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RESEARCH NOTE 26

£1 MILLION NHS PENSIONS

In December 2007, the TaxPayers' Alliance revealed that there are almost 3,700 retired civil servants with retirement benefits worth £1 million. In the second paper of our public sector pensions series, we look at the generosity of pension arrangements in the NHS in England and Wales. The NHS as a whole employs over 1 million people and is the world's third largest employer after the Chinese army and the Indian railways.

The bill for unfunded public sector pension liabilities has been estimated by Neil Record for the Institute of Economic Affairs at £1,025 billion, over £40,000 for each household. Part of the reason for this is that the public sector retirement age is generally 60, compared with a state pension age of 65, and that almost 90 per cent of public sector employees receive final salary pensions, compared with just 16 per cent in the private sector. With people living longer and an increasing number of pensioners relative to workers, current public sector pension arrangements are unsustainable.

Using data supplied to us under the Freedom of Information Act by the NHS Business Services Authority Pensions Division, it is possible to calculate how many retired NHS employees in England and Wales have retirement benefits worth (in present value terms) at least £1 million from the NHS pension scheme alone (any private pension or other occupational pension as well as the basic state pension would increase the pension pot, but is not under consideration here). The findings are startling:

- There are almost **8,500 retired NHS employees** (including GPs) in England and Wales with **retirement benefits** worth **£1 million**.
- The **total value** of these retirement benefits is almost **£8.5 billion**.

Corin Taylor, Research Director at the TaxPayers' Alliance, said:

"Unfunded public sector pension liabilities are reaching completely unsustainable levels. Every household will have to pay up to £40,000 over the next few decades to fund gold-plated retirement benefits for public sector employees, including £1 million pension pots for the NHS elite. Urgent change is needed to reduce the bill to taxpayers – for a start, the pension age for existing public sector employees should be raised to the state pension age as soon as possible."

Further details

The number of NHS employees in England and Wales with retirement benefits worth £1 million was calculated using data on the retired members of the NHS pension scheme (England and Wales) supplied to the TaxPayers' Alliance by the NHS Business Services Authority Pensions Division on 8 February 2007. This data was obtained using the Freedom of Information Act. (Copies of the request and response are available from the TPA.) The NHS Business Services Authority Pensions Division confirmed that there are 8,449 NHS pensioners who are currently receiving an annual NHS pension, net of lump sum, of at least £33,000. This comprised 8,374 in payment and 75 suspended.

An annual pension of £33,000 net of lump sum is equivalent to a pension pot, from which an equivalent annuity could be purchased, of around £1 million. This is confirmed by Terry Arthur, a Fellow of the Institute of Actuaries who has written widely on pensions matters and who is a leading expert in the field.

Terry Arthur writes:

- 1. "At the age of 60 (the standard retirement age for existing NHS employees) current annuity rates show that the value of an annuity of £1 pa, increasing according to the Retail Prices Index and with continuation at a rate of 50 per cent to a surviving spouse, is approximately £26 (note 1)."*
- 2. "I understand that currently there are some 8,500 retired NHS employees in England and Wales receiving a pension of £33,000 or more. In the overwhelming majority of such cases there would have been an additional tax-free lump sum of three times the initial pension."*
- 3. "Clearly, if all these pensioners had retired today on £33,000 pa plus a lump sum of £99,000, each would be worth £1 million."*

4. *"In fact some would have retired many years ago; the value of their pensions at the starting time would have been smaller than £1 million. On the other hand £33,000 pa is the minimum under consideration here; many pensioners will be receiving appreciably more. Furthermore, many hundreds of NHS employees will be retiring each year on pensions far greater than £33,000 pa.*
5. *"Given the above situation, in my opinion it is perfectly reasonable to say that "there are 8,500 retired NHS employees in England and Wales with retirement benefits worth £1 million".*

Notes

1. *"This ratio is entirely consistent with Neil Record's authoritative publication, "Sir Humphrey's Legacy", published last year by The Institute of Economic Affairs in association with Profile Books Limited. <http://www.iea.org.uk/record.jsp?type=book&ID=390>"*

