States of Jersey
States Assembly

États de Jersey
Assemblée des États

Public Accounts Committee

Report on the Accounts of the States Of Jersey

for the year ended 31st December 2010

Presented to the States on 11th November 2011

P.A.C 3/2011

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1. CHAIRMAN'S FOREWORD

The majority of people suffering from alcoholism or other drug addictions are in denial. They say that the hardest problem is to admit that the problem exists because it is only after the problem is accepted that treatment can begin.

In this report the PAC believes that unless there is a swift realisation and acceptance of the severity of the problems facing the Island then the long term financial consequences may be dire.

Despite numerous warnings over the years we now have a situation whereby the Public Sector Final Salary Pension liabilities are significantly larger than the 'Rainy day Fund' (Strategic Reserve), liabilities that exceed one years total income.

The fact that we had to wait for the deficit to exceed £1/2 billion[1] and for questions to be raised regarding the actual solvency of the scheme is to the credit of no one. Elimination of this deficit may require extreme generosity by the taxpayer towards the public sector employees. If this is the case, there is no doubt that some offset in employee terms and conditions will be required.

With expenditure exceeding income in 2010 by £229 million[2], a massive pension fund deficit, some public sector employees being paid significantly more than their UK counterparts in some areas, and a CSR savings programme where many 'savings' are just the utilisation of different funding streams (taxpayer pays), this report should perhaps have been given an 18 rating and filed under the category of 'horror'.

Whilst the PAC agrees that it is wrong to 'talk down the economy', it is also conscious of the fact that corrective measures are unlikely to be taken until the depth of the problem is recognised and accepted.

[1] Discussed at paragraph 5.15 to 5.21 of this report.
[2] States of Jersey Financial Report and Accounts 2010 page 63.

The mis-management of the Public Sector pension liability, and years of denial that a problem exists, has led to a situation whereby the long term liability of the taxpayer exceeds the rainy day fund. Islanders should be under no illusion that a deficit of one thousand million pounds is a serious matter. The level of necessary belt-tightening by all, and particularly the public sector, will be painful and unpopular. It won't be helped by self-interest organisations refusing to accept the severity of the problem.

Through neglect and incompetence we have a public sector pension that is not fit for purpose and an administration that has preferred to spin that no problem exists rather than deal with it.

The PAC is also of the opinion that the imperfect implementation of Ministerial Government could have negative economic consequences for Islanders. The lack of a holistic approach to overall spending and the role of government coupled with a lack of collective responsibility, at both government and executive level, is of significant concern.

Areas of the public sector are extremely expensive on a comparable basis with the private sector and it is questionable whether the public will continue to pay higher taxes to fund inefficiencies and unrealistic pension packages.

Senator Ben Shenton

2. EXECUTIVE SUMMARY

2.1 As an Executive Summary, this section summarises the main findings of the report without discussion or reference to evidence. Further detail may be found in the text of the report.

2.2 The overall message in the PAC Report for the Accounts of 2009 was:
'There is no effective control of States Finances at an overall level.'
It may come as no surprise that nothing has changed. There is still no collective responsibility for the finances of the States of Jersey and no sign of such responsibility being created in the near future.

2.3 Is it therefore being over simplistic to suggest that this could be part of the problem behind the 2010 structural deficit of £229 million? A structural deficit of this magnitude is clearly unsustainable over the long term for an economy such as ours and still, nobody is responsible.

2.4 More emphasis must be placed on the bottom line, on expenditure. Otherwise, the taxpayer will remain vulnerable to savings through higher and higher charges and or taxes. In terms of financial control, the public sector appears to believe that cost of living increases are inevitable and must be funded by the taxpayer. That concept should not be allowed to continue.

2.5 No holistic analysis of Government functions has been undertaken to prevent expenditure in areas outside the States core competences.

2.6 We hear that Jersey is in a good position financially, if that is the case, the Strategic Reserve should be maintained above the equivalent of one year's net revenue expenditure.

2.7 The States of Jersey Financial Report and Accounts are such complex documents that they are of limited value to the public or States Members. There should be a clear and concise document for public consumption.

2.8 As a substantial deficit has built up in the PECRS scheme, the solvency of the scheme has to be questioned, given the assertion of no employer guarantee and limited responsibility. Employee contribution rates should be increased to cover the deficit in a timely manner. The total pension fund liability as at 31st December 2010 was in excess of half a billion and given market movements, this liability is likely to be higher as at 30th September 2011.

2.9 It is questionable whether the States can distance themselves from such a liability as they have a constructive liability. The PAC is concerned about the lack of urgency to deal with the growing pension fund liability and the apparent lack of taxpayer representation on the PECRS Committee of Management, which should be reconstituted with a greater representation on behalf of the taxpayer. Jersey has been slow to deal with the public sector pension time-bomb.

2.10 P143/1999, Public Employees Contribution Retirement Scheme: Proposal to Establish the Scheme Under a Trust Deed and Rules', was agreed by the States in 1999 but never enacted. In 2011 a report (R117/2011) advised that the proposition would not be enacted. There should be a system of checks and balances to ensure that propositions debated and agreed by the States are enacted. This issue has been raised in previous PAC Reports and ignored by the PPC.

2.11 The States of Jersey are providing insufficient financial support for the maintenance of the Islands' infrastructure. This is storing up problems for the future and is indicative that the Island may not be as financially secure as it purports to be. Borrowing may be unavoidable in the future.

2.12 The Committee recognises the good work being done in the area of Terms and Conditions of the workforce. This is a difficult area that is being treated very professionally by all sides to date. However, the generous voluntary redundancy programme implemented in 2010 may not have been the best use of taxpayer's funds given the revision of terms in 2011.

3. Key Findings and Recommendations

The following key findings and recommendations will be found through this report. They are numbered according to the position of the paragraph within the text.

4.7 **KEY FINDING: There is no effective control of States Finances at an overall level.**

4.8 **RECOMMENDATION: Any changes to budgets should be laid before the States Assembly and be fully justified. All financial reports should clearly detail performance against both the final approved budget and all previous budgets.**

4.16 **KEY FINDING: A structural deficit of this magnitude is unsustainable over the long term.**

4.18 **KEY FINDING: Without greater emphasis on expenditure, the taxpayer will remain vulnerable to savings through higher charges.**

4.19 **RECOMMENDATION: Total expenditure should be the primary measure of cost savings initiatives and financial performance throughout the States. CSR cost saving headline figures should not be bolstered by increased charges and other revenue from the public.**

4.24 **KEY FINDING: In terms of financial control, the public sector appears to believe that cost of living increases are inevitable and must be funded by the taxpayer.**

4.25 **RECOMMENDATION: In future there should be no automatic cost of living increases built into any budgets. If cost of living increases are involved, this should be subject of negotiation and justification by the relevant department.**

4.28 **KEY FINDING: No holistic analysis of Government functions has been undertaken, leading to areas of expenditure in areas outside the States core competences.**

4.29 **RECOMMENDATION: There should be a detailed analysis of what functions should be provided by the States of Jersey and what services should be jettisoned because they lie outside the Governments remit. This should be done in consultation with the public – with the clear message that the public will ultimately bear the cost of their requirements.**

4.32 **RECOMMENDATION: The £65 million CSR savings, or whatever figure is decided politically, should be achieved by the cessation of non-core services. Any 'savings' from increased charges should be detailed separately and published to give the taxpayer complete openness on how the public sector is operating.**

4.38 **RECOMMENDATION: The Strategic Reserve should be maintained above the equivalent of one year net revenue expenditure.**

4.54 **KEY FINDING: The complexity of the accounts means that they are of limited value to the public or States Members.**

4.55 **RECOMMENDATION: A set of accounts should be produced in a format that would be more informative for the public and easier to understand.**

5.4 **KEY FINDING: In exchange for passing a £177 million liability to the taxpayer (now over £265 million), the members of the PECRS scheme accepted responsibility for any future deficits.**

5.9 **KEY FINDING: As a substantial deficit has built up in the PECRS scheme, the solvency of the scheme has to be questioned given the assertion of no employer guarantee and limited responsibility.**

5.14 **RECOMMENDATION: Employee contribution rates should be increased to cover the deficit in a timely manner, with payments frozen at current levels.**

5.24 **KEY FINDING. The total pension fund liability as at 31st December 2010 was in excess of £1/2 billion and given market movements, this liability is likely to be higher as at 30th September 2011.**

5.30 **KEY FINDING: It is questionable whether the States can distance themselves from the PECRS liability as they have a constructive liability.**

5.31 **RECOMMENDATION: The full PECRS liability should be recognised in the accounts.**

5.36 **KEY FINDING: The PAC is concerned at the lack of urgency to deal with the growing pension fund liability and the apparent lack of taxpayer representation.**

5.42 **KEY FINDING: A new £4.6 million pension liability appears to have been passed to the taxpayer in less than an open manner.**

5.43 **RECOMMENDATION: Any future agreements to accept pension fund liability shall be brought before the States Assembly for sanction and not agreed behind closed doors. Legal advice received should be made available to States members.**

5.49 **RECOMMENDATION: The PECRS Committee of Management should be reconstituted with a greater representation on behalf of the taxpayer.**

5.54 **KEY FINDING: Jersey has been slow to deal with the public sector pension time-bomb.**

5.55 **RECOMMENDATION: There should be greater urgency to deal with the issues relating to the pension funds and this should be led by the Treasurer who should produce a Report to the States Assembly by March 2012 setting how the liability will be managed and contained.**

5.68 KEY FINDING: A proposition was passed by the States in 1999 but never enacted. In 2011, R.117 advised that the proposition would not be enacted.

5.69 RECOMMENDATION: There should be a system of checks and balances to ensure that propositions debated and passed by the States are enacted. This issue has been raised in previous PAC Reports and ignored by the PPC.

6.7 KEY FINDING: The States of Jersey are providing insufficient support for the maintenance of the Islands' infrastructure.

6.8 RECOMMENDATION: The level of financial support for the maintenance of the Islands' infrastructure must be significantly increased.

6.26 KEY FINDING: The Island may not be as financially secure as it purports to be and borrowing may be unavoidable in the future.

6.27 RECOMMENDATION: The Minister for Treasury and Resources must prepare legislation in the event that borrowing may be essential in the future.

