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# Pensions – challenges for council finance

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# LGPS employer contribution rates

**Primary (Future service) rate: Average rate from 2016 valuation is 17.6%. (average spread is 13% to 30% across the 88 funds)**

Although the benefits package is the same for all active members, variation in membership profiles and discount rate assumptions can cause significant differences in future service rates across employers. For example providing a benefit to an older employee generally costs more than providing the same benefit to a younger person while lower discount rates result in higher contributions.

**Secondary (Past service (deficit) contribution) rate: Average rate from 2016 valuation is around 7% but in many cases is paid as a cash lump sum rather than a percentage of payroll.**

Deficit contributions will vary between employers within funds because of the circumstances of each employer. In simple terms, an employer’s deficit contributions will reflect their own deficit and the period over which they are asked to remove it. Deficits can result from any combination of incorrect actuarial assumptions, historical underpayment by employers, increases in longevity, changes to macro pensions policy or shifts in economic factors.

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# LGPS costs and stats

- 0.6% increase in average future service rate at 2016 valuation mainly due to change in discount rate
- Overall LGPS deficits have decreased from a total of £47bn in 2013 to £37bn in 2016 (liabilities of unfunded public service schemes estimated at £1.5t NAO July 2016)
- Employer contributions in 2016/17 were £7.4b, employees paid £2.1b SF3 2016/17
- LA's account for about 75% of membership so about £5.5b of employer contributions
- Employer contributions constituted just under 6% of £93.6b LA revenue expenditure in 2016/17
- Assets in the LGPS rose by 21% in 2017 to £260b
- About 60% of LGPS assets invested in listed equities with around 10% on alternatives including infrastructure
- Investment income contributed some £4b to the cost of the scheme in 2017 without which employer costs could be in the region of 38% of payroll
- Membership increased by 3.5% to 5.6m of which almost 2m are active members
- Average pension paid in 2017 was less than £5,000 per annum

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# LGPS what are the options?

- Leave it alone? - Without deficits the cost of scheme to LA's would be less than £4b per annum – is that unaffordable?
- Reduce the benefits? - Future benefits can only be changed by cost management or legislation with agreement of members
- Stop offering LGPS? - LA's have to offer the LGPS to all staff by law and even if all LA's somehow left the LGPS tomorrow they would get an immediate bill for something in the region of £28b to cover the deficit for already built up for pensioners and deferred pensioners
- Hand back the keys? – but would HMT really be interested in another Royal Mail?

However

- Incentivised and/or greater promotion of 50/50 could reduce the future service cost – but be careful of the right to opt back up
- Use of arms length companies could reduce the number of new entrants – but be careful of impact of both future rate and deficit recovery period
- Optants out could be incentivised if offered an alternative qualifying scheme – but be careful of impact of both future rate and deficit recovery period and the right to opt back in

Most importantly beware cash flow shocks

- Lower contributions equal lower cash flows into LGPS funds which could result in unmanaged asset disposal which in turn would increase deficits

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