation
- Properly constituted Boards
- Role for tPR?

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Timescale

- "... before end of this Parliament..."
- Sounds like April 2015 to me!
- Final details needed 12-18 months ahead
- Two years for consultation/agreement
- Challenging!

Agenda

Overview of LGPS

Hutton

Discount Rate

Other factors

Hutton Interim Report

Why is the discount rate so important to any design?

Critical to benefit value comparisons

- DC vs DB comparison
- Pension vs cash balance
- Indexation cost
- “Top up” benefits expected/target benefits
- Proportion of “value” funded by member contributions
- ...and so on.

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Discount Rate Change

- Was RPI plus 3.5%
- Interim report “... may be too high...”
- Now CPI plus 3%
- Huge change in isolation
- Some mitigation from CPI pension increases
- Reinforced government’s case for cost savings.

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Discount Rate

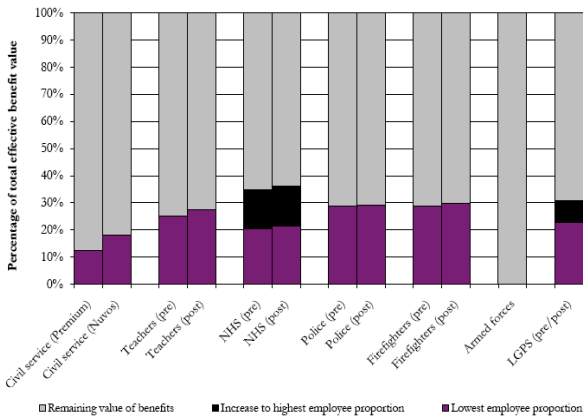
Other factors

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Member contributions – cross scheme comparison

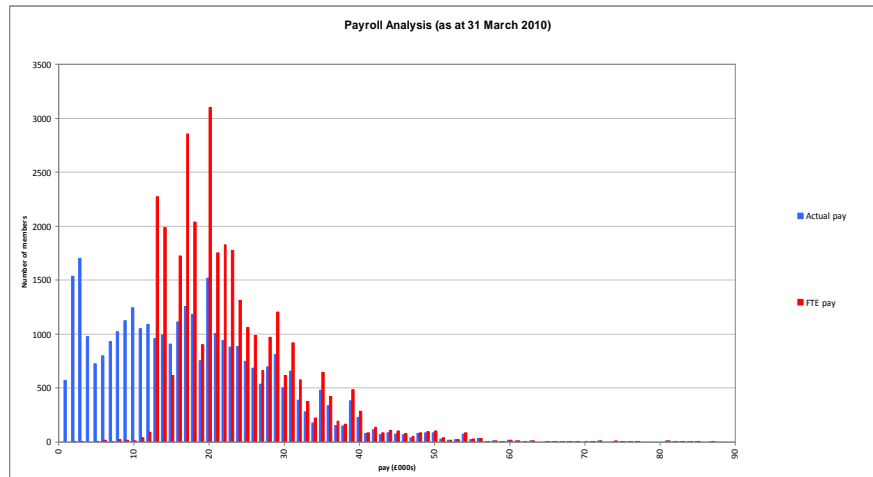
Chart Ex.4: Employee contributions as a proportion of the overall cost of accrual (pre and post reform)



Source: IPSPC and PPI

Note: Figures based on effective employee benefit rates described in Box 5.8.

LGPS Pay Distribution



Employee Contributions

- Currently 5.5% – 7.5%, dependent on earnings
- HM Treasury – 3.2% increase required in LGPS
- Could change to 5.5% – 15%
- Around 10% for moderate earners
- Depends on extent of protection for lower paid.

Fair Deal Consultation

- Protection of pension rights for compulsory transfers to private sector
- Current consultation – closes 15 June
- Hutton: "...in principle undesirable for future non-public service workers to have access to public sector pension schemes..."
- What is a public service worker?

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Outlook for the LGPS?

- Higher contributions – more opting out
- No Fair Deal – fewer active members
- Reduced value of future service benefits
- Rapidly maturing
- More derisking
- Higher costs.

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Questions or comments?

Expressions of individual views by members of the Actuarial Profession and its staff are encouraged.

The views expressed in this presentation are those of the presenter.