6.35 KEY FINDING: The Committee recognises the good work being done in the area of Terms and Conditions.

6.36 RECOMMENDATION: The Public Accounts Committee, as constituted in 2012, should examine progress with remuneration when it undertakes the review of the States of Jersey Financial Report and Accounts 2011.

6.45 KEY FINDING: The generous voluntary redundancy programme implemented in 2010 may not have been the best use of taxpayer's funds given the revision of terms in 2011.

6.46 RECOMMENDATION: The States Employment Board should have external independent members to ensure transparency of the decision making process.

4. The Sustainability of the Current Economic Path

4.1 In 2010, the Committee published its report, "Report on the Accounts of the States of Jersey for the year ended December 31st 2009". The report contained the below table pointing out that the expected level of expenditure for 2009 increased from £466 million when first forecast in the 2005 budget statement, to £546 million in the 2009 budget statement and to an actual expenditure of £603 million (which included the financial stimulus package).

Year of account										*Budgets- £ million*
	2001	*2002*	*2003*	*2004*	*2005*	*2006*	*2007*	*2008*	*2009*	*2010*
2001	343									
2002	363	375								
2003	381	394	394							
2004	398	414	414	408						
2005			435	424	423					
2006				438	433	441				
2007				450	444	454	474			
2008				462	455	457	492	505		
2009					466	480	507	525	546	
2010					478	490	518	546	563	586
2011							532	565	581	611
2012								583	598	620
2013									616	

[3]

4.2 This observation was concluded by the following key finding:

"Key Finding

In 2009, the States overspent against forecast by over £100m based on the original financial forecast 2005-2010."

[3] Erratum: the figure '457' in line '2008 column '2006' should read '467'

4.3 The report went on to make the following recommendation:

4.12 Recommendation

The importance of accurate financial forecasting cannot be under-estimated. A maximum deviation of 2% should be the goal and there should be an annual review of forecasting accuracy with a detailed analysis of circumstances where a 2% deviation is breached. This should be published by the Minister for Treasury and Resources."

4.4 The committee recognises that changes in that area cannot be made immediately; however, the problem has been exasperated in the last twelve months. The expected level of expenditure for 2010 increased from £478 million when first forecast in the 2005 budget statement, to £599 million[4] in the Budget Statement 2010. It should be noted that actual expenditure in 2010 was £975 million, £229 million more than income received.

4.5 Whilst the increase in budget may have been "justified" the ability to seemingly increase budgets at will makes a mockery of the concept of prudent financial management.

4.6 Even accepting that estimating budgets is perhaps as much art as science, these inaccuracies are surely more than any institution can bear within a strategic plan. There is little point reiterating the reasons for the problems examined in the report mentioned above, as the figures evidence that the recommendations contained in that report for more accurately forecasted budgets have not been heeded.

4.7 **KEY FINDING: There is no effective control of States Finances at an overall level.**

4.8 **RECOMMENDATION: Any changes to budgets should be laid before the States Assembly and be fully justified. All financial reports should clearly detail performance against both the final approved budget and all previous budgets.**

[4] Figure repeated in Budget Statement 2010. Page 15

4.9 Further, there is a complete disconnect of responsibility for States wide finances beyond Departmental level. Ministers are corporate sole and therefore legally responsible for the finances of the Department. Chief Officers (in the main) are the Accounting Officers and hold legal responsibilities for Departmental spending. However, there is no collective responsibility. This has been pointed out and discussed on numerous occasions, for example:

- PAC Report on the Accounts of the States of Jersey for the year ending December 31st 2009. (PAC 4/2010) Key Finding 8.8 and Recommendation 8.9.

- Comptroller and Auditor General report 'Public Finances (Jersey) Law 2005. A review in the light of experience. February 2010':

  "If the Treasurer is not the person responsible for monitoring expenditure control, it is not clear who has the responsibility. At least, it is clear that the 2005 Law does not refer to anyone else who might be thought to have responsibility and that appears to be a significant weakness in the 2005 Law. It is unsatisfactory that the 2005 Law is precise in its description of Departmental responsibilities but silent on States-wide control and responsibilities."

- Corporate Services Scrutiny Panel report 'Forecasting of Expenditure' 16th April 2010 (SR 5/2010) Key Findings 5 and 7, discussed between pages 19 and 23.

4.10 It is not the intention of the Committee to go through the detail of these arguments again but it needs to be recognised that this is a problem which will re-surface whenever the finances of the Island are examined. It will be a thorn in the side of financial planners and the Council of Ministers until the Public Finances (Jersey) Law 2005 is amended to apportion collective responsibility.

4.11 KEY FINDING

There is no collective responsibility for the finances of the States of Jersey.

4.12 RECOMMENDATION

The Minister for Treasury and Resources must have the Public Finance (Jersey) Law 2005 amended to have collective responsibility included.

4.13 The public are perhaps under the false impression that Jersey's finances are balanced and in good order. Yet the operating cost statement shows that in 2010, Operating Expenditure (£935.9 million) exceeded total revenue (£745.7 million) by about £190 million.

4.14 When other costs such as depreciation are taken into account the deficit increases to £229 million.[5]

4.15 The Council of Ministers has recognised that the States is faced with a potential permanent shortfall between its income and the cost of providing services - a structural deficit - based on the forecasts in 2009 and 2010. It also recognised that the historic pattern of year on year increases above planned spending targets cannot continue if the States is to live within its means.

4.16 **KEY FINDING: A structural deficit of this magnitude is unsustainable over the long term.**

4.17 The Comprehensive Spending Review (CSR) was intended to run in parallel with a Fiscal Strategy Review to identify both savings and fiscal options to address the structural deficit. The process was designed to review government income and expenditure and set firm cash limits for expenditure, which should only be varied in extreme circumstances. The CSR process required the agreement of savings targets for all departments and commitment to the requirement for departments to deliver.

4.18 **KEY FINDING: Without greater emphasis on expenditure, the taxpayer will remain vulnerable to savings through higher charges.**

[5] States of Jersey Financial Report and Accounts 2010 page 63.

4.19 **RECOMMENDATION: Total expenditure should be the primary measure of cost savings initiatives and financial performance throughout the States. CSR cost saving headline figures should not be bolstered by increased charges and other revenue from the public.**

4.20 2010 saw the first tranche of work on this project being undertaken to implement the first 2% of savings within the 2011 year. The Committee can see the writing on the wall before the process gets underway. The savings recommended are in many cases simply passing the costs onto the public of the Island by user pays options. This does not reduce the cost of a service, it simply creates an alternative funding stream. Therefore, few real savings are being made.

4.21 In addition, most departments are in receipt of 'cost of living' increases at the same time. The Committee is confused how a budget can be said to be saving money when the budget actually increases because the real terms adjustment for 'cost of living' increase is greater than the CSR savings imposed upon it. The States appear to be 'talking the talk' of saving money but not 'walking the walk'.

4.22 During the hearing with the Treasurer, the Committee recognised that the gross expenditure of departments was still rising despite the CSR process. If significant savings are to be achieved, should this not be reflected in the gross amount being spent by departments? The Treasurer replied:

> *"… why would you want to do that when it is not a proper reflection of the position because, to give a proposer reflection of the position, you need to take account of the real terms cost which means that you have to adjust for inflation, you have to adjust for pay awards and other matters."*

4.23 The States of Jersey is not a private company and there are many reasons why it is dangerous to draw analogies between the two. However, private companies are required to remain within their income budget. They have no sacred cow to milk when the going gets tough i.e. the taxpayer. They are obliged to spend the same or less than their income and have to cut their cloth accordingly. Failure to balance the books is not only unsustainable but will lead to the collapse of the business at some point.

4.24 **KEY FINDING: In terms of financial control, the public sector appears to believe that cost of living increases are inevitable and must be funded by the taxpayer.**

4.25 **RECOMMENDATION: In future there should be no automatic cost of living increases built into any budgets. If cost of living increases are involved, this should be subject of negotiation and justification by the relevant department.**

4.26 The lack of political will to cut the States spending to a level below its income can only lead to higher taxes for the public. How to raise more taxes is in itself a completely new argument, which could keep States Members busy in debate for years.

4.27 The Panel considered why there was a need for expenditure to continue to rise. The answer appeared to be that the CSR fails to deal with the fundamental issues of the financial problems. A root and branch review of what the States of Jersey do as a government is required. As a minimum, the following questions need answers:

i) What are the core tasks of Government?
ii) What services should or could the Government of Jersey be providing for its residents?
iii) Where do the expectations of the public start and finish?
iv) What are the options and limitations of provided services?

4.28 **KEY FINDING: No holistic analysis of Government functions has been undertaken, leading to areas of expenditure in areas outside the States core competences.**

4.29 **RECOMMENDATION: There should be a detailed analysis of what functions should be provided by the States of Jersey and what services should be jettisoned because they lie outside the Governments remit. This should be done in consultation with the public – with the clear message that the public will ultimately bear the cost of their requirements.**

4.30 In the meantime, despite the CSR, the States gross spending appears set to continue to rise and the public will be required to meet the bill.

4.31 That means that there will, by necessity, be further infrastructure taxation. It may be termed 'User Pays' or higher Goods and Services Tax but means that the public will pay for a service one way or another. As indeed, at the moment, the public pay over and above their normal taxes for, amongst many other things:

- the roads infrastructure by way of an additional tax on the fuel they use in their vehicles.
- some x-ray services at the Hospital.
- the emptying of septic or tight tanks etc.

The introduction of general sewerage charges might seem to be a good way of raising revenue, but that does not mean that the States has to provide the service. Others could do that, as indeed others supply electricity, water and communications in the Island now. The PAC is concerned that higher user pays charges may be levied to bail out a government unwilling to carry out real savings. Therefore any increased charges should only be implemented once non-core savings have been made. The PAC is concerned that the public sector inefficiencies will be funded by the taxpayer who will suffer the double burden of higher user charges plus higher taxation.

