

**2.4. Central Government pension liability –
Addressing the increase**

The Hon. Member for Onchan (Mr Callister) to ask the Minister for the Treasury:

If he will make a statement on the Central Government pension liability, which increased by £832 million to £3,823 million in 2016-17; how this is being addressed?

The Minister for the Treasury (Mr Cannan): Government's Annual Accounts are prepared in compliance with United Kingdom Generally Accepted Accounting Principles ('UK GAAP'). This includes the requirement for an accounting valuation of Government pension schemes as at each balance sheet date. Central Government's accounting valuation is prepared by Scheme Actuaries Hymans Robertson LLP, following the accounting requirements of Financial Reporting Standard 102 (FRS102).

As at 31st March 2017, Central Government's pension liability stood at £3.823 billion. This represents an increase of £832 million (27.8%) on the prior year figure of £2.991 billion. The Scheme Actuary has calculated the pension liability based on a series of financial assumptions. The key financial assumption which determines the pension liability is the 'real discount rate (in excess of CPI)', which is applied to future scheme liabilities, based on anticipated levels of future market returns. This figure reduced down to 0.2% from the discount rate assumed as at 31st March 2016. The movement in this figure is purely as a result of financial market conditions as at the balance sheet date, and in particular a fall in corporate bond yields as at the balance sheet date, together with a rise in expected future inflation. The liability position is very sensitive to significant movements to the financial assumptions, and the real discount rate in particular.

FRS102 states that the discount rate used should be determined by reference to market yields on high quality bonds at the reporting date. Hymans derived the discount rate from a corporate bond yield curve constructed from yields on high quality corporate bonds at 31st March 2017, an approach consistent with the methodology used as at 31st March 2016, in accordance with Pensions Technical Actuarial Standards. The market saw a movement of investors seeking safe haven investments, which pushed up the price of corporate debt and drove down the corporate bond yields. It is this movement which has led to a fall in the real discount rate and hence a corresponding increase in pension liabilities which is not reflective of the sustainability changes made to schemes by the PSPA.

The FRS102 pension liability serves its purpose as an accounting calculation of a liability position, in order to comply with statutory reporting requirements and accounting regulations. The FRS102 accounting liability does not in itself serve the purpose of determining policy surrounding the administration or funding of the Public Sector Pension Schemes.

The FRS102 accounting valuation is not to be confused with the formal statutory triennial valuation of the Isle of Man's unfunded Public Sector Pension Schemes, which was published earlier this year. This formal valuation is undertaken using different methodologies, in particular the calculation of the discount rate which is determined with reference to the expected future income growth of the Island, this being more typical of the sorts of return that a pension scheme could be expected to generate in the long term given freedom to invest in assets wider than just corporate bonds. It is this valuation that is used by the Public Sector Pensions Authority (PSPA) to determine any policy changes or actions required and in particular, the sustainability changes introduced for the Unified Scheme from April 2017 and further changes being discussed with regard to the Police, Teachers and Judicial Pension Schemes.

In addition to the sustainability changes being implemented for schemes, further work is also being undertaken by the PSPA and Treasury to look at cashflow management issues and options (the 'legacy funding issue') with a view to a report coming before Tynwald early in 2018.