

# Pensions Update

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## Are Public Sector Pensions Affordable?

by Roger May

Those of us who will be affected by the proposed strikes of public service workers in November may regard them as a temporary inconvenience – having to find child care for a day while the schools close.

But when the employers and employed have opposed views, these strikes can quickly escalate. This year the good folk of Southampton found their rubbish piling up in the streets when the dustmen went on strike. Rats appeared in broad daylight – contact the Council's vermin control officers? – No, they are on strike too . . .

So are public sector pensions affordable? The trade unions say they are, and the Government is just bluffing. But it appears the unions are basing their arguments on a misconception.

In March of this year Lord Hutton produced a closely-argued, but surprisingly readable, report on public sector pensions (available free on the HM Treasury website). This contained a graph showing that the actual cost of payment of public sector pensions now is 1.9% of our Gross Domestic Product (GDP). On the basis that the Hutton Report's recommendations are all followed, the cost then drops to 1.4% of GDP by 2050.

However, the unions have stated that the graph shows that public sector pension costs have reached a natural peak and will drop in future, even if no changes are made to the public sector pension schemes.

Lord Hutton himself disagrees: *"People are still choosing the facts that most suit them from the report and then torturing the data until it confesses. That chart does not show that public sector pensions*

### STOP PRESS

New round of quantitative easing disastrous for pensions (see below).

*are sustainable as they stand. If they were, I would not have made 27 recommendations for fundamental change."*

#### We're all living longer

One of the other graphs in Lord Hutton's report shows the projected longevity of British workers. Back in the 1950s the average worker would live for 10 years after retiring at 65. Now the figure is well into the 20s, and the graph shows no signs of tailing off – a Swedish study a few years ago found that for Northern Europe the line on the graph had been straight since 1850. It follows that if a public sector worker lives longer, his pension will have to be paid for longer, so the Government will have to set aside more money – not less – to pay for that pension.

Public sector pensions are also index-linked. Although the link is now to the Consumer Price Index, and not to the higher Retail Prices Index, public sector pensions could easily rise in value by 4% per year compound for the next 25 years. A modest pension of £10,000 a year would have risen to £25,633 by the time the pensioner reached 90. Will your taxes – which ultimately pay for public sector pensions – also have risen by 156% in that period? I rather doubt it.

So it is difficult to avoid the conclusion in Lord Hutton's report that public sector pensions, in their current form, are unsustainable. This is one fight the unions, and the public sector workers, cannot win.

# Pension Lifeline for Ageing Rockers

“Hope I die before I get old,” sang Roger Daltrey in the Who’s 1965 hit *My Generation*. But ageing rockers show remarkable resilience – Roger Daltrey is still performing, touring the USA and Canada as I write this, and the Rolling Stones’ Mick Jagger has formed a new band ‘SuperHeavy’ this year and released an album and the aptly named single ‘Miracle Worker’.

Why do they put themselves through this, you might ask. Probably because they need the money. Roger Daltrey has said, “Musicians need to be paid. There are thousands of small musicians whose independence relies on the little bit of royalty, for the work they did in the 1960s, they get by way of pension.”

The problem is that European copyright law only gave protection for 50 years – so many of the 1960s recordings

were about to go out of copyright.

Step in the European Union. On 12 September it ratified what has been called “Cliff Richard’s law”, extending copyright for performances of music from 50 to 70 years. Performers’ rights in sound recordings entitle them to royalties on the sale and other exploitation of the recordings, including downloads from the internet, and a statutory fee from the copyright owner each time their work is played in public. Composer’s rights last for 70 years after their death, but the rights of performers would have expired 50 years from the date of the recording.

I am sure that today’s ageing rockers never thought they would need a pension – but it’s good to know they will get one...

The new law has to be incorporated into EU members’ domestic law by 2014, but (as all pension lawyers know), EU directives have direct effect, so in practice the law has come into force already.

## QE2 Disaster?

Not the famous ship, but the Bank of England’s proposed injection of £75 billion. It may stave off a double-dip recession in this country, but the Bank will inject the new money by buying Government gilts and UK corporate bonds. These are the very assets bought by pension funds to safeguard their members’ pensions, both in payment and as promised in the future.

As in all cases where demand exceeds supply, this will raise the price of the gilts and bonds. Higher prices mean pension funds can buy fewer gilts and bonds with the money available. The problem is compounded by artificially low interest rates, which means that cash deposits – the pension funds’ other “solid” investment – now give a lower return than the rate of inflation.

The pension funds’ trustees are not the only ones who have to worry. As gilts and bonds become more expensive, pension funds’ liabilities will also increase, as the Pensions Regulator’s scheme funding regime is based on gilts. This

means employers will have to pour more money into the “pensions black hole” to maintain current funding levels. To a nation teetering on the brink of another recession, this is very bad news.

What can be done to avoid this? The Pensions Regulator could change the funding criteria for pension schemes. People have forgotten that in the 1960s and 1970s an investor in gilts would have made a substantial net loss. It is time the Regulator acknowledged that gilts are now risky investments, a long way from the boring but dependable investments of the last 20 years. But regulators are hardly renowned for acting swiftly . . .



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