4.32 **RECOMMENDATION: The £65 million CSR savings, or whatever figure is decided politically, should be achieved by the cessation of non-core services. Any 'savings' from increased charges should be detailed separately and published to give the taxpayer complete openness on how the public sector is operating.**

4.33 The Committee recognises the benefits of the Strategic Reserve and agrees with its purpose.

> ***"Strategic Reserve***
> *The Strategic Reserve Fund is established in accordance with the provisions of Article 4 of the Public Finances (Jersey) Law 2005. This is a permanent*

reserve, where the capital value is only to be used in exceptional circumstances to insulate the island's economy from severe structural decline such as the sudden collapse of a major Island industry or from major natural disaster.

In December 2006 the States agreed that the long-term aspiration was to grow the Strategic Reserve by an additional £100-£120 million so that it equates to about 20% of GDP.

The total assets of the Reserve at year end [2006], at market value, were £477.2 million."[6]

4.34 In 2006, the Net Revenue Expenditure was £465 million[7]. Therefore, the Strategic reserve represented 102% of that year's expenditure.

4.35 The Strategic Reserve balance at the end of 2010 was £586.7 million[8]. The Minister for Treasury and Resources has stated in the Draft Budget Statement 2012:

"The States' balance sheets includes a safety net of close to a years spending set aside in the Strategic Reserve."[9]

4.36 The Net Revenue Expenditure for 2010 was £599 million[10]. Therefore, in 2010 the Strategic Reserve represented 98% of the year's expenditure.

4.37 The reserve is in decline relative to annual expenditure and steps are required to rectify the situation either by reducing the Net Revenue Expenditure or by increasing the contributions to the Strategic Reserve. The Committee notes that the Jersey Fiscal Policy Panel have recommended no transfers into or out of the Strategic Reserve at this stage,[11] which suggests the only available course of action is to reduce expenditure.

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[6] States of Jersey Financial Report and Accounts 2006, page 79.
[7] States of Jersey Financial Report and Accounts 2006 page xi.
[8] States of Jersey Financial Report and Accounts Annex P127
[9] Draft Budget Statement 2012 Page 7.
[10] States of Jersey Financial Report and Accounts Page 6.
[11] Jersey Fiscal Policy Panel report July 2011 page 3, recommendation 2.

4.38 **RECOMMENDATION: The Strategic Reserve should be maintained above the equivalent of one year net revenue expenditure.**

4.39 Although the Net Revenue Expenditure was £599 million, that is not a complete picture of the expenditure of the Island and to obtain that one needs to look to the total expenditure. This includes operating expenditure and non-operating expenditure. The total expenditure for the Island in 2010 was over £974 million.[12] (£190 million more [24%] than the total expenditure in 2009 of £784 million).

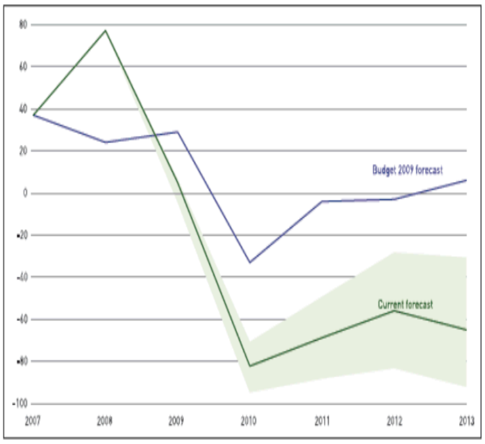
4.40 That is a £229 million deficit for 2010.

4.41 The move to GAAP accounting requires the inclusion of 'Depreciation' and 'Impairment of Fixed Assets'. This is a real cost to the Island as at some point everything used has to be replaced and even buildings have a finite lifespan, as the increasingly inappropriate hospital buildings are currently demonstrating. So the money for these items to be replaced is taken into account with 'Depreciation' and 'Impairment of Fixed Assets'. This money must be put aside year on year or there will be nothing available in the future to pay for essential replacements. If this is not done, the Island is 'living beyond its means'. A deficit of £229 million certainly appears to qualify for 'living beyond its means'

4.42 The explanation to the States of Jersey by the Fiscal Policy Panel in their 2009 report explained that a serious financial crisis was on the horizon.[13]

Figure 2.9:
Changes in the forecast for public finances
Financial forecasts – budget surpluses and deficits, £m (with EfW timing adjustment)
Sources: States of Jersey Treasury and Resources Department and Economics Unit

Note: Budget 2009 forecast shows 2008 probable estimate and the original EfW adjustment. Current forecast shows 2008 provisional outturn, the revised EfW timing adjustment, the current estimate of the net capital expenditure allocation adjustment and the impact of the economic downturn



[12] States of Jersey Financial Report and Accounts 2010 page 63.
[13] Jersey Fiscal Policy Panel report 2009 page 25, Figure 2.9.

4.43 On 9th April 2009 the Minister for Treasury and Resources lodged au Greffe P55/2009, Economic Stimulus Plan with the intention of assisting the Island through the recognised forthcoming financial downturn. As the finance for this was from the Stabilisation Fund, the outflow was effectively neutral but it shows clear recognition of the financial problems lying in wait for the Island. However, it appears to have done nothing to alleviate the relationship between spending and income in 2010. The runaway train of expenditure continues onward and upward regardless of the consequences.

4.44 The Fiscal Policy Panel has repeatedly recommended that any unallocated funds in the Consolidated Fund in excess of £20 million should be transferred into the Stabilisation fund. The Committee notes that the Fiscal Policy Panel states that 2010 ended with £54 million in the Consolidated Fund.[14] Different data within the States of Jersey Financial Report and Accounts shows figures relating to the Consolidated Fund at the end of 2010 of:

£40.6 million[15]
£106 million[16]
£2,165 million[17]

4.45 In an attempt to sort out the confusion, the Treasury Department were asked to explain the different figures. The following explanation was offered:

"The best way to examine the Consolidated Fund Balance available to be spent by the States is to review section 2.7.1 of the Accounts (Page 28), which also includes a brief explanation of how the balance is calculated. The figures for the top half of the table can be tied back to the Balance Sheet for the Consolidated Fund via Note 2b on Page 81 ("Total Consolidated Fund" column) as follows:

14 Jersey Fiscal Policy Panel Report July 2011 page 34/5 and Figure 2.14.
15 States of Jersey Financial Report and Accounts 2010 page 29.
16 States of Jersey Financial Report and Accounts 2010 page 25.
17 States of Jersey Financial Report and Accounts 2010 page 97.

	Note 2b	Table	
Fixed Assets	2,476,597	0	Not Included
Financial Assets	501,346	212,889	Strategic Investments in Utility Companies (£254m - Note 10) and WEB (£20m), and Housing Bonds (£14m - Note 13) removed
Current Assets	146,688		
Interfund Balance	-48,065	-20,336	Combines into Net Assets
Current Liabilities	-118,959		
Long Term Liabiliteies	-384,127	-4,387	Only Long Term Provisions included (other amounts relate to Pensions and Finance Leases)
Add Back:		9,191	As shown in Table
	2,573,480	**197,357**	

As explained, the amounts removed are either not easily realizable (Fixed Assets, Strategic Investments etc), or will be funded from future approvals (liabilities etc). Adjustments are then made to incorporate amounts already committed, including Unspent Capital Budgets. This gave a final available balance of £41m.

The FPP report shows the balance on the same basis as the Budget and Business Plan, by removing the effect of Carryforwards on the closing balance (and instead including them as part of expenditure in the following year). For 2010, the total amount carried forward from was £16m, but removing amounts carried forward from Fiscal Stimulus and 11(8) (see MD-TR-2011-0040 and MR-TR-2011-0042), the total was £13m - the difference between the two figures."[18]

4.46 The States of Jersey Report and Accounts states that at 31st December 2010, the Strategic Reserve stood at £568,659 million[19] according to the main report or £586.7 million[20] according to the Annex. A note sent to the Treasury Department for clarification of the £18 million difference obtained the following response:

"For the Strategic Reserve, the balance was indeed £586m, with the difference from the figure you refer to being the investment reserve (see page 130 of the Annex)."[21]

18 Email received in the Scrutiny Office 1555hrs 10.10.11.
19 States of Jersey Financial Report and Accounts Annex P127
20 States of Jersey Financial Report and Accounts 2010 page 97.
21 Email received in the Scrutiny Office 1555hrs 10.10.11.

4.47 The reply goes on to explain that the figures above each look at something different in the accounts that are rather technical accounting points and would have to be explained.

4.48 The Committee is aware of the lack of clarity available to the average man reading the States of Jersey Financial Report and Accounts. The problem was highlighted with the Consolidated Fund earlier in this report and here again with the Strategic Fund. This raises the questions:

- Who is this documents' target audience?
- What is its purpose and
- Does it achieve those aims?

4.49 Clearly, it is not intended for the ordinary man in the street or even the average States Member. Article 32 of the Public Finances (Jersey) Law 2005 (1) (a) requires the Treasurer to prepare the Annual Financial Statement in respect of the accounts of the States. (1) (b) Requires the Treasurer to send the statement to the Comptroller and Auditor General for audit. Therefore, the target audience would appear to be the Comptroller and Auditor General.

4.50 Article 46 of the Public Finances (Jersey) Law 2005 requires the Comptroller and Auditor General to ensure, amongst other things, that the provisions of that Law are being duly complied with.

4.51 This would suggest that the document is intended for consumption at the highest levels within the accounting profession and that it is therefore not intended for the understanding of the average man, i.e. States Members. That raises some fundamental questions:

- Is it safe to put such checks and balances beyond the understanding of States Members?

- Should there be a simplified document designed for general understanding?

4.52 The Treasurer was asked at the hearing about the difficulties of comparing one years report with those of previous years. An observation she agreed with.[22] When asked about the explanation of the accounts to States Members the Treasurer stated:

> *"… I am keen to produce summary statements of the accounts and the budget which I am used to preparing in previous jobs, simple statements…I think we should be producing a version of these accounts which ordinary people in Jersey can pick up and follow and understand, and there is no reason why we cannot do that, and the same applies for the budget."*[23]

4.53 The PAC agrees with these sentiments. The Accounts of the States must be made more transparent and accessible and would be interested to hear the views of the C&AG on the current format.

