

FIREFIGHTERS' PENSION COMMITTEE

FIREFIGHTERS' PENSION SCHEMES: OPTIONS FOR THE FUTURE

Note by CLG

At the 33rd meeting on 11th January, the Committee considered the Actuarial Valuation report and CLG undertook to produce a paper setting out options for the schemes for discussion.

This paper does not seek to offer any solution to the cost pressures but sets out the range of options that are available if it is decided that the pressures need to be met either by an increase in contributions, from employers and/or members, or changes to the benefit structure.

The paper does not set out Departmental policy. CLG's objective is to give the Committee the opportunity to comment on and discuss the options at the earliest opportunity; to see whether there is any consensus; and to ensure that, as more detailed work is developed, the considered views of stakeholders is taken into account.

CLG is concerned to manage pension liabilities over the foreseeable future and to ensure that the two Schemes remain viable, affordable, sustainable and fit for purpose.

The problem

The underlying employer cost of the Firefighters' Pension Scheme 1992 (FPS) net of ill health charges has increased from 21.3% to 24.4% and Fire and Rescue Authorities want to see this 3.1% increase addressed either through a transfer of cost to members or changes to the benefit structure.

At 2008/9 figures, 3.1% of pensionable pay would total £31.5m for the English authorities.

Options for Change

1. Transfer of costs to members

Increase contribution

Increase employee contributions for members of the FPS, either by a flat rate increase for all members or by introducing tiered contributions linked to salary levels.

Tiered contributions

Tiered contributions would mean that those in certain roles would pay more than the standard rates which are 11% in the FPS and 8.5% in the NFPS.

Given the small numbers in roles above operational firefighter roles (i.e. firefighter, crew and watch managers) the yield would be small. Numbers in England and salaries are set out at Appendix 1.

Each 1% increase in employee contributions above the standard rate for station officers and above would yield £1.23m.

2. Changes to the Benefit structure

Flexible retirement

It was suggested at the 33rd meeting that whilst authorities had been given the incentive to manage, and control the cost, of ill-health retirements, they do not have any means to manage ordinary retirements.

There would appear to be two main options:

i. allow the person to accrue additional pensionable service after 30 years' service. This would enable members to defer taking their pension and commuted lump sum. In the case of those who joined the FPS before age 20, the downside would be that they would be given additional benefit at a cost to the Scheme; it would also give additional benefits to those who would have voluntarily opted to defer taking their pension until a later point; and the main gainers would probably be brigade managers. However, this would increase scheme costs as it would benefit those who already remain in service. It would only bring a significant benefit if it changed behaviour generally and led to the majority of members postponing their retirement.

At this stage it would be difficult to place a value on the cost as this would depend on the actual experience of the membership who took the option.

ii. allow the person to remain in service but defer taking their FPS pension until they finally retire, with an option to join the NFPS for future service. They would not pay FPS contributions and FPS pension would be based on pensionable pay at point that they chose to defer taking pension.

Clearly, if members pay no contributions there would be a cash shortfall over the current position.

Raising minimum pension age

Raising the minimum pension age from 50 to 55, with protection for those reaching age 55 before, say, 1 April 2016.

It is estimated that this would give savings of about 3%, although this would reduce if members were allowed further accrual up to 45/60.

An alternative option would be to raise the minimum pension age for all staff on promotion into or within management grades. This could be set to catch those on promotion to station manager or above, although the point for applying such a requirement could be set at a more senior level.

Whilst it is difficult to justify an earliest pension age of 50 for staff in roles with a diminishing front-line operational requirement, the savings would be lower, in the same way as increasing contribution rates for people in these roles raises only a small amount.

Commutation

Commutation linked to the value of pension surrendered remains an incentive for members to retire at the earliest point, after which the factors start to reduce the value. Given the trend, there is little prospect of longevity assumptions being revised downwards and a risk that they will continue to rise, so there is an argument for addressing the problem now.

There are limits on the action that can be taken as accrued rights would need to be protected. This probably means that accrued rights would have to retain actuarial equivalence rather than being fixed at the current rates, and probably determined by age at which person would have accrued 30 years' pensionable service. This points to addressing the problem now and moving to a fixed rate for future service in line with the NFPS and other public sector schemes.

If past service and those eligible to retire before 1 April 2016 were given protection potential savings relative to the current factors would be 2% of pensionable pay if the commutation rate was fixed at 12: 1, or 1% if fixed at 15:1. For future service, the factor would need to be at 12:1 in line with the NFPS and other public sector schemes.

Pensionable pay

We have already initiated consultation on pensionable pay with a view to making the definition more restrictive and limited to basic pay. Any additional payments or allowances would be pensionable at the discretion of the employing authority on an additional pension benefit basis (i.e. on a similar basis to the CPD arrangements at Rule B5C).

