Meeting:	Licensing and General Purposes Committee
Date:	19th September 2005
Subject:	Assessment of future Harrow Pension Fund liabilities, following revocation of 2004 regulations.
Responsible Officer:	Executive Director – Business Development
Contact Officer:	Greg Foley – Group Manager – HR Employee Services
Portfolio Holder:	Portfolio Holder Communications, Partnership and Human Resources For information: Members of the Pensions Investment Panel.
Key Decision:	No.
Status:	Part 1 - Public

Section 1: Summary

Decision Required

1. Elected Members having noted the future additional costs arising directly from the revocation, instruct the Group Manager to write to the Office of the Deputy Prime Minister (ODPM):-

    a) requesting that future amendments to the regulations address the additional burden of cost., and

    b) provide a copy of the actuary's full report .

2. Elected Members instruct the Group Manager to write to all associated employers, providing them with detail of the actuary report and advising them of their right to make contributions higher than those detailed in the 2004 valuation rates and adjustment certificate.

Reason for report

1. Need to assess and report on future liabilities to the Harrow Pension fund following the revocation of the 2005 regulations and the impact of longer life expectancy.

Benefits

1 Elected members are fully aware of future liabilities.

2 The ODPM is aware of Harrow's view and this authority's wish that future regulations should redress balance in relation to meeting cost of future liabilities.

3 Associated employers have sufficient information to make a judgement as to the merits/demerits of a voluntary increase in employer's contributions.

Cost of Proposals

1. Actuary is not recommending change to the rates and adjustment certificate.

2. Elected members to note actuary's assessment of future liability.

3. It is for each associated employer to make a decision as to any voluntary increase in employer's rate over and above that prescribed in the 2004 rates and adjustment certificate.

Risks

Failure to instruct the actuary to undertake exercise would have meant that:-

1) Harrow's written representation to the ODPM was without supporting evidence, and

2) associated employers would have insufficient data available to make an informed judgement as to the future employer's contribution rate.

Implications if recommendations rejected

1 ODPM will be unaware of actual cost associated with revocation in relation to the Harrow Pension fund.

2 Harrow Council, as the Pension Fund administering authority, would have failed in its duty to provide associated employers with full, timely and accurate information relating to the pension fund.

Section 2: Report

2.1 Brief History

The 2004 regulations were laid before parliament on 22 December 2004 with an effective date of 1st April 2005. Licensing & General Purposes Committee, at its meeting of 7th March 2005, received a full report from the Executive Director – Organisational Development on the 2004 regulations.

The 2004 regulations legislated for an increase in the minimum age for access to pension from 50 to 55 and the removal of the 85-year rule. [The regulations included transitional arrangements providing protection to certain scheme members]. The changes were designed to:

- Deal with effects of demographic changes and increasing longevity;
- Stabilise the future cost of the LGPS and to ensure a good defined benefit pension scheme can be retained for current and new employees;
- Ensure that the scheme does not directly or indirectly discriminate against people on the grounds of age and complies with the anti-age discrimination laws coming into effect next year. Only older, longer serving pension scheme members could meet the '85 year rule'; and
- Refocus the scheme on retention rather than early retirement.

On 1st April 2005 the ODPM issued draft consultation regulations proposing revocation of the 2004 regulations. The response date for submissions was 31st May 2005 and due to the fact that Licensing & General Purposes Committee was not due to meet within this timeframe, an urgent action was raised. The action proposed is detailed below and the letter forwarded to the ODPM is attached as **Appendix A.**

(Extract from Urgent Non-Executive action report)

ACTION PROPOSED

Elected members are requested to agree that given:-

i) the detail provided to Licensing and General Purposes meeting on 7th March 2005 in relation to the future costs of the Local Government Pension Scheme, and

ii) the rationale that underpinned the promulgation of the 2004 Regulations,

this authority could only agree to the proposed amending regulations if immediate alternative changes to funding of costs are provided.