4.54 **KEY FINDING: The complexity of the accounts means that they are of limited value to the public or States Members.**

4.55 **RECOMMENDATION: A set of accounts should be produced in a format that would be more informative for the public and easier to understand.**

[22] Hearing 5th Sept. 2011. Question by Senator A. Breckon page 8.
[23] Hearing 5th Sept. 2011. Question by Senator J. L. Perchard page 27

5. Public Sector Pensions

5.1 Public sector pensions have caused significant financial pain in the past to the States of Jersey. The realisation of the pre 1987 scheme left the States of Jersey with a liability as at 31st December 2001 of over £177 million that will be drawing from the Islands income until 2083. [24]

5.2 In relation to the current scheme, the Public Employees Contribution Retirement Scheme (PECRS), the next three year Actuarial review is due at the end of December 2011. However, there is increasing concern about the liabilities of the States of Jersey and Members of the scheme should there be a deficit.

5.3 The matter of liability is dealt with in the Public Employees (Contributory Retirement Scheme) (General) (Jersey) Regulations 1989. Article 6(3) (d) + (e) deals with the responsibilities of the States, Chief Minister and the Committee of management of PECRS. It states:

(d) where a deficiency is disclosed such proposals may with the agreement of the Committee (but not to the exclusion of other proposals upon which the Chief Minister and the Committee have by then agreed or shall, within the period of 6 months immediately after the report is laid before the States, agree) consist of –

(i) if the deficiency appears to be of a temporary nature, a recommendation that no action should be taken, or

(ii) an increase in the contributions payable by the members under the 1989 Existing Members Regulations and the 1989 New Members Regulations and/or in the contributions payable by the employers to the scheme;

(e) if a deficiency is disclosed and, within the 6 months immediately after the report is laid before the States, the Committee and the Chief Minister have not agreed on proposals, then after a further period of 3 months –

(i) the Committee shall reduce or cancel any increase in pensions, deferred pensions and deferred lump sums (including pensions and lump sums determined at normal retiring age under Regulation 5 or 10(4) of the

[24] Article 4a Public Employees (Contributory Retirement Scheme) (General) (Jersey) Regulations 1989.

Former Hospital Scheme Regulations which have been deferred owing to the employee remaining in membership beyond normal retiring age) that might otherwise thereafter have been made pursuant to Regulation 11 in the manner recommended in the Actuary's report in order to eliminate the deficiency as far as possible, and

(ii) if the Actuary's report indicates that even after the operation of clause (i) a deficiency is likely to continue to exist, the Chief Minister shall submit proposals to the States for an increase in the contributions payable by the members under the 1989 Existing Members Regulations and the 1989 New Members Regulations and/or in the contributions payable by the employers to the scheme and/or a reduction of other benefits payable under the 1989 Existing Members Regulations and the 1989 New Members Regulations;

(f) the agreement of the Committee to proposals under sub-paragraphs (b) and (d) shall be supported by a majority of the employer representatives and a majority of the member representatives present.

5.4 **KEY FINDING: In exchange for passing a £177 million liability to the taxpayer (now over £265 million), the members of the PECRS scheme accepted responsibility for any future deficits.**

5.5 The Actuarial Valuation of 2007 revealed a total deficiency of £63.2 million which instigated a series of negotiations in compliance with Article 6 above. The Human Resources position was that the Chief Minister, advised by the Employer's Actuary, considered the deficiency could not be seen as being of a temporary nature and should not be carried forward, especially in the light of the serious stock market decline since the valuation date and its effects on pension schemes. As the employer refused to increase their current contribution to the scheme, the deficiency was to be met entirely by scheme members.

5.6 Unless an increase of 2.8% in member contributions was agreed, the default position would have to apply. The default position had been stated by the Scheme Actuary in the Valuation as reducing future increases to all pensions and deferred pensions due on or after 1 January 2011 to 0.3% below the annual increase in the Jersey Cost of

Living Index in each successive year. The Chief Minister's 3-month report to the States as at 11 November 2009 indicated that no agreement on proposals had been reached.

5.7 Continued negotiations failed to reach an agreement and the default applied as at 1 January 2011. Relating to the surplus or deficit within the PECRS scheme, the Financial Report and Accounts shows a deficit of £526 million.[25] There is nothing relating to this figure within the PECRS Annual Report 2010. Enquiries about this with the Treasury Department produced the following response[26]:

> *"The figures shown in the notes to the States of Jersey Annual Accounts are calculated by the Independent Actuary under Financial Reporting Standard 17 (FRS 17)* [27]*. The States are required to calculate pension figures in accordance with this accounting standard for the notes in the annual accounts.*
>
> *You will not find these FRS17 figures in the PECRS annual accounts. The pension fund is also valued on an actuarial basis every three years by the Independent Actuary. This provides an assessment of the funding level of the scheme at a point in time. An actuarial valuation as at 31st December 2010 is currently being completed."*

5.8 The statement of accounting policies is of particular interest as it clearly and unambiguously states that the employer is not responsible for meeting any ongoing deficiency in the schemes. On the basis that the scheme is no longer term guarantor and has substantial debts, it is difficult to fully understand why the contribution rates by employees have not been increased significantly to eliminate the deficit in a timely manner. Furthermore, it is questionable whether the enrolment of new members in a scheme that has substantial liabilities and no guarantor is morally correct or would be sanctioned in any other environment. New States employees may have to make significant contributions to the debts accumulated before they began employment – a situation that should be made illegal as it is not in the best interests of the individual members.

[25] States of Jersey Financial Report and Accounts P117
[26] Email received at Scrutiny Office 1550hrs 12.10.11.
[27] Accounting Standards Board Financial Reporting Standard 17 sets out the requirements for accounting for retirement benefits.

5.9 **KEY FINDING: As a substantial deficit has built up in the PECRS scheme, the solvency of the scheme has to be questioned given the assertion of no employer guarantee and limited responsibility.**

5.10 The Committee has also noted that issues in respect of the Teachers Superannuation Scheme have still not been resolved. A situation that is totally unacceptable.

5.11 Whilst the taxpayer may be comforted by the repeated declaration that the pension fund liability lies with members, the Committee questions whether these schemes are now 'solvent' in the absence of a guarantor. We believe that the actuary is applying solvency calculations on the basis that the employer will step in. Given that these are unique schemes, the Committee believes that much harsher calculations should be adopted based on the political assurances of no additional funding from the employer and a smaller membership in line with the stated Government objectives of significant cost controls.

5.12 There is a problem with the cross-subsidy between uniformed and non-uniformed staff. It is a fact of life that a uniformed person cannot earn in his or her relatively short career enough to pay the generous final salary scheme. They will require the charity of the taxpayer in order to claim their pension. It is immoral for the pensions and early retirement provisions of uniformed staff to be subsidised by non-uniformed staff.

5.13 There should be no change to the employer contribution without negotiation as the fall-back provision in the ten-point plan is clear and unambiguous (See Appendix 3).

5.14 **RECOMMENDATION: Employee contribution rates should be increased to cover the deficit in a timely manner, with payments frozen at current levels.**

5.15 There is an alarming lack of willingness on behalf of the Treasury to get to grips with the public sector pension problems. The deficit is substantial and may be the biggest threat to the wealth of the Island.

5.16 As previously mentioned the last published Actuarial Valuation of the scheme was dated 31st December 2007 – almost four years ago – and showed an actuarial deficit of £63.2 million.

5.17 On 8th September 2009 Hewitt Associates presented the Committee of Management with a paper provided the following figures:

	2007	2009
	Value	Estimated Value
Accrued benefits shortfall	£305.9m	£895.0m

5.18 Since that time, weak investment returns and falling long term interest rates would have significantly increased this deficit. The anticipated optimistic investment returns have proved to be hopelessly unrealistic and the decline in long term interest rates has accelerated the problem.

5.19 In the Consolidated Balance Sheet[28] the following liabilities are detailed;

- PECRS Pre-1987 Past Service Liability £ 265,435,000
- Provision for JTSF Past Service Liability £ 114,000,000
- Defined Benefit Pension Scheme Net Liability £ 11,152,000

5.20 The scheme does not include the current PECRS liability which is shown at £526,245,000 on page 117 of the Accounts. This figure should be properly reflected in the accounts.

5.21 Since the valuation was prepared, the deficit will have increased substantially as long term interest rates have declined and stock markets have suffered a sharp setback.

5.22 The liability is now likely to exceed £1 billion and the buy-out figure would be significantly higher than this.

5.23 **KEY FINDING. The total pension fund liability as at 31st December 2010 was in excess of £1/2 billion and given market movements, this liability is likely to be higher as at 30th September 2011.**

5.24 What is even more disconcerting is that these figures may have been repressed through the use of unrealistic investment return assumptions which should be reduced in light of the new investment landscape.

5.25 If the taxpayer was not liable to the liabilities within the scheme it would make sense for the taxpayer (States) to distance itself as far as possible – and on 28th September 1999, proposition ‘P.143/1999 – Public Employees Contributory Retirement Scheme:

[28] States of Jersey Financial Report and Accounts P64

proposal to establish the scheme under a trust deed and rules', was lodged *au Greffe* by the Establishment Committee of the day for debate by the States Assembly. In that Proposition, the States were asked to agree in principle that PECRS should cease to be a statutory scheme and instead should be established as a Trust and administered under a Trust Deed and Rules.

5.26 It was interesting to read 'R.117, Public Employees Contribution Retirement Scheme: Trust Status', presented to the States on 27th September 2011(See Appendix 2 for full report). It states;

> *"Any move to a private trust scheme might lead, either immediately or over time, to a loss of influence by the States without any commensurate reduction in responsibility or liability in real terms."*

5.27 Yet the accounts state;

> *"The scheme, whilst a final salary scheme, is not a conventional defined benefits scheme as the employer is not responsible for meeting any ongoing deficit in the scheme"* [29]

5.28 That disclosure[30] goes on to state that the liability is therefore not recognised in the States' accounts on the balance sheet.

5.29 **KEY FINDING: It is questionable whether the States can distance themselves from the PECRS liability as they have a constructive liability.**

5.30 **RECOMMENDATION: The full PECRS liability should be recognised in the accounts.**

5.31 Yet compare that declaration – signed off by the Minister, Treasurer and Auditors – with the reason for not seeking trust status. The elimination of the liability appears to be just smoke and mirrors accounting rather than fact.

