

Armed Forces Pension & Compensation Schemes

Main Estimate 2019-20: Estimates Memorandum

1 Overview

1.1 Objectives

The Armed Forces Pension Scheme (AFPS), incorporating the Armed Forces Compensation Scheme (AFCS), is an unfunded defined benefit scheme, in which payments to pensioners are funded by employer contributions, with the shortfall being financed by the Exchequer. The AFPS is free to its members, and therefore, the scheme receives no employee contributions. The AFCS provides compensation for injury, illness and death that are caused by service on or after 6 April 2005.

1.2 Spending controls

The AFPS budgets are not subject to pre-set Departmental Expenditure Limit (DEL) control totals; they sit within a category of spending known as Resource Annually Managed Expenditure (AME), which can be revised and reforecast regularly. This is because net expenditure and cash payments are largely outside the control of the scheme administrators on a day to day basis, instead being affected by factors such as membership numbers; salary levels; mortality rates; the age profile of members, and annual pension increases.

The **Resource AME** sought under the AFPS Estimate is essentially the amount by which liabilities under the pension scheme are estimated to increase during the year, less the contributions paid by employer towards those liabilities.

In addition, the **net cash requirement** represents the estimated net cash required for the year to cover payments of pensions, after taking account of estimated contributions and transfer values paid in. Over time, these amounts are intended to balance, but in a particular year they will not. A negative value means that more is forecast to be received than paid in year.

1.3 Comparison of net spending totals sought

The table below show how the totals sought for the AFPS compares with last year:

Net Spending total Amounts sought this year (Main Estimate 2019-20)		Compared to final budget last year (Supplementary Estimate 2018-19)		Compared to original budget last year (Main Estimate 2018-19)	
		£ m	%	£m	%
Resource AME	£6,407.9m	-£2,895.4m	-45.2%	-£135.5m	-2.1%

1.4 Key drivers of spending changes since last year

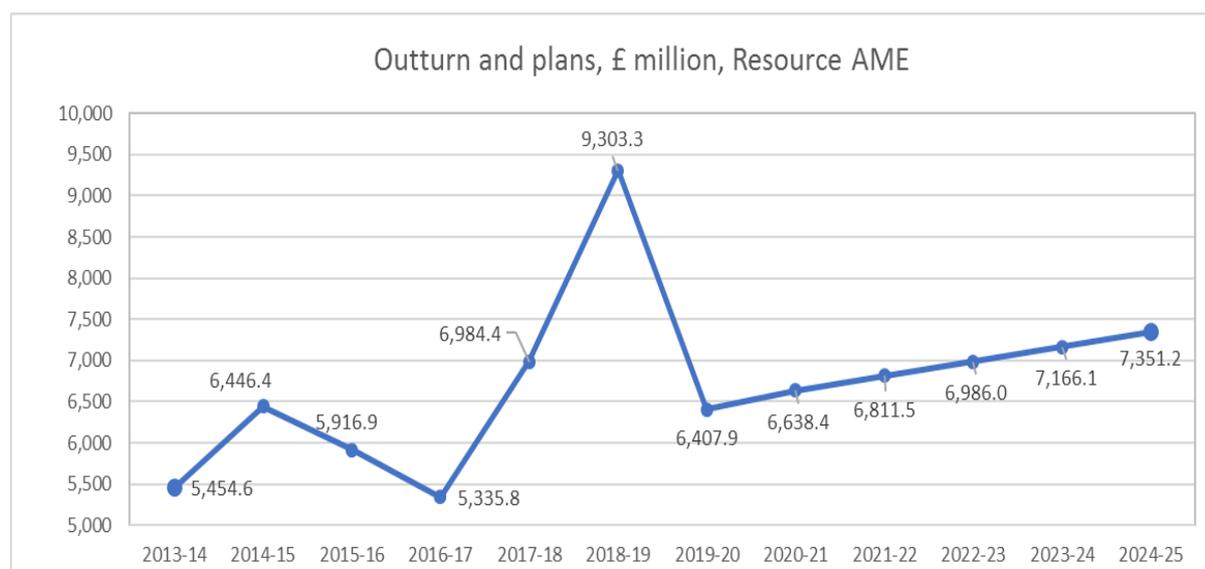
The provision sought under Resource AME is lower than last year, largely as a result of changes to the Treasury set discount rate for long term liabilities, from 0.10% as at 31 March 2018, to 0.29% as at 31 March 2019; and of the interest rate on scheme liabilities, from 2.55% to 2.90%. This reduces the value of additional liabilities expected this year, compared to amount needed to cover new liabilities last year.