2.2 *Current Position*

Following the statutory consultation period, the ODPM issued the local Government Pension Scheme (Amendment) Regulations 2005 on the 14 July 2005, effective from 3rd August 2005.

These regulations allow for:

a) Further evidential studies to be carried out, by the Autumn, to provide more detail of the cost implications of the phasing out of the 85-year rule. These studies will continue under the auspices of the LGPS tri-partite committee and will enable ministers to satisfy their statutory obligation to ensure that the Scheme's solvency is maintained and prudently managed, whilst remaining affordable and sustainable for all stakeholders.

b) Harrow Council London, as an Administering Authority, to consider whether and what adjustment, if any, needs to be made to the rates and adjustments certificate issued by Hymans Robertson as a result of the 2004 valuation. The regulation provides powers to carry out a fund valuation as at 31 March 2005. Should Harrow Council London agree changes to the rates and adjustment certificate the outcome must be reported to the Secretary of State no later that the 30th September 2005.

The Director of Finance and Business Strategy and the Group Manager HR Employee Services sought the advice of Hymans Robertson and the following represents their considered judgement.

"We see little merit in carrying out a major, costly and time-consuming exercise in recalculating employer's contribution rates. Given that employers will already have made 3-year budgetary plans based on the outturn of the 2004 valuation further adjustment would require a compelling reason.

However, we do believe that all employers, decision-makers and influencers ought to be aware of the impact of retaining the Rule of 85 on future pension liabilities if there is to be a sensible and informed debate about whether those costs are affordable. If employer contributions are not to change, employers ought to make the Tripartite Committee aware of their thoughts on costs. The fact that extra contributions are not immediately demanded does not mean that there are no cost implications.

In light of both Hyman Robertson's opinion and the pressing timeframe, the Director of Finance & Business Strategy and the Group Manager HR Employee Services took the decision not to engage in a costly, full valuation. However, Hymans Robertson were instructed to undertake a mini interim valuation, the main purposes being to:-

1. review the progress of the financial position of the fund since 31 March 2004 as part of the Administering Authority's ongoing risk management programme;

2 to advise, at whole fund level, on the cost to employers of the reinstatement of the Rule of 85 for service after 1 April 2005 as requested by the Employers' Organisation and the ODPM on behalf of the Tripartite Committee;

3. to consider the outlook for future employers' contributions, taking into account the reinstatement of the Rule of 85 and allowing for longer life expectancy at future valuations;

4. to consider whether a revised Rates and Adjustments Certificate is required, and

5. to consider whether any changes are required to the Funding Strategy Statement. (**Note:** A separate report will be submitted to the Pensions Investment Fund Panel).

Conclusions & Recommendations

See **Appendix B.**

Note: in terms of placing an illustrative cash value against **Appendix B 5.4**, a **1%** increase in employer's contribution rate would equate to **£816,000** increase in employer's pension contribution on-cost.

2.4 Consultation

UNISON and associated employers were advised of the instruction to Hymans Robertson. All parties were offered the opportunity to either provide written submission to this meeting or write directly to the ODPM.

Details of the actuary's findings and Elected Member decisions will be communicated to all parties.

Financial implications

The mini review that Hymans Robertson have undertaken is based on the 2004 data about pension fund members. However, it does update asset values, hence the increase in the level of funding. In addition the review takes account of longer life expectancy, the revocation of the changes in the regulations, and reduced bond yields (which feed into the calculation of the value of future benefits). In aggregate the review shows that if cost-saving measures are not introduced by the ODPM then employer contributions will have to increase by around 1.7% of pay. However, the review makes it clear that any change to contribution rates can wait until the next triennial valuation and be implemented from 2008/09. A provision will be made in the MTBS for further increases in employer contributions from 2008/09.

2.6 Legal implications

Included in the report.

Equalities Impact

Included in the report

2.8 Appendices

Appendix A – Letter to LGP Division
Appendix B – Extract from actuarial report.