5.32 So, on the uncertain assumption that the taxpayer is responsible for the deficit, who is actually looking after the interests of the taxpayer? It certainly does not appear to be

[29] States of Jersey Financial Report and Accounts. Note 30 P112
[30] States of Jersey Financial Report and Accounts. Note 30 P112

the PECRS Committee of Management (CoM). The Chairman states in the PECRS Annual Report – page 8 – that the CoM acts

> “in the best interests of all pensioners, deferred pensioners and active members”.

5.33 There is no mention of the wider taxpayer and this is perhaps why previous attempt of the PAC to get the pension liability problem properly addressed has been met with unprofessional disparaging comments such as

> “a significant lack of understanding on the part of many States Members.” [31]

5.34 If the CoM are acting in the best interests of the members of the scheme it may be in their ‘best interests’ not to deal with the issues, to procrastinate, and allow a situation to develop that forces the taxpayers to step in whilst retaining all benefits.

5.35 **KEY FINDING: The PAC is concerned at the lack of urgency to deal with the growing pension fund liability and the apparent lack of taxpayer representation.**

5.36 The PAC remains convinced that it is impossible to have a final salary pension scheme without the employer acting as final guarantor – the PAC cannot find schemes anywhere in the world of this nature. In the Report on the Accounts of the States of Jersey for the Year ending 2009, the Committee quoted the then Interim Treasurer :

> *“I would say it is an unusual arrangement that I have not come across elsewhere where the employer is not responsible for the deficit on the scheme, but that appears to be the agreement that has been made and the auditors have verified and assured themselves that it is correct, so I am informed."* [32]

5.37 Indeed the whole argument in respect of limiting future liability is thrown into confusion in the accounts. Page 95, note 20, of the SoJ Accounts shows a 1972 Act Pensions Increase Liability of £4,664,000 with a note that “this is a new liability resulting from a decision made in 2010”. (See Paragraph 5.6)

5.38 If the taxpayer is to be lumbered with a new £4.6 million liability perhaps there should have been some discussion. If you cross-reference with page 7 of the PECRS CoM

[31] PECRS Annual Report 2010 page 7.
[32] Public Hearing with the Interim Treasurer 20th September 2010. Page 2.

Annual report you discover that the additional liability arose in respect of members who retained entitlements under the 1967 regulations or the Former Hospital Scheme regulations.

5.39 The difficulty here is that one would assume that the obligation to pay these increases to such members was part of the pre-1987 liability of PECRS which, as far as the States are concerned, are supposed to be capped.

5.40 Page 72 of the SOJ Accounts (note xix.iv) states that the issue was the subject of legal discussions. The admission of the liability in the accounts, and the acceptance of an additional liability of £4.6 million without notifying States Members, appears to demonstrate that exposure to pre-1987 liabilities is not limited. Any back-bencher reading this will be appalled that £4.6 million can be added to liabilities so easily – especially if they have attempted to get smaller sums allocated for worthy causes.

5.41 **KEY FINDING: A new £4.6 million pension liability appears to have been passed to the taxpayer in less than an open manner.**

5.42 **RECOMMENDATION: Any future agreements to accept pension fund liability shall be brought before the States Assembly for sanction and not agreed behind closed doors. Legal advice received should be made available to States members.**

5.43 The actions of Policy and Resources Committee in dealing with the pre-1987 debt was inept as, in their desire to distant the States from the liability, they failed to take into account the fact that final salary schemes over the longer term are unaffordable for the taxpayer.

5.44 The procedure for the appointments to the Committee of Management is created by the Public Employees (Contributory Retirement Scheme) (General) (Jersey) Regulations 1989.

Article 3 Committee of management

(1) There shall be established a Committee of Management which shall have and exercise all such powers, authorities and discretion as are vested in it by the Regulations governing the scheme.

(2) *Subject to the provisions of this Regulation, the Committee shall be appointed by the States on the recommendation of the Chief Minister and shall comprise –*

(a) *a Chairman who shall be appointed in accordance with paragraph (6);*

(b) *6 employer representatives and 6 member representatives (or such greater equal number of employer representatives and member representatives as may be determined from time to time by agreement between the Chief Minister and the representative associations) appointed as follows –*

(i) *one-half of the employer representatives shall be chosen by the Minister for Treasury and Resources,*

(ii) *nominations for member representatives shall be determined in such manner as the Chief Minister shall agree with the representative associations.*

5.45 This requires a Chairman, with a Committee containing six employer representatives and 6 employee representatives. The Treasurer of the States of Jersey held a position on the Committee of Management but 'P60/20010, public Employees Contributory Retirement Scheme Committee of Management: Membership' replaced the treasurer with an employee representative. It may be argued that the Treasurer was either poacher or game-keeper, however, since then there has clearly been no representative of the taxpayer. All members of the Committee of Management now have a direct interest in the fund. There are no completely independent members of the committee, nor are there any direct representatives of the taxpayer.

5.46 The taxpayer must have a much greater involvement in the running of the fund, reducing the power of a self-interested Committee of Management that through failure to act in the best interests of the Island may have burdened the taxpayer with an unacceptable encumbrance.

5.47 The Treasurer and Treasury Minister must take much greater control – acting strongly on behalf of the taxpayer who will be charged with paying off a significant portion of the debt.

5.48 **RECOMMENDATION: The PECRS Committee of Management should be reconstituted with a greater representation on behalf of the taxpayer.**

5.49 The PAC asks for an estimate to be produced and published, by the Committee of Management of all schemes, based on a 30th September 2011 valuation as a matter of urgency.

5.50 The point here comes from a note at the top of page 120 of the States Of Jersey 2010 Financial Report and Accounts. In respect of the JTSF, the contributions paid during 2010 amounted to: £8.4 million (employer) and £3.0 million (participants) (i.e. a total of £11.4 million). The benefits paid out amounted to £14.2 million. This implies that in terms of current receipts/payments there were excess payments of £2.8 million so that any increase in the scheme's funds to meet increases in future liabilities would have to come from investment gains. This seems a somewhat uncomfortable position: especially where the recent reconstruction has not yet been finally agreed so that there is a risk that the States will be liable.

5.51 The changes made in the United Kingdom deal with:

(1) increasing the retirement age.

(2) moving from career end salary as the basis for a pension to average career salaries.

(3) changes to the rate of accrual of entitlement (i.e. how quickly a member can establish a right to a full pension).

(4) changes to early retirement arrangements (eg increasing the age from which policemen can retire on a full pension).

(5) changes to defined contribution from defined benefit schemes (i.e. to schemes which only pay what the contributions will buy)

5.52 These changes began in the United Kingdom in mid 2010 – the position is clouded by the fact that they have many different schemes whereas in the Island there are just two. In general the Island has been slow to match United Kingdom practice although it should be recalled that if the reconstructed arrangements for PECRs and JTSF can be sustained, they approximate to defined contribution arrangements for current members.

5.53 **KEY FINDING: Jersey has been slow to deal with the public sector pension time-bomb.**

5.54 **RECOMMENDATION: There should be greater urgency to deal with the issues relating to the pension funds and this should be led by the Treasurer who should produce a Report to the States Assembly by March 2012 setting how the liability will be managed and contained.**

5.55 With public sector salaries now ahead of private sector equivalents and the almost extinct nature of private sector final salary pension schemes, the absorption of a significant debt liability to bail-out the public sector employees should not be taken lightly.

5.56 The Tribal report mentioned later already demonstrates significant over-payment of employment packages in the public sector. This is a point highlighted by both the PAC and the C&AG in previous reviews.

5.57 The PAC Recommend that no action is taken on the transfer of liability until a comprehensive review of terms and conditions is undertaken with appropriate changes implemented. It is our view that intransigence on either side could lead to a collapse of the scheme as the deficit is too high for members to address without the charity of the taxpayer.

5.58 The meeting with the Acting Chief Executive touched briefly on the subject of reviewing public sector terms and conditions.

5.59 In the Tribal Terms & Conditions Review – September 2010 - it was noted, with the possible exception of the teaching profession, that some Jersey Public Sector salaries are considerably higher than London salaries (administrator +14%, Gardener +12%, Police Sergeant +35%, Prison Officer +30%, Fire Station Manager +21%).

5.60 Any acceptance of liability by the taxpayer in respect of the pension should be offset by a resetting of terms & conditions so that there is a neutral effect in terms of package. In other words the public sector need to pay for their pension fund on a true cost basis, with an opt-out option if they find the actual level of contributions unaffordable. This would require the closure of the current scheme and the creation of a new scheme.

5.61 Negotiations in this respect should adhere to the best interests of the Island rather than self interest.

5.62 In 1999, the then Establishment Committee lodged 'P143/1999, Public Employees Contribution Retirement Scheme: Proposal to Establish the Scheme Under a Trust Deed and Rules':

> ***"THE STATES are asked to decide whether they are of opinion -***
>
> *(a) to agree in principle that the Public Employees Contributory Retirement Scheme should be established as a Trust and administered under a Trust Deed and Rules, instead of the present Regulations;*
>
> *(b) to charge the Establishment Committee to prepare the necessary legislation to give effect to this proposal."*

5.63 Following a debate, the States carried the proposition. (see Appendix 1 for full proposition)

5.64 On 27th September 2011, the States Employment Board submitted 'R.117, Public Employees Contribution Retirement Scheme: Trust Status'. The report explained that trust status was no longer suitable for the in-principle decision of 1999 would not be implemented. (See Appendix 2 for full report)

> *"As a result of the further comprehensive advice that the SEB has received, the Board is now of the view that –*
>
> *1. The advantages claimed for a move from a statutory-based scheme to a private trust scheme within P.143/1999 no longer apply.*

2. *Any move to a private trust scheme might lead, either immediately or over time, to a loss of influence by the States without any commensurate reduction in responsibility or liability in real terms.*

3. *The pension arrangements are an important part of the basis on which States employees are employed and that it may, in effect, even were it otherwise desirable, be impossible for the States to fail to take into account any adverse occurrences within PECRS.*

4. *Accordingly, it would not be desirable to make any change in the status of PECRS at this time.*

5.65 The Committee notes with interest, item 2 above which relates to the requirement for the States to maintain its responsibilities in real terms.

5.66 This is an area previously reviewed by the PAC. There are no checks and balances that propositions passed by the States Assembly are enacted by the civil servants charged with carrying out their imposition. A proposition debated and passed by the States assembly 12 years ago was nullified simply by the publishing of a short report.

