IPSA
Independent Parliamentary Standards Authority

MPs' pensions: updates to the cost control mechanism

A consultation – March 2024

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Background to the consultation

When the MPs' pension scheme introduced a CARE section in 2015, it also introduced a cost control mechanism (or cost cap). This is similar to what is in place in other public service pension schemes which aims to control the cost of pension benefits to the public purse by ensuring those costs remain within a pre-determined cost 'corridor'. The MPs' scheme uses a simplified version and does not look at past benefit costs unlike the other public service schemes.

The cost control mechanism sets out the expected parameters of cost for future benefits. To ensure that the cost is controlled there is a ceiling and a floor applied which are 3% above or 3% below the employer cost cap. If, when the Scheme actuary tests the mechanism, the projected costs are greater than +/-3% of the employer cost cap, then that triggers a decision around what changes to make to member contributions. This widened corridor from +/-2% to +/-3% following consultation in February 2022, reduces the regularity of breaches occurring.

Since its introduction, we have consulted twice on the mechanism, first in March 2021 and subsequently in February 2022. This third consultation aims to bring in an extra level of assurance into the MPs' scheme by further aligning it with the intention for the wider public service pension schemes in considering the country's longer term economic outlook.

In 2021 the Government consulted[1] on the idea of an economic check as part of the reform of the cost control mechanism in the main public service pension schemes. An economic check means that pension schemes are considering the affordability of that scheme in relation to the long-term economic outlook of the country. The Government Actuary recommended that public service pension schemes introduce an economic check into the full mechanism and the 2023 HM Treasury Directions provide details on how the check should work and when implementation would take place.

We are proposing to introduce an economic check which we consider appropriate for the MPs' pension scheme. IPSA is outside the scope of the 2023 Directions and therefore the introduction of a full economic check as detailed in the 2023 Directions is not required. The proposal includes incorporating relevant sections of the 2023 Treasury Directions into the scheme to ensure that the Scheme Actuary is using the most relevant information when assessing the cost control mechanism every three years. Finally, we

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

have some additional proposals relating to clarifying the cost cap implementation period in the scheme rules.

Proposals

To introduce an economic check into the pension scheme rules to test the cost control mechanism against long-term economic assumptions.

To introduce relevant elements of the 2023 Treasury Directions for actuarial valuations including rates of pensions increases, revaluation of deferred pensions, and the discount rate.

To introduce clarity on the timing of the cost cap implementation period.

Introducing an Economic Check

1. An economic check demonstrates that pension schemes are considering the affordability of the scheme in relation to the long-term economic assumptions about the outlook of the country. Changes to member contributions therefore would only be triggered by breaches of the ceiling or floor if the long-term economic assumptions have also been taken into account.

2. In line with the proposal for the main pension schemes, an economic check uses the same calculation as the cost control mechanism but without removing the impact of long-term economic assumptions (including the SCAPE[2] discount rate) when considering the long-term economic outlook. However, as the MPs' scheme does not use the full cost cap mechanism methodology like the other schemes, we propose to introduce the economic check in an appropriate way by using the current lighter touch methodology. If both calculations, for the cost cap and the economic check, show a breach of the ceiling or a breach of the floor, this indicates that the cost control mechanism result is consistent with the long-term economic outlook.

   Question 1. Should IPSA introduce an appropriate economic check which is similar to the rest of the public service pension schemes with the intention that contribution changes are aligned with the longer-term economic outlook of the country?

Treasury Directions

3. The new HM Treasury Directions 2023[3] were published on the 16 September 2023 and replaced the 2014 Directions. The current MPs' scheme rules reference the 2014 Directions for actuarial assumptions; however, there are some actuarial differences between the 2014 and 2023 Directions. Therefore, IPSA is not proposing a wholesale adoption of the 2023 Directions but instead to incorporate relevant parts of them as

[2] Public service pension schemes – SCAPE discount rate methodology: a GAD technical bulletin
[3] The Public Service Pensions (Valuations and Employer Cost Cap) Directions 2023

appropriate to the MPs' scheme, given that the MPs' scheme uses a simplified version of the cost control mechanism but using the new actuarial assumptions.

4. Our proposal is to incorporate the relevant provisions of the Directions, namely those within part 4, the section relating to the new Economic Check and part 5, the comparison with the employer costs cap, into Schedule 1 of the MPs' scheme rules. The Directions themselves outline the implementation of the full cost cap process for the main public service pension schemes; as the PCPF is not one of the main schemes, the targeted incorporation of the 2023 Directions into the MPs' scheme is intended to reflect the outcome of the economic check but not replicate the full cost control mechanism. The areas that we propose to incorporate from the 2023 Directions for actuarial reasons include the rates of pension increases, revaluation of deferred pensions in deferment, and the discount rate.

Question 2. Should IPSA introduce the relevant provisions in parts 4 and 5 of the 2023 Directions into the rules in a way that is consistent with the 'lighter' version of the cost control mechanism?

Clarifying the 'cost cap implementation period'

5. The cost cap valuations for the main public service pension schemes specify a "cost cap implementation period" that represents the period the scheme actuary should consider for calculating future costs, as well as the period during which breaches of the ceiling or floor should be actioned. The current MPs' scheme rules do not clearly specify the implementation period, and this could mean that contributions changes resulting from a ceiling or floor breach could apply retrospectively or within a short time frame of the valuation.

6. We propose to clarify this and set the cost cap implementation period as the period of three years starting at the next cost cap valuation date (i.e. three years after the current cost cap valuation date). Any changes to member contributions necessitated by the cost cap valuation outcome would be implemented at the start of the implementation period. This is consistent with other public service pension schemes but reflects the shorter period between valuations for the MPs' scheme.

7. We have also considered whether to go a step further and introduce some flexibility to avoid retrospective contribution changes by including a backstop position. For example, the date that any contribution changes would be implemented would be the later of either the start of the cost cap implementation period or the April after the Government Actuary signs the valuation report (the backstop).

Question 3. Should IPSA specify an implementation period as the period for which the Scheme actuary should calculate the future costs of the scheme, and to clarify when any resulting changes to member contributions should be actioned?

Question 4. Should IPSA consider introducing a back stop position to avoid changes to contributions being made either retrospectively or shortly after completion of the cost cap valuation?

How to respond

8. Please use our online survey to submit your response.

9. You can also email consultation@theipsa.org.uk if you prefer. **Please do not send us responses by post** as this may delay the processing of your response.

10. We will summarise the responses we receive when we publish our decisions. In doing so, we may refer to individual respondents and the content of their responses. We may also publish a list of who responded. If you would like your response to be treated as confidential, please say so clearly in your response. We will not quote from confidential responses or attribute the views in them to any particular respondent. Whether your response is confidential or not, we will not publish your email address or any other contact details, in line with our compliance with data protection law and the General Data Protection Regulation (GDPR). For more information about what we do with personal data, please see our privacy notice.

11. **Please send us your response by 3 May 2024.**

Equality impact assessment

12. We do not currently expect there will be specific equality impacts as a result of these technical changes, but would like to hear from our stakeholders about any possible or likely impacts?

Question 5: Are there any areas of possible inequality in the approach we are consulting upon that we should consider? Do you have any views on these proposals or any other possible equality impacts resulting from the proposals in this consultation?