The provision sought this year is lower than the 2018-19 Supplementary Estimate, as this included Past Service Costs of £2,600m in relation to the McCloud and Sargeant legal challenges.

1.5 Spending trends

The charts below show overall spending trends for the last five years, plans presented in Estimates for 2019-20.

The year on year changes to Resource AME, shown in the above chart, are largely as a result of annual changes to the Treasury set discount rate for long term liabilities.



1.6 Administration costs and efficiency plans

The costs of the administration of the AFPS are borne by the Ministry of Defence, the employer, and are reflected in the Department's Estimates and Annual Report and Accounts.

2 Spending detail

2.1 Explanations of changes in spending

Subheads	Description	Detail	Resource AME				Over 10% / £10m - See explanation, note/para number
			Main Est 19-20	Supp Est 18-19	Change from Supp Estimate 18-19		
			£ million			%	
A	Expense	- Current service cost	4,365.8	4,480.9	-115.1	-2.6%	1a
		- Past Service cost	0	2,600.0	-2,600.0		1b
		- Interest on scheme liabilities	5,748.0	5,122.4	625.6	10.9%	1c
		- Enhancements and transfers in	1.9	1.9	0	0%	
	Sub Total		10,115.7	12,205.2	-2,089.5	-20.7%	
A	Income	- Employer contributions	-3,644.2	-2,900.0	-744.2	-20.4%	1d
		- Enhancements and transfers in	-1.9	-1.9	0		
		- Other income	-61.8	0	-61.8	0%	1e
	Sub Total		-3,707.9	-2,901.9	-806.0	-21.7%	
A	Net total		6,407.9	9,303.3	-2,895.4	-45.2%	

Note – due to rounding, the totals in the above table may not equal the sum of the parts.

Differences which are above 10% and/or £10 million are explained below:

1.a – A decrease in current service cost is due in the main to the change in discount rate from 0.10% up to 0.29%. As a result, the Government Actuary's Department (GAD) have calculated the current service cost factors (calculated as a percentage of pensionable pay) as 75.4% for both Officers and Other Ranks (previously 76.0% for Officers and 76.8% for Other Ranks).

1.b – In light of the ongoing McCloud and Sargeant court cases, a provision was recognised within 2018-19 to reflect the effect on past service costs due to the potential outcome.

1.c – An increase in interest on scheme liabilities is due in the main to an increase in the interest rate from 2.55% to 2.90%.

1.d – Increase employer contributions are as a result to an increase in the employer contribution rate, as calculated by GAD, from 53.4% (Officers) and 52.0% (Other Ranks) in 2018-19, to 65.5% for both Officers and Other Ranks in 2019-20.

1.e – The scheme will receive additional income in 2019-20 from the Army to cover arrears of pension to a select group of AFPS members.

2.2 Estimated scheme liabilities

The latest valuation of the scheme liabilities for accounting purposes was £195.5 billion, as at 31 March 2018. At the time there were 339,396 Active member benefits, 475,019 Deferred member benefits, and 431,667 Pensioner benefits.

Details of the latest scheme liabilities can be found within the 2017-18 AFPS accounts, report of the Actuary page 13, at the following link: <https://www.gov.uk/government/publications/armed-forces-pension-scheme-annual-accounts-2017-to-2018>

The valuation above is based on detailed member data as at 31 March 2016, and demographic assumptions which are the same as those used for the most recent actuarial valuation of AFPS as at that date.