5.67 **KEY FINDING: A proposition was passed by the States in 1999 but never enacted. In 2011, R.117 advised that the proposition would not be enacted.**

5.68 **RECOMMENDATION: There should be a system of checks and balances to ensure that propositions debated and passed by the States are enacted. This issue has been raised in previous PAC Reports and ignored by the PPC.**

6. Financial Wealth of the Island

6.1 During 2010 a substantial amount was spent on capital projects from the Consolidated Fund (£68 million) – with the implication being that it was all for infrastructure projects. The detailed analysis of that total amount is set out in the table on pages 24 and 25 of the accounts booklet. Although the total amount of £68 million may seen substantial, it is distorted by the sum (£34million) spent on the Energy from Waste Plant.

6.2 The balance of capital expenditure amounts to £34 million which should be compared with the total amount of fixed assets held by the States. The most significant figures are:

	Cost £m	Depreciation	Net book value
Social housing (including land)	545	-27	518
Infrastructure (including land)	1,040	-3	1,037
Other structures	240	-13	227
	1,825	-43	1,782

6.3 The implication is that during 2010 the States spent an amount equal to only about 3-4% of the total book amount of its investment in infrastructure and social housing assets. If the distorting effect of the Energy from Waste plant is removed, the amount spent is equal to only about 2% of the total amount. What is more, this comparison does not take account of the fact that the total spending of £68 million includes expenditure on projects that would not normally be regarded as infrastructure projects such as:

Chief Minister's Department	£1.2m
Health– ICR project	£3.1m
Health– new CT scanner	£1.1m
Total	£5.4m

6.4 This analysis raises questions concerning the States' care for the Island's infrastructure. It is tempting when budgeting on an annual basis to keep within cash targets by restricting capital expenditure. Whilst this may not be harmful as a temporary expedient, in the longer term it results in degradation of infrastructure. There are suggestions that the backlog of investment in the Island's roads, sewers, sea defences, airport, hospital and social housing is a material amount.

6.5 The PAC considered what the level of capital expenditure should be to sustain the island's infrastructure in an acceptable condition and how that level of expenditure might best fit within the Medium Term Financial Strategy.

6.6 This raised questions about how the States' should ideally be financed, and what were the States responsibilities, which will be considered further below. However the question of whether maintenance of specific infrastructure is a central States responsibility funded by taxation, or a periphery duty which can be outsourced on a user pays basis must be examined first. The Council of Ministers should produce a Report within six months detailing the core responsibilities of Government and identifying non-core or peripheral activities that can be disconnected from the States.

6.7 **KEY FINDING: The States of Jersey are providing insufficient support for the maintenance of the Islands' infrastructure.**

6.8 **RECOMMENDATION: The level of financial support for the maintenance of the Islands' infrastructure must be significantly increased.**

6.9 When the Treasurer made a presentation to the press at the beginning of June 2011, the following message was conveyed;

- The States' current position is strong with no debt on the Balance Sheet.

- The States is taking steps to tackle the structural deficit and ensure sustainable finances.
- Proposals for Medium Term Financial Planning and strengthen financial management across the States – delivering better value for money.

6.10 There is no question that the States' balance sheet is relatively strong: particularly in comparison with the balance sheets of United Kingdom (UK) local authorities which would be expected to have substantial amounts of borrowing and substantial pension scheme debts. Certainly one would not expect a UK local authority to have a substantial strategic reserve.

6.11 However the PAC does not agree that there is no debt. The States have substantial debts due to PECRS and JTSF15 which could be regarded as tantamount to borrowing. Indeed, the balance due to PECRS is specifically constituted as a debt. The Financial Report and Accounts 2010 show that this liability amounted to £379million. In addition, the States do have a relatively small liability under finance leases which is shown in those accounts to be £14 million. This liability is, in substance, borrowing. In other words, the total amount of balances that in substance are equivalent to debt is £393 million at 31 December 2010.

6.12 There is a further point. Although the States may not have raised finance by direct borrowing, they have enabled other parties to borrow to acquire fixed assets for social use: i.e. they have arranged for proxy borrowing. Generally these arrangements are backed by some form of comfort or support provided by the States.

6.13 The States have issued letters of comfort in respect of loans made to housing trusts. The terms of these arrangements are described in the Accounts (Note 24 page 99 of the Accounts). The loans in question amounted to £151 million as at 31 December 2010. The effect of these arrangements is that the States would be obliged to provide financial support to the housing trusts in the event that they were unable to meet their commitments to the banks either in terms of interest payments or capital repayments. Such arrangements enable the States to say that they have not guaranteed the loans whilst banks are reassured that the loans can be made on the assumption of the financial backing of the States. In substance, this is an arrangement by which the

States enables social housing to be provided by means of borrowing by a proxy (i.e. a housing trust). This practice is intended to grow as on the transformation of the Housing Department into a trust, expenditure on new social housing by the new trust will not be treated as expenditure of the States but will presumably be financed in the same way as the existing housing trusts.

6.14 Similar issues appear to arise in respect of a guarantee of a loan to Jersey Water of £14.9 million. The balance sheet does not of course take any account of backlogs in capital maintenance and expenditure.

6.15 So how strong would one expect the States' balance sheet to be?

6.16 The island is not in the position of a UK local authority where, to a large extent levels of spending (especially in certain areas) are directed and limited by central government. In some areas, local authorities will be directed to increase their liabilities (e.g. the decreasing level to which the local authority pension schemes have been funded and thus pension liabilities have increased is effectively dictated by central government). In Jersey there is no fall-back position. In other words, there is no higher authority which can be expected to bailout a local authority which collapses.

6.17 Moreover, whilst the Island has the good fortune to be relatively prosperous, its economy is relatively small and imbalanced: i.e. its strength comes from a narrow source. If that source were for some reason to be undermined, then the ability of the States to maintain the income of the public sector and thus to continue to provide what are regarded as essential public services would quickly be called in question.

6.18 Certain of the key services on which the Island relies are provided by largely independent businesses which are, in the largest part, owned by the States. If for some reason one of these were to fail (e.g. if Jersey Telecom were to over-extend its investment programme), the States would be obliged to ensure that the service were maintained.

6.19 The strength of the States' balance sheet is important because it would be the principal source of the Island's resilience if it were to be faced with problems affecting its long-term economic performance or problems arising from critical service failure. The effect is that one would expect the States to maintain a strong balance sheet and monitor it closely.

6.20 There is no single correct answer to the question of how strong the balance sheet should be. The nature of the risks to the financial stability of the States determines that. What is appropriate strength will depend upon the judgement of the people responsible and upon their perception not only of the risks that are being faced but also likelihood that those risk will crystallise. It is also bound to depend upon a judgement of the States' capacity to encompass change: i.e. upon the period of time which would have to be allowed for the island to adjust to changed economic circumstances.

6.21 Financing the Island's infrastructure

One of the oddities of the States' current balance sheet is its counter-intuitive approach to long term funding. There is a respectable economic justification for borrowing to finance investment in infrastructure for its effect is to go some way towards charging the cash cost of acquiring the infrastructure to the future generations which will use the infrastructure rather than to the current generation which will only use it for a limited time. As it happens, most of the Island's infrastructure investment has been met from cash resources (with the exception of social housing acquired by housing trusts using loans supported by the States, as already explained). This can be (and is) justified on the grounds that it is a conservative approach to financing and is thus in keeping with the need for the Island to maintain the strength of the balance sheet.

6.22 On the other hand, the States' pension obligations to its employees are being met from future expenditure. In other words, in cash terms, the cost of those obligations is being met by generations which will not have the direct benefit of the services of the employees to whom the obligations are owed.

6.23 There may well be a case for borrowing to finance the increase in capital expenditure which sustaining the infrastructure probably requires. This could be undertaken directly or through proxies (e.g. transferring responsibility for sewers to Jersey Water or by separating harbours and the airport from the States by creating an independent company to manage them). There is also a case for borrowing to finance the necessary provision of social housing and the refurbishment of existing social housing stock, which is currently being financed by the sale of social housing. This has the effect of reducing the stock of social housing for rent and thus exacerbates the shortage of social housing stock.

6.24 But if this were to be considered, it would be necessary to re-consider the States' long held aversion to borrowing and to consider the conditions which should be fulfilled if substantial borrowing were to be considered. It might also be appropriate to consider the vehicles through which borrowing might be affected and its transparency. Should the States be aware of the total amount of such borrowing? If so, how might this be achieved if the borrowing were to be arranged through independent entities in positions similar to that of (say) Jersey Water?

6.25 Provision for borrowing should be made available with legislation reviewed and updated to allow borrowing if required. Types of borrowing and funding should be identified and assessed. The PAC believes that the Homebuy debacle should not be repeated. In this case the law was never changed to legally allow for shared equity – with potentially disastrous consequences. If private public partnerships or government bond issuance *may* be required in future the legal framework should be examined and updated *now* to avoid potentially costly delays.

6.26 **KEY FINDING: The Island may not be as financially secure as it purports to be and borrowing may be unavoidable in the future.**

6.27 **RECOMMENDATION: The Minister for Treasury and Resources must prepare legislation in the event that borrowing may be essential in the future.**

6.28 Employees

From the table set out in Note 5 to the accounts, one can calculate an average cost of employment per FTE: which in 2010 was £52,121 (i.e. £326.540 million for 6265 FTE). The equivalent average for previous years was as follows:

	Total remuneration £	FTEs	Average £
2010	326.540	6265[33]	52,121
2009	313.945	6265	50,111
2008	259.407	6157	42,132
2007	245.073	6169	39,726
2006	232.388	5888	39,468

6.29 The annual increases in the average costs per FTE are as follows:

	2010	2009	2008	2007
Annual % increase over Previous year	4.01	18.94	6.05	6.15

6.30 The implication is that remuneration in the island's public sector has been rising more quickly than remuneration in the private sector (and more quickly than in the financial sector) and that the remuneration of staff in the public sector has been insulated from the effects of recent economic difficulty.

6.31 Quite apart from special exercises such as the Comprehensive Spending Review, this raises questions about the effectiveness of management within the States; for the disparity appears to have been evident before the recent economic difficulty.