Section 3: Supporting Information/Background Documents

Interim Actuarial Valuation as at 31 March 2005
Actuarial Valuation report 31 March 2004
The Local Government Pension Scheme (Amendment) (no.2) Regulations 2004
The Local Government Pension Scheme (Amendment) Regulations 2005

Appendix A

Harrow COUNCIL
LONDON

JILL ROTHWELL
Executive Director -
Organisational Development

Nicola Rochester
LGP Division
Zone 2 E/6 Ashdown House
123 Victoria Street
London SW1e 6DE

our ref: P/Draft Regs 2005 your ref: LGR 102/12/5 date: 27th May 2005

Dear Nicola,

Draft Local Government Pension Scheme (Amendment) Regulations 2005

Further to Terry Crossley's notification dated 1st April 2005, the following represents the considered response of Elected Members.

Accepting that the combined impact of workforce demographics and the fact that people are now living longer translates to increased liability on pension funds, the amendments introduced through the Local Government Pension Scheme (Amendment) (No. 2) Regulations 2004 appeared both sensible and timely.

It is accepted that there are a limited number of options available to control spiralling pension fund costs and the April 2005 reforms were viewed by this authority as providing a sensible balance in terms of scheme member / funding employer.

Should the Secretary of State decide to revoke the regulations this authority suggests that suitable alternative reforms, to control cost of post 31 March 2005 service accrual, are brought in with immediate effect. If current regulations are revoked without replacement reforms then this authority would suggest that a suitable funding method is found to negate the cost of lost savings to the pension fund.

Appendix B

5. Conclusions and Recommendations

Whole Fund Position

5.1 This interim valuation reveals that the ongoing funding level of the Fund on 31 March 2005 was 86%. The shortfall of assets compared to the past service liabilities was £52m. This funding level reduces to 83% and the shortfall increases to £67m if allowance is made for longer life expectancy.

5.2 The average cost of accruing benefits to employers, including administration expenses and lump sum death in service benefits, is 13.3% of pensionable pay, assuming that members will retire at their Earliest Retirement Age. The reinstatement of the Rule of 85 for most employees in respect of service from 1 April 2005 has no direct impact on the cost of accruing benefits because we did not allow for the abolition of the Rule of 85 in setting contribution rates. However, allowing for improvements in life expectancy (which was deferred in the 2004 valuation on the basis that the additional cost was offset by the abolition of the Rule of 85) would increase the average cost of accruing benefits by 0.9%, to 14.2% of pensionable pay.

5.3 The shortfall of assets over the past service liabilities requires the employers' contribution rate to be increased by 5.5% of pensionable pay, if recovery of the deficit is targeted over a period of 20 years from the latest formal valuation date and improvements in life expectancy are anticipated. The Common Contribution Rate based on the results of this interim valuation is therefore 19.7% of pensionable pay. This compares to 18.0% as at the 2004 valuation.

5.4 Thus, if compensating cost-saving measures are not introduced by the ODPM, then in theory employer contributions will need to increase by 1.7% of pay on average. This compares to the cost of reinstating the Rule of 85 of 1.6% of pay (allowing for the transitional protections that were in place). This cost-saving would increase to 2.0% of pay if no transitional protections are in place.

5.5 If the April 2006 tax changes permit flexible retirement, any 'savings' from late retirement would be expected to disappear. Thus, it would appear unwise when funding the scheme to anticipate saving from late retirement.

Recommendations

5.6 It is widely expected that cost saving measures to compensate for the reinstatement of the Rule of 85 will be introduced by the ODPM from 1 April 2006. In light of this, and the fact that contribution increases based on the 2004 valuation are being phased in over a three year period, we do not consider that employer contributions need to be increased automatically as a result of this interim valuation.

5.7 The Administering Authority should, however, consider advising employers of future contribution rises at the 2007 valuation if commensurate cost saving measures are not introduced. Employers should also be given the opportunity to increase contributions voluntarily if they wish to do so. (As our Rates and Adjustments Certificate specifies minimum contributions, additional contributions may be made without changing the current certificate.)