Public Service Pensions: cost control mechanism consultation
Proposal to reform the mechanism

Response of the Association of School and College Leaders

A. Introduction

1. The Association of School and College Leaders (ASCL) represents over 21,500 education system leaders, heads, principals, deputies, vice-principals, assistant heads, business managers and other senior staff of state-funded and independent schools and colleges throughout the UK. ASCL members are responsible for the education of more than four million young people in more than 90 per cent of the secondary and tertiary phases, and in an increasing proportion of the primary phase. This places the association in a strong position to consider this issue from the viewpoint of the leaders of schools and colleges of all types.

2. ASCL welcomes the opportunity to contribute to this consultation. However, HMT's consultation paper was published on 24 June 2021 and the deadline for comments is 19 August 2021, a period of eight weeks. This seems very short for such a significant issue especially when the consultation runs over the school holiday period.

B. Key points

3. ASCL understands the need to reform the cost control mechanism considering the preliminary 2016 breach as its first valuation. The proposals to move to a reformed scheme only design and widen the corridor are essentially parametric changes, changing key markers within the existing structure. ASCL is broadly supportive of these. However, the introduction of an economic check is a fundamental change to the mechanism. ASCL sees the proposal as a breach of the 'Heads of Agreement' of in 2011-12 pensions negotiation, and a breach of the 25-year guarantee of no changes to public service pension schemes given by the Chief Secretary to the Treasury in November 2011.

C. Answers to specific questions

Question 1: Do you agree that a reformed scheme only design would achieve the right balance of risk between scheme members and the Exchequer (and by extension the taxpayer), and would create a more stable mechanism?

4. ASCL concurs with the proposal to base cost sharing on the reformed schemes alone. The reformed (career average) scheme only can be adjusted within the cost sharing framework. Consequently, it follows cost variations will only arise from factors that affect the cost of benefits in the reformed schemes, not the legacy schemes. This is sensible approach in that the benefits potentially being assessed are consistent with those potentially being reformed.

The current mechanism incorporates assessment of legacy (final salary) scheme costs that contributed to some 60% of the preliminary 2016 breach (*Cost control mechanism - Government Actuary's review - Final report*). This was primarily caused by lower-than-expected increases in pay and a reduction in the life expectancy growth rate. Both are inherently designed out of the reform scheme by the CARE accrual mechanism, and the linking of normal pension age to the state pension age, respectively. Whilst the legacy scheme includes active members, it cannot be retrospectively adjusted or retrofitted to ameliorate these factors. Consequently, ASCL is of a view that that such a reformed scheme only design will create a more stable mechanism.

Moreover, ASCL agrees that a solely reformed scheme design engenders greater equitability on intergenerational grounds. This is would otherwise be exacerbated for those joining the reformed scheme after April 2022, mitigating potential costs driven by the legacy scheme.

Question 2: Do you agree with the Government's intention to widen the corridor? If not, why not?

5. ASCL agrees with the proposal to widen the corridor to develop a more stable cost control mechanism, as per the Government's stated intention. A wider corridor will reduce volatility, leading to fewer changes in benefits or member contributions. Nevertheless, any subsequent changes will be necessarily greater in exacerbating the "cliff edge" nature of the cost control mechanism. However, on balance ASCL concurs that the additional stability provided by a wider corridor, within the caveat of a reformed scheme design, outweighs any potential disadvantages.

Question 3 : Do you think that a corridor size of +/-3% of pensionable pay is appropriate? If not, why not?

6. ASCL agrees, as above, that an increase in the size of the corridor coupled with a reformed scheme only design should improve the stability of the mechanism. ASCL supports the $^{+}/_{-}$3% based on modelling from the Government Actuary's Department, in order to only have breaches due to "extraordinary, unpredictable events", whilst noting that any modelling is only as secure as its inherent assumptions. Consequently, we reserve the right to highlight any concerns should they become apparent.

Question 4 : Do you agree with the proposal to introduce an economic check?

7. ASCL does not agree with the proposal to introduce an 'economic check'. ASCL understands that the intended purpose of the economic check is to prevent a scenario whereby the costs to employers move in one direction and the cost control mechanism moves in an opposite direction, as in the preliminary 2016 valuation. Nevertheless, this is fundamental breach of guarantees given at the establishment of the reformed schemes in 2011, as indicated in point 3 above. It would introduce financial elements into the mechanism, which were not previously designated "member" costs.

   The 2016 scheme valuations were the first valuations to be conducted under the new cost control mechanism, and do not include costs due to Transitional Protection. ASCL does not see the need to fundamentally change the mechanism and structure of cost sharing at the first valuation, coupled with what can be deemed an extraordinary event, to the possible detriment of members.

A driver in the consultation for the economic check cites the "original policy objectives", (section 2.3) for the cost sharing/cost control mechanism as
• To protect taxpayers from unforeseen costs;
• To maintain the value of pension schemes to the members; and
• To provide stability and certainty to benefit levels – the mechanism should only be triggered by 'extraordinary, unpredictable events'.

However, whether in agreement or not, there is a lack of transparency as to where these original policy objectives were located or agreed.

Question 5: Do you think that the SCAPE discount rate, as it currently stands, is an appropriate economic measure for the cost control mechanism?

8. ASCL does not agree with the concept of an 'economic check' or 'affordability offset assessment' in the cost sharing mechanism and believes that it is a breach of the 25-year guarantee of no changes to public service pension schemes. Moreover, ASCL believes this breaks the deal which was based on the Government providing the promised pension benefits, whatever the discount rate.

   "The Government intends that only changes to scheme costs due to 'member costs', such as a dramatic change in longevity and as defined by previous cap and share arrangements, would be controlled by the cap. Financial cost pressures, including changes to the discount rate, would be met by employers". (Teachers Pensions "Heads of Agreement").

   ASCL's view is that the exclusion of the SCAPE discount rate from the cost control mechanism is a fundamental part of its design. So, whilst the discount rate currently has no impact on member's benefits, the proposal introduces a risk of to both members' benefits and contributions being affected by changes in the discount rate.

   The introduction of the economic check in the LGPS, as suggested, would be particularly problematic as it is a funded scheme, locally administered, with substantial overseas investment.

Question 6: If the SCAPE methodology changes, and the Government considers that the SCAPE discount rate is therefore not an appropriate measure for the cost control mechanism, then do you think that a measure of expected long-term GDP should be used instead? If not, please set out any alternative measures that may be appropriate in this scenario. Please consider in the context of the separate review of the SCAPE methodology currently being undertaken by HM Treasury.

9. Please see the response to Question 5. Given the lack of any figures on the impact of the proposals it is not possible at this stage to arrive at any definitive conclusions about the overall effect on members. ASCL reserves the right to highlight any concerns should they become apparent.

Question 7: Do you envisage any equalities impacts from the proposals to reform the cost control mechanism that the Government should take account of?

10. As intended, a reformed scheme only design would have positive consequences for younger members of the scheme and minimise any intergenerational unfairness. ASCL is supportive of this proposal and does not envisage any other specific equality issues with the consultation proposals. As the proposed reform would apply to all future accrued benefits, we do not see any obvious equalities impact. However, considering the considerable complexity of the proposals we reserve the right to highlight any concerns should they become apparent.

D. Conclusion

11. I hope that this response is of value to your consultation. ASCL is willing to be further consulted and to assist in any way that it can.

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