6.32 The PAC is extremely concerned with the total cost of remuneration packages in 2010. Even though the quantity of staff employed had been stabilized, costs of staff escalated far above the cost of living and appear to be beyond control giving some credence to the public perception that States workers are all overpaid.

6.33 The Committee is aware that this area is being addressed and it further recognises that part of the problem lies within the increment system that has been inherent in the States pay structure for many years. Some employees doubling their remuneration simply by being in post for a period of time. In October 2011, negotiations are known to be well in hand between the States Employment Board and staff representatives to agree strategies to control states spending on staff. A complete root and branch review of Terms and Conditions, including pensions, is being undertaken.

[33] States of Jersey Financial Report and Accounts P84

6.34 The Committee recognises the good work and sensible approach to these problems being taken at this stage of the negotiations by both employer and employee representatives. The remit of this review is to examine the States of Jersey Financial Report and Accounts 2010. Therefore no comment is going to be made in regard to the specifics of the work being undertaken in 2011 in relation to the Terms and Conditions.

6.35 **KEY FINDING: The Committee recognises the good work being done in the area of Terms and Conditions.**

6.36 **RECOMMENDATION: The Public Accounts Committee, as constituted in 2012, should examine progress with remuneration when it undertakes the review of the States of Jersey Financial Report and Accounts 2011.**

6.37 Total Severance Payments

The table on page 133 of the Accounts shows that total severance payments amounted to £7.521 million. This figure includes the amount of the voluntary redundancy scheme approved under P64/2010 (see page 7 of the Annex to the Accounts).

6.38 This raises two questions;

1. What were the other severance payments paid during the year amounting to £1.521 million?

2. Why the urgency to pay off staff when a delay would save the taxpayer £2,458,021.

6.39 It is questionable whether a private sector firm would have been so generous to it's employees. The cost differential between the old VR scheme and the new one for the VR's taken at the end of 2010. These calculations have been made on the basis of the VR's determined in respect of the £6 million funding provided from the Article 11(8) P64/2010. The payments in 2010 were made on the basis of the original scheme and a new scheme has been agreed by SEB and is effective from 1st January 2011. An equivalent cost of the 2010 redundancies calculated on the new scheme is shown as 2011 terms.

1. £6,083,594 (2010 terms)
2. £3,625,573 (2011 terms)

6.40 The new terms are as follows:

<u>From 2011 to 2012 inclusive</u>

(i.e. during the comprehensive spending review programme):

Voluntary Redundancy:

Four weeks' pay per completed year of service capped at 18 months' pay.

Compulsory Redundancy:

Three weeks' pay per completed year of service capped at 12 months' pay.

<u>From 2013</u>

Voluntary Redundancy:

Three weeks' pay per completed year of service capped at 18 months' pay.

Compulsory Redundancy:

Three weeks' pay per completed year of service capped at 12 months' pay.

In all of the above, the maximum salary for redundancy calculation purposes will be capped at Civil Service grade 15/3, currently £83,018.

6.41 There appeared no urgency to undertake the redundancy programme and it is concerning that the move could be construed as favours for fellow employees.

6.42 However, the employers are represented by the States Employment Board (SEB). The constitution of this body is defined within the Employment of States of Jersey Employees (Jersey) Law 2005 which states:

5 Membership of States Employment Board

(1) The States Employment Board shall be constituted by –

(a) the Chief Minister, or another Minister who is nominated by the Chief Minister to be a member of the Board in his or her place;

(b) 2 other persons, each of whom –

(i) is a Minister or an Assistant Minister, and

(ii) is appointed in writing by the Chief Minister to be a member of the Board; and

(c) 2 elected members of the States, each of whom –

(i) is neither a Minister nor an Assistant Minister, and

(ii) is elected by the States to be a member of the Board.

(2) The Chief Minister or, if the Chief Minister nominates a person under paragraph (1) to be a member of the Board in his or her place, that person, shall be the Chairman of the States Employment Board.

6.43 The Committee understands that the Chief Executive of the States of Jersey is present during the meetings.

6.44 This leaves little involvement of States employees within the SEB management process, other than Elected Members who have not been eligible for the voluntary redundancy or pensions. This suggests that the accusation of 'favours for fellow employees' is a misconstrued perception. However, membership from completely outside the "family" of States employees is missing and inclusion of independent members would prevent the current misconceptions.

6.45 **KEY FINDING: The generous voluntary redundancy programme implemented in 2010 may not have been the best use of taxpayer's funds given the revision of terms in 2011.**

6.46 **RECOMMENDATION: The States Employment Board should have external independent members to ensure transparency of the decision making process.**

6.47 Final Comment

This is the final Report of the current Public Accounts Committee which will cease to exist when the new Assembly is sworn in on the 14th November, 2011. During the past three years we have identified many areas within the States that require attention. Some of these deficiencies were a direct result of the move to Ministerial Government, some as a result of unforeseen consequences of changes in legislation or procedures, and some through poor or undefined management.

6.48 The PAC would like to thank all those that gave evidence, contributed to our numerous question requests, and openly discussed issues with us. It is in everyone's interest to find solutions for the issues that we raise and we hope that no one will take our reports as personal criticism.

6.49 This Report will be passed to the new Public Accounts Committee and we wish them every success in making Government more efficient and shedding light on areas of concern.

6.50 Finally we would like to thank the support officers that have worked with us during the past three years – Anna Heuston, Mel Pardoe, and Mick Robbins - for their hard work, dedication, and ability to deal with a Chairman who would have about eight plates spinning at any one time covering many diverse issues of PAC interest.

7. Terms of Reference

PUBLIC ACCOUNTS COMMITTEE

FINANCIAL REPORT & ACCOUNTS 2010 REVIEW
TERMS OF REFERENCE

1. To review the States of Jersey Financial Report and Accounts 2010

2. In accordance with paragraph 132(1)(a)(i) of the Standing Orders of the States of Jersey, to receive a report from the Comptroller and Auditor General on the results of the audit of the Annual Financial Statement of the States, and to report to the States upon any significant issues arising.

3. To ensure that the issues identified in the Public Accounts Committee's reviews of previous States Accounts have been addressed.

4. To examine any further issues relating to the Financial Report and Accounts 2010 which the Committee considers relevant.

8. Committee Membership

The current membership of the Public Accounts Committee (as at the date of the presentation of this report) comprises:

States Members

Senator B.E Shenton (Chairman)

Senator A. Breckon (Vice Chairman)

Senator J. Perchard

Deputy J. Le Fondré

Independent Members

Mr A. Fearn

Mr M. Magee

Mr S. Haigh

Officer Support: Mick Robbins

9. The Role of the Public Accounts Committee

The primary function of the Public Accounts Committee is defined in Standing Orders[34] to review reports by the Comptroller and Auditor General and to report to the States upon any significant issues arising from those reports regarding :-

- The audit of the Annual Accounts of the States of Jersey
- Investigations into the economy, efficiency and effectiveness achieved in the use of resources by the States, States funded bodies, independently audited States bodies (apart from those that are companies owned and controlled by the States), and States aided independent bodies
- The adequacy of corporate governance arrangements within the States, States funded bodies, independently audited States bodies, and States aided independent bodies,
- and to assess whether public funds have been applied for the purpose intended and whether extravagance and waste are being eradicated and sound financial practices applied throughout the administration of the States.

The Public Accounts Committee may also examine issues, other than those arising from the reports of the Comptroller and Auditor General.

The Public Accounts Committee represents a specialised area of scrutiny. Scrutiny examines policy whereas the Public Accounts Committee examines the use of States' resources in the furtherance of those policies. Consequently initial enquiries are made of Chief Officers rather than Ministers.

[34] Standing Orders of the States of Jersey 1st January 2006, No. 132.

10. Appendix 1

PUBLIC EMPLOYEES CONTRIBUTORY RETIREMENT SCHEME: PROPOSAL TO ESTABLISH THE SCHEME UNDER A TRUST DEED AND RULES

PROPOSITION

THE STATES are asked to decide whether they are of opinion -

(a) to agree in principle that the Public Employees Contributory Retirement Scheme should be established as a Trust and administered under a Trust Deed and Rules, instead of the present Regulations;

(b) to charge the Establishment Committee to prepare the necessary legislation to give effect to this proposal.

ESTABLISHMENT COMMITTEE

NOTES: This proposition is supported by -

1. the Finance and Economics Committee;
2. the Committee of Management of the Public Employees Contributory Retirement Scheme;
3. the Public Employees Pension Scheme Joint Negotiating Group.

REPORT

Background

1. The Public Employees Contributory Retirement Scheme (“the Scheme”) came into effect from 1st January 1968 under the Public Employees (Retirement) (Jersey) Law 1967 (L.11/67) (“the 1967 Law”) and the Public Employees (Contributory Retirement Scheme) (Jersey) Regulations 1967 (R & O 5010). It was set up to replace various non-contributory pension arrangements for public employees, and was administered by the States Treasury.

2. Until the late 1980s, the States Treasury reported in that respect to the Finance and Economics Committee, which was the Committee responsible for investment of the Scheme’s assets. The Establishment Committee was also involved, in two ways: firstly, it acted as principal employer on behalf of the States, and secondly it was responsible for matters which in most other schemes would be dealt with by trustees.

3. Significant changes were made to the Scheme with effect from 1st January 1988 by way of amendments to the existing legislation and promulgation of the following additional Regulations -

   the Public Employees (Contributory Retirement Scheme) (General) (Jersey) Regulations 1989 (R & O 7956);

   the Public Employees (Contributory Retirement Scheme) (Existing Members) (Jersey) Regulations 1989 (R & O 7954);

   the Public Employees (Contributory Retirement Scheme) (New Members) (Jersey) Regulations 1989 (R & O 7955).

4. Designed primarily to implement modifications to the Scheme’s structure, funding and benefit provisions, these changes also introduced a requirement for the Scheme to be run by a Committee of Management. The States Treasury continued to administer the Scheme but reported to the Committee of Management. The investment of

the Scheme's assets became the responsibility of the Committee of Management, although the Finance and Economics Committee retained a role in approving investment managers and strategy. The Establishment Committee continued to act as principal employer but responsibility for other matters was passed to the Committee of Management.

