

PUBLIC SERVICE PENSIONS ACT 2013

EXPLANATORY NOTES

COMMENTARY ON SECTIONS AND SCHEDULES

Cost Control

Section 11: Valuations

72. This section sets out that defined benefits schemes made under section 1 must be actuarially valued in accordance with Treasury directions.
73. *Subsection (1)* requires scheme regulations to provide for actuarial valuations that will cover both defined benefits pension schemes that are created by, or governed by, the Act and any connected scheme. Section 4(6) defines a connected scheme as one which covers employees who are employed in the same kind of public service as the new scheme, provided they are not excepted from this rule under scheme regulations.
74. *Subsections (2) and (3)* set out that the valuations must be carried out in accordance with Treasury directions. Those directions may specify key details on how valuations should be carried out, including:
- how and when the valuation is to be carried out;
 - the time periods over which a valuation will measure a scheme's assets and liabilities;
 - the data, methodology and assumptions to be used in valuations;
 - the matters that must be covered by the valuations (which may relate to the outputs that must be produced);
 - how valuations of new and connected schemes will be combined, where they are to be valued together; and
 - the time period for implementing changes to the employer contribution rate as a result of the outputs of the valuation.
75. *Subsection (4)* requires the Treasury to consult the Government Actuary before making, revoking, or amending directions.
76. *Subsection (5)* provides that scheme regulations for other kinds of schemes, such as injury and compensation schemes, may provide for actuarial valuations of that scheme and any connected scheme. This will allow for those schemes to be valued alongside a pension scheme if this is appropriate.

Section 12: Employer cost cap

77. This section requires scheme regulations for defined benefits schemes made under section 1 to set an employer cost cap and sets out how this cap should be set, measured and operated. The section does not apply to defined contributions schemes, or injury

and compensation benefit schemes, as these schemes do not require this type of cost control.

78. *Subsections (1) and (2)* require scheme regulations to set a rate, known as the employer cost cap, which is to be used for measuring the costs of a scheme made under section 1 and, subject to Treasury directions made under this section, those of any connected schemes as defined in section 4(6).
79. *Subsection (3)* provides that the cap is to be set in accordance with Treasury directions.
80. *Subsection (4)* gives non-exhaustive examples of what those Treasury directions may cover. They may, in particular, specify how the first valuation under section 11 will be taken into account when setting the cap, and how costs or changes in costs at subsequent valuations are to be taken into account when measuring the costs of the scheme against the employer cost cap (the comparison that will be made at subsequent valuations).
81. The directions may also specify to what extent the costs of connected or other schemes are to be taken into account when setting the employer cost cap.
82. *Subsection (5)* requires the Treasury to make regulations to determine how the cap will operate. Treasury regulations will:
 - set margins either side of the cost cap; and
 - specify the target cost (within those margins) that the scheme should take action to return costs to if the costs of the scheme go beyond those margins.
83. *Subsection (6)* makes provision for scheme regulations to specify the processes to be followed to reach agreement on the action to be taken if the cost of the scheme arising from a second or subsequent valuation does not fall within the margins set out in Treasury regulations. A default action may also be specified if there is no agreement.
84. *Subsection (7)* provides that the action taken to bring the scheme costs within the margins may include an increase or decrease in members' benefits or contributions. It is not envisaged that such action will affect any pension already built up in the scheme.
85. *Subsection (8)* allows Treasury regulations to make consequential and supplementary provision. It also allows regulations to make different provision for different schemes with regard to the way the employer cost cap is set, measured and operated.
86. *Subsection (9)* provides that Treasury regulations under this section are subject to the negative Commons procedure (as defined in section 38(5)).

Section 13: Employer contributions in funded schemes

87. **Section 13** provides for the setting of the rate of employer contributions in defined benefits schemes with a pension fund, most notably the funded Local Government Pension Scheme. The section requires an actuarial valuation of the pension fund to inform the setting of the employer contribution rate. The valuation of the pension fund is separate from and in addition to the valuation of the whole scheme under section 11. Section 13 provides for an independent review of the valuation and employer contribution rates to check that they are appropriate and requires remedial action to be taken where that review identifies a problem.
88. *Subsection (1)* provides that the pension schemes to which the section applies are defined benefits schemes set up under the Act which have a pension fund. These will be the Local Government Pension Scheme in England and Wales, the Local Government Pension Scheme in Scotland and any other funded defined benefits schemes established under section 1 in the future.
89. *Subsection (2)* requires the scheme regulations of a funded scheme made under section 1 to set the employer contribution rates so that they meet two specified objectives. These

*These notes refer to the Public Service Pensions Act 2013
(c.25) which received Royal Assent on 25 April 2013*

objectives are to ensure that the rates of employer contributions are set at a level that is sufficient to ensure the solvency of the pension fund and the long-term cost-efficiency of the part of the scheme to which that fund relates. The valuation will take into account the current and anticipated liabilities of the scheme; the effect of these objectives is to ensure that those liabilities are provided for in a prudent manner.

90. The terms “long-term cost-efficiency” and “solvency” are not defined in the Act. Long-term cost-efficiency implies that the rate must not be set at a level that gives rise to additional costs. For example, deferring costs to the future would be likely to result in those costs being greater overall than if they were provided for at the time. Solvency means that the rate should be set at such a level as to ensure that the scheme’s liabilities can be met as they arise.
91. *Subsection (3)* provides that scheme regulations must require the pension fund to be subject to actuarial valuation. Provisions in the scheme regulations will require the scheme actuary to set the employer contribution rate for the employers who contribute to the pension fund. There are 89 pension funds in the Local Government Pension Scheme in England and Wales and 11 pension funds in the Local Government Pension Scheme in Scotland. Each pension fund will undertake a separate actuarial valuation and will set its own employer contribution rate or rates for the employers who participate in that fund.
92. *Subsections (4), (5), and (7)* require an appropriately qualified person to be appointed by the responsible authority to review the actuarial valuation and employer contributions rates and publish the findings of that review. The review will consider whether the valuation is in compliance with the scheme regulations, whether it is consistent with other valuations under the scheme, and whether the employer contributions rates were set as required by *subsection (2)*.
93. The purpose of the review is to provide an independent verification of the assessment of the scheme’s assets and liabilities and to confirm whether appropriate employer contributions will be paid to meet those liabilities. The independent person’s report must be published (*subsection (5)*).
94. *Subsection (6)(a)* provides that where the review identifies a problem with the valuation or the employer contribution rates the independent person may recommend how these can be corrected. Regardless of whether or not the review recommends actions, the scheme manager of the scheme is required by *subsection (6)(b)* to take steps to remedy any problem identified by the review. The scheme manager is also required to set out publicly what actions have been taken and why.
95. Where there has been an adverse review, *subsection (6)(c)* provides that the responsible authority may require the scheme manager to report on progress in taking remedial steps. The responsible authority may also direct the scheme manager to take such steps as he or she considers are needed to correct the problem. These powers are expected to be used as a last resort; for example, where the scheme manager is not (in the opinion of the responsible authority) taking appropriate remedial steps, or is delaying doing so.
96. For the local government pension schemes, the scheme manager will be the relevant local authority that is an administering authority for that scheme. In England and Wales, the responsible authority for the local government scheme is the Secretary of State; and for the local government scheme in Scotland it is the Scottish Ministers.