Terry Arthur

*Fellow of the Institute of Actuaries
Fellow of the Pensions Management Institute
Financial Services Fellow of the Institute of Economic Affairs
Visiting Fellow of Westminster Business School
Adjunct Scholar of the Ludwig von Mises Institute
Director, Allianz Dresdner Second Endowment Policy Trust Plc
Director, SVM Global Fund Plc*

A growing problem

The alarming number of NHS employees with retirement benefits worth £1 million is symptomatic of a growing problem of over-generous and unaffordable public sector pensions:

- Demographic changes are putting increasing pressure on pension provision:
 - Life expectancy for men is projected to increase from 77.6 years currently to 85.5 years by 2056, while life expectancy for women is projected to increase from 81.7 years currently to 88.7 years by 2056.¹

¹ Government Actuary's Department, Period Projection of Life 1981-2056, Principal Projection, 2006. Cohort projections also give similar results.

- There are currently almost four people of working age (aged 20-64) for every pensioner (aged 65+). By 2056, that ratio will fall to just over two people of working age for every pensioner.²
- Public sector pension arrangements are not responding to these demographic challenges:
 - The public sector pension age remains at 60 for existing workers, compared with a state pension age of 65 rising to 68 by 2046.
 - Between 1995 and 2004, the proportion of public sector workers enrolled in final salary pension schemes has increased from 78 per cent to 88 per cent. At the same time the proportion of private sector workers has declined from 23 per cent to just 16 per cent.³
- Therefore, unfunded public sector pension liabilities are becoming increasingly unsustainable:
 - The Treasury estimates total unfunded public sector pension liabilities to be £530 billion, or £21,000 per household.⁴
 - Consultant actuaries Watson Wyatt estimate the bill to be £960 billion, or £38,000 per household.⁵
 - The Institute of Economic Affairs estimate the bill to be £1,025 billion, or over £40,000 per household.⁶

Attempts at reform – the Government’s U-turn in 2005

The Government’s U-turn over public sector pension reform in October 2005, after it was faced with the threat of a major public sector strike, has been widely discussed. It is worth re-visiting the original proposals:⁷

Existing accrual of existing members:

- Neither the Government’s original proposal, nor the October 2005 agreement, increased the public sector pension age for the existing accrued pension of existing members.

² Government Actuary’s Department, Population Projections 2006-2081, Principal Projection, 2006. NB: To a small extent this alarming change in the dependency ratio will be mitigated by the impact of the higher state pension age.

³ Occupational Pension Schemes, Government Actuary surveys, 1995, 2004; Labour Market Trends time series data, Office for National Statistics

⁴ House of Commons Hansard, 25 June 2007, Col. 393W

⁵ Watson Wyatt press release, 8 March 2006

<http://www.watsonwyatt.com/news/press.asp?ID=15784>

⁶ Neil Record, Sir Humphrey’s Legacy: facing up to the cost of public sector pensions, Institute of Economic Affairs, 2006

⁷ For a discussion, see Pensions Policy Institute, Briefing Note 25



Future accrual of existing members:

- The Government originally proposed to increase the public sector pension age from 60 to the state pension age of 65 for the future accrued pension of existing members from 2013.
- The October 2005 agreement maintained the public sector pension age at 60 for the future accrued pension of existing members. *This was the key climb-down.*

New entrants:

- The Government's original proposals would have increased the public sector pension age from 60 to the state pension age of 65 for all new entrants.
- The October 2005 agreement increased the public sector pension age to 65 for new entrants, although new entrants have the choice of paying higher contributions to keep their own pension age at 60.

The first steps to reduce the public sector pension bill

Implementing and extending the Government's original reform proposals would mark the first steps to reduce the bill to taxpayers of unfunded public sector pension liabilities:

- Firstly, the public sector pension age should be increased from 60 to the state pension age of 65 for future accrued pension of existing members, as the Government originally proposed. This should be done immediately, instead of the Government's original proposal to wait until 2013.
- Secondly, the public sector pension age should then increase from 65 to 68 by 2046, in line with the future increases in the state pension age. This would fully equalise the public sector pension age and the state pension age, providing a level playing field for all employees.

Reforms should then be extended to cover the nature of the final salary arrangements enjoyed in, and indeed the overall size of, the public sector.

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