

Public Sector Pensions

a synopsis of where we are and a plan for the way forward

1) Preamble:

- a) I believe in fair and adequate pensions for all in the United Kingdom, not just for some of us. That many people who have worked and paid taxes for sometimes more than 50 years, then to have an inadequate pension is a national disgrace. Having said that, the State and employers cannot be expected to do it all; there is also a personal responsibility to save for one's retirement.
- b) When I joined the Treasurer's Department of a local authority in 1966 as a trainee accountant, I was told words to the effect of, "*Your pay is better now than in most jobs but, by the time you are 35, you will notice that private sector accountancy will pay you better. It is doubtful the private sector will recognise the Chartered Municipal Treasurer qualification, so you will have little chance to move across. However, annual leave and sick pay in the public sector are better, job security is almost guaranteed and the pension scheme is second to none.*"
- c) On average public sector employees in the 1960s were paid less than the private sector, whereas now public sector employees earn on average approximately 7% more than employees in the private sector.

2) Present:

- a) Accordingly the private sector taxes now have to pay towards a public sector which earns more, has better terms and conditions in almost every respect and a pension scheme which the private sector cannot afford for itself. **The present government puts fairness for all as one of its main features, yet this situation is manifestly unfair by any standards.**
- b) A substantial part of public sector pensions is unfunded (i.e. today's taxpayer pays for the pensions paid today) and many of the public sector funded schemes are in actuarial deficit. In effect those deficits are supported by future taxes and so can be regarded also as unfunded to the extent of such deficits.
- c) Final salary pension schemes, once popular in the private sector, especially with larger companies, are now almost non-existent. Many companies which had such schemes have gone into liquidation through being unable to make up the actuarial deficit in their pension schemes.
- d) After 45 years of working in financial services, those of our clients who are well off in advanced old age (80s and 90s) are mainly those in inflation proofed final salary pension schemes; i.e. former public sector employees. As our clientele consists mainly of middle and senior management in the private sector, who are not so well off in retirement, I ask is this situation fair?

- e) If final salary schemes are not affordable in the private sector, then they are not affordable in the public sector which, after all, is funded entirely by the private sector.

3) Technical:

- a) Public sector unfunded pensions due for payment today have to be paid by today's tax payers.
- b) One school of thought was that an increasing population would mean that we wouldn't have to worry about unfunded pensions, as the taxes from an increased population would be paying for a relatively small number of unfunded pensions. This idea has proven flawed, as no effective plan was made for:
 - i) increasing longevity brought about by improved healthcare/food/exercise regimes etc.
 - (1) Successive governments have enabled and encouraged the NHS to grow and be more effective, yet it's apparent that little or no thought has gone into the obvious knock on effect of people living longer.
 - (2) Apparently little thought has been applied to the strain which this would put on the public purse if the private sector doesn't provide in advance through taxes for adequate future public sector pensions
 - ii) if the population didn't grow sufficiently fast
 - iii) if population reached the maximum sustainable in a geographically small country.
 - iv) I have the view that the Treasury and/or successive governments were asleep on the job when it came to considering these issues.
- c) Those born in the post World War II birth bulge years of 1946/7/8 have started retiring. We have known about this for more than 60 years, yet apparently little of effect has been done to plan for now.
- d) Life expectancy when I began working for a large mutual life insurer in 1972 was males aged 72 and females aged 76. Now life expectancies are approximately 84 and 86 respectively.
- e) As early as 1974, I was recommending companies to consider changing final salary schemes to contribution based schemes, as it was clear that the former was and remains "an open cheque book," with no limit on what amount could be on the cheque.
- f) Taking males retiring at age 65 as a reference point, in the mid 1970s a pension fund of £100,000 would have bought a lifetime pension of approximately £13,000 per annum, based on then commonly available pension rates. Put the other way around, the cost then to the tax payer of an unfunded single life pension without escalation of £13,000 would have been approximately £100,000. (Currently many public sector employees qualify to retire at 60, for which the cost of the same pension then was approximately £144,000.) N.B. - These are single life figures, with no widow's pension and no escalation of pension once in payment. Public sector schemes provide a substantial widow's pension and inflation proofing, both of which boost the cost very substantially!

- g) Increased longevity and lower interest rates have resulted in the cost of an annual pension of £13,000 at the best available single life pension rate now being £214,000, without providing escalation or a widow's pension.
- h) Put another way, the cost of providing a public service pension is now more than twice what it was 35 years ago. This is not sustainable and it isn't fair of public sector employees to expect the private sector to pay for it.
- i) Through the pension scheme, the public sector has had a very substantial rise in the value of its pay package simply through the fact of us all living longer.

4) What is to be done?

- a) Whilst the private sector cannot afford final salary pensions, it is not supportable that public sector employees should have them. The final salary schemes of all public sector employees should cease forthwith.
- b) Past service is a different matter. Conditions of service must be honoured for past benefits. This is what has already happened in the private sector and it's unfair to private sector employees if the public sector doesn't follow suit.
- c) There is an argument for saying (for the sake of example, take someone who joined the scheme in 1981) that "longevity has increased by (say) 8 years in that time and the promise we made then was based on your then life expectancy, so we are actuarially reducing benefit by that amount, but the value of your pension is the same in real terms now as it would have been then." I am sure that this argument, though actuarially sound, would be extremely unpopular and may not be politically possible.
- d) **For future service unfunded (i.e. no provision in advance) will cease.** From now on pension should be funded for ALL public service employees. Benefits for future service would be based on the value of an employee's individual fund, not on final salary.
- e) **This should be expected to have substantial benefits for pensions provision throughout the public AND private sectors:**
 - i) The increased demand for stocks and shares will boost markets, helping to increase all pensions provision thereby, including the private sector.
 - ii) This provision is sustainable, final salary is not sustainable and inflation proofed final salary is highly unsustainable.

5) Comments on arguments against:

- a) Lower paid public sector employees – I am not at all sympathetic to the Unions' patronising nonsense about their lower paid workers. (I wonder what proportion of these are paid the minimum wage?) At least such workers have a pension scheme. Office cleaners, fast food chain employees, catering workers and other lower paid personnel in the private sector (the vast majority of which **are** on the minimum wage) have no pension provision at all, nor any expectation of it. Moreover the last government's rush into the NEST scheme for all will not prove to be good provision either, although any provision is better than none.

- b) “Public sector employees are tax payers too.” Of course, but this is a fatuous argument, as it’s still the private sector which gives public sector employees the money with which to pay their taxes!

6) Conclusion:

- a) Solving this problem is probably going to prove divisive and difficult, in the same way as were the problems of the miners’ strikes. Having said that I believe that the public as a whole will accept the logic and fairness of these arguments. **This is a winnable argument!** The public sector unions (if not the whole union movement) are in any case spoiling for a fight with a non-Labour Government, so nothing short of a complete cave in will appease them, after which they’ll then pick on something else to fight for.
- b) It’s a battle which our nation has to win if we are to live within our means and if we are not to repeat the mistakes of the past, at least as regards pension provision.

Copyright R M Brown & Moneynotation Limited – 23 December 2010 (last amendment 21 November 2011)