The potential savings are difficult to calculate at this stage because it would take some years for behavioural changes which would result from the change to become apparent in valuation data. However, if as we expect substantial increases in pay occur in the run up to retirement the savings would be material.

3. Closure of the FPS

In 2004, the Government accepted that a new pension scheme for firefighters was needed with the flexibility to meet the future requirements of the Service. The NFPS 2006 was the consequence. However, it was decided to keep the 1992 Scheme for existing members with some modification specifically related to the introduction of two tier arrangements for ill-health retirement awards, but more substantial changes relating to the minimum pension age were not progressed.

The transfer terms offered during the options exercise in 2007 were not sufficiently attractive because qualifying service by normal pension age was capped at 40 years which meant that any person who had joined the FPS in their early to mid-twenties could not transfer in their accrued rights, and we were unable to persuade HM Treasury that more beneficial terms should be available. At the time, we assumed that few would chose to transfer whatever the terms, and this was supported by the outcome as there was no substantial move to the NFPS by members of the FPS (just over 100 across the UK, of whom 85 transferred service from the FPS).

Also we failed to appreciate the extent to which firefighters would wish to continue in fire and rescue service employment after they had completed 30 years' service (and were entitled to draw their pension) or the extent to which they would want to be employed in non-operational roles; the abolition of the compulsory retirement age in the FPS in 2005 and the amendment to the definition of regular firefighter in 2004, plus age discrimination legislation appear to have had a marked impact on retirement patterns.

However, despite the changes that have been made, the structure of the FPS remains unsatisfactory and there must be doubts as to whether the Scheme continues to meet the needs of the FRS sufficiently to justify retention in the medium to long term.

The FPS is unsatisfactory for the following reasons:

- 30 year scheme, with a minimum pension age of 50, means that if a member wants to continue working after the 30 year point they must either transfer to NFPS and accept a deferred FPS pension or resign and seek re-engagement;
- because the FPS is a 30 year scheme, accruing to a maximum of 40/60, there is no benefit in a member working beyond 30 years' service and, in fact, the commutation arrangements are an incentive to retire at the earliest point, because the factors give a reducing lump sum after age 50;
- 30 year scheme with a low retirement age may no longer be appropriate as Scheme experience data shows that mortality rates of scheme members are no different to that of the general population;
- commutation arrangements encourage retirement at the earliest point;
- employee contributions also remain constant throughout service, which means that members do not recognise any benefit in return for payment once 30 years has been completed;
- the threat of challenge under age discrimination legislation remains real; as we have found recently in the case of a person recruited between age 18 and 20.

In relation to closure, there are two options:

i. close the FPS and transfer members for future service to NFPS. Accrued benefits in the FPS would be payable from age 50 with 25+ years' service. If the person decided to retire at that point any NFPS pension would be deferred, or paid from age 55 with an actuarial reduction.

If transitional protection was given to those with an entitlement to retire before 1 April 2016, the savings would be 8.6% of pensionable pay.

ii. close the FPS and transfer accrued service to NFPS.

The Committee is invited to discuss.

CLG
March 2010

Tiered contributions

Those with pensionable pay of £50k or more per annum would capture:

Group Managers:

Development - £41,881 plus FDA of 20%.= £50,257: total 65 staff
 Competent A - £43,138 “ “ = £51,766: total 198 “
 Competent B - £46,428 “ “ = £55,714: total 410 “

Area Managers:

Development - £49,167 “ “ = £59,000: total 24 “
 Competent A - £50,642 “ “ = £60,770: total 62 “
 Competent B - £53,938 “ “ = £64,726: total 122 “

Brigade Managers:

Development}
 Competent A} – say average £75,000*: total 161
 Competent B}

*this is very conservative but reflects NJC rates.

Total pensionable pay approx. £61,514,425

- Note total pensionable pay all members in 2008/9 was £1,017m, so pensionable pay of managers earning over £50k about 6% of total
- 1% of pensionable pay would therefore yield: £615,144
- 1.5% “ “ “ “ “ £922,716
- 2% “ “ “ “ “ £1,230,288
- 2.5% “ “ “ “ “ £1,537,860

However, if extended to Station Officers:

Station Officers

Development - £36,365: total 195
 Competent A - £37,456: total 317
 Competent B - £40,109: total 1,065

Total pensionable pay approx. £61,680,812

- 1% would yield an additional: £616,808
- 1.5% “ “ “ “ £925,212
- 2% “ “ “ “ £1,233,616
- 2.5% “ “ “ “ £1,542,020
- This would in effect double the yield but would still not plug gap between 21.3% and 24.4% (£31.5m at 2008/9 figures)