5. Subsequently a further set of Regulations entitled the Public Employees (Contributory Retirement Scheme) (Former Hospital Scheme) (Jersey) Regulations 1992 (R & O 8443) were promulgated as part of the process of transferring the assets and liabilities of a pension arrangement for medical and auxiliary staff to the Scheme. The current legislative structure of the Scheme is therefore complex due to the presence of five sets of Regulations in addition to the 1967 Law.

Membership of the Committee of Management

6. The current Committee of Management is comprised of seven member representatives and seven employer representatives, with an independent Chairman. They are all appointed by the States on the recommendation of the Establishment Committee.

7. The employer representatives are nominated by the Finance and Economics Committee and the Establishment Committee.

8. The member representatives are nominated by the Public Employees Pension Scheme Joint Negotiating Group. This was set up in 1976 at the request of the Establishment Committee as a co-ordinating panel of union and staff associations to represent the interests of all public employees in negotiations with the Establishment Committee concerning pension provisions.

9. Legal advice concerning the status of the Committee of Management confirmed that in effect it is a Board of Trustees holding the Scheme's assets as a trust fund administered as set out in the Regulations.

Formally establishing a Trust Deed and Rules

10. Further consideration has now been given to the status of the Committee of Management, and it has been concluded that it would be beneficial to establish the Scheme formally as a Trust, with no change to the Scheme's commitments, operation, funding or benefits save that these would become administered under a Trust Deed and Rules rather than the present Regulations. The parties that came to this conclusion were the Committee of Management, Establishment Committee, Finance and Economics Committee and the Joint Negotiating Group, supported by the Scheme's legal advisers and actuaries. Such a change would be in line with modern best practice for large pension schemes. Appropriate high level safeguards and the proper input of the States would be retained.

11. One of the substantial advantages would be removal of the need to compete with other States Committee projects for law drafting resources. The existing legislative process is a less than ideal structure within which to administer the Scheme. Modifying the structure would speed up the process of implementing agreed changes to the Scheme's provisions as the need arises and greatly improve the flexibility of its administration.

12. The Establishment Committee therefore intends to promote amendments of the 1967 Law which will enable the Scheme to be established as a Trust and administered under a Trust Deed and Rules.

Key principles

13. In the following paragraphs of this report some key principles are outlined which would form the basis of establishing the Scheme under a Trust Deed and Rules.

14. The Committee of Management would, as individuals, be appointed as the initial trustees. The enabling Law (and the Trust Deed and Rules) would allow for trusteeship either through individuals or through a trust corporation, with the power to appoint any such trustees or trustee being retained by the States in the same manner as at present for the appointment of members of the Committee of Management.

15. Under the proposal the Trusts (Jersey) Law 1984 (L.11/84) ("the Trusts Law") would apply. This would bring many advantages. For example, currently the Regulations specify that the States shall indemnify each member of the Committee of Management against all personal liabilities incurred by him in the management and administration of the Scheme, other than those incurred by his own wilful misconduct. It is intended that the

Trustees would continue to be indemnified. However, having regard to Article 26(9) of the Trusts Law which states that "nothing on the terms of a trust shall relieve, release or exonerate a trustee from liability for breach of trust arising from his own fraud, wilful misconduct or gross negligence", it will be necessary to refer to fraud and gross negligence, as well as wilful misconduct, as being excluded from the indemnity. This will tend to emphasise the responsibilities of those discharging the role of Trustee. In addition, the Trustees will be able to draw upon a large body of authority as to the role and responsibility of pension fund trustees.

16. In order that the Scheme's life shall continue to be unlimited, it is the intention that it will be established under an *indefinite* Trust. However, under Article 11 of the Trusts Law, the maximum duration of a Trust is 100 years. To enable the trust-based Scheme to exist indefinitely it will be necessary for the legislation enabling its establishment to provide that, as is the case now for charitable trusts, the hundred year limitation does not apply to the Scheme.

17. As at present the Establishment Committee would carry out all the functions of the principal employer on behalf of the States. In particular, the Trustees and Establishment Committee would agree any necessary changes to the Trust Deed and Rules. The Establishment Committee would keep the States informed of such changes and any States Member could request that they are debated.

18. The Trustees would be fully responsible for the investment strategy and appointment of the Scheme's investment managers. This is in line with best practice for pension schemes. The Finance and Economics Committee would no longer have any direct involvement with the Scheme's investments.

19. Further details of the proposal will be provided at the time of promoting the amendments of the 1967 Law. The Committee plans to present the amendments to the States during 2000 (they are included in the States' Legislation Programme for that year) and set up the Trust Deed and Rules for 2001.

11. Appendix 2

PUBLIC EMPLOYEES CONTRIBUTORY RETIREMENT SCHEME:

TRUST STATUS

Presented to the States on 27th September 2011
by the States Employment Board
STATES GREFFE
R.117/2011
2

REPORT
The States Employment Board wishes to inform States Members of a decision of 6th September 2011 relating to the Public Employees Contributory Retirement Scheme (PECRS).
On 28th September 1999, Proposition P.143/1999 – Public Employees Contributory Retirement Scheme: proposal to establish the scheme under a trust deed and rules – was lodged *au Greffe* by the Establishment Committee of the day for debate by the States Assembly. In that Proposition, the States were asked to agree in principle that PECRS should cease to be a statutory scheme and instead should be established as a Trust and administered under a Trust Deed and Rules. The Establishment Committee was charged to prepare the necessary legislation. That Committee acted as principal employer on behalf of the States. The principal reasons advanced in P.143/1999 for the conversion from a statutory scheme to a trust were that –

1. such a move constituted “modern best practice for large pension schemes”;
2. such a move would remove the need to compete for law drafting resources in changing the provisions of the scheme from time to time and, speed up drafting changes to the scheme as the need arose and greatly improve the flexibility of its administration;
3. the Committee of Management or Trustees would be subject to the provisions of the Trusts (Jersey) Law 1984.

P.143/1999 was adopted by the States Assembly on 12th October 1999.
The Proposition expressed the intention that the scheme should be formally established as a trust “with no changes to the scheme’s commitments, operation, funding or benefits, save that these would become administered under a trust deed and rules rather than the present regulations”.
During the considerable time that has passed since that resolution and today, substantial work has been undertaken pursuant to that decision of the States Assembly.
During that time, a draft Law and a trust instrument under which PECRS would cease to have a statutory status and be reconstituted as a trust was prepared. Comprehensive further legal advice was taken and advice was taken from pension specialists, the Comptroller and Auditor General and the Treasurer of the States.
During that period, it should be noted many amendments have been made to PECRS,

and it is clear that notwithstanding one of the reasons advanced in support of P.143/1999, there is no difficulty in fact in making alterations to PECRS in a timely manner.
The States Employment Board has further been advised that many public sector schemes are statute-based and that so far as is not inconsistent with the instruments under which it is based, the Committee of Management are Trustees and the general law of trusts applies to PECRS.
R.117/2011
3
Members will be aware of significant changes in circumstances within which pension funds are operating. For example, it is now known that the Stock Market collapse has led to significant shortfalls in funding levels for most UK pension sector schemes. Whilst we do not yet have the formal outcome of the valuation of PECRS or the Jersey Teachers' Superannuation Fund, we know that investment returns have been adversely affected by the falls in the Stock Market in 2007 and 2008 in particular.
Furthermore, a formal inquiry into the future of the UK public sector schemes is under way and this is also a significant new development. The UK inquiry does in fact give rise to potential for change to the Jersey schemes, particularly if one of our objectives is to stay close to the UK pension club requirements and thereby facilitate the transfer of health and social care staff and teaching staff between the UK and Jersey.
As a result of the further comprehensive advice that the SEB has received, the Board is now of the view that –

1. The advantages claimed for a move from a statutory-based scheme to a private trust scheme within P.143/1999 no longer apply.
2. Any move to a private trust scheme might lead, either immediately or over time, to a loss of influence by the States without any commensurate reduction in responsibility or liability in real terms.
3. The pension arrangements are an important part of the basis on which States employees are employed and that it may, in effect, even were it otherwise desirable, be impossible for the States to fail to take into account any adverse occurrences within PECRS.
4. Accordingly, it would not be desirable to make any change in the status of PECRS at this time.

In the light of all of the advice that it has received and in the current economic situation, the States Employment Board after very careful consideration has accordingly decided not to implement the States' in-principle decision of 1999 and will be doing no further work on this matter.
There are no financial or manpower implications arising from this Report

12. Appendix 3

The ten-point plan referred to in paragraph 5.13 is taken from Appendix 1 of the PECRS Annual Report 2010:

The framework agreed between the Policy and Resources Committee and the Committee of Management for dealing with the pre-1987 debt was documented in a ten-point agreement approved by Act of the Policy and Resources Committee dated 20 November 2003. The provisions of the agreement, which have subsequently been reflected in Regulations approved by the States of Jersey on 27 September 2005, enable us to treat the pre-1987 debt as an asset of the Scheme for valuation purposes. The text of the agreement is reproduced below.

1. *The States confirms responsibility for the Pre-1987 Debt of £192.1 million as at 31 December 2001 and for its servicing and repayment with effect from that date on the basis that neither the existence of any part of the outstanding Debt nor the agreed method of servicing and repayment shall adversely affect the benefits or contribution rates of any person who has at any time become a member of the Scheme.*
2. *At the start of the servicing and repayment period, calculated to be 82 years with effect from 1 January 2002, the Employers' Contribution rate will be increased by 0.44% to the equivalent of 15.6%. These contributions will be split into 2 parts, namely a contribution rate of 13.6% of annual pensionable salary and an annual debt repayment. The Employer's Contribution rate will revert to 15.16% after repayment in full of the Debt.*
3. *During the repayment period the annual Debt repayment will comprise a sum initially equivalent to 2% of the Employers' total pensionable payroll, re-expressed as a cash amount and increasing each year in line with the average pay increase of Scheme members.*
4. *A statement of the outstanding debt as certified by the Actuary to the Scheme is to be included each year as a note in the States Accounts.*
5. *In the event of any proposed discontinuance of the Scheme, repayment and servicing of the outstanding Debt shall first be rescheduled by the parties on the advice of the Actuary to ensure that paragraph (1) above ("Point 1") continues to be fulfilled.*
6. *For each valuation the States Auditor shall confirm the ability of the States to pay off the Debt outstanding at that date.*
7. *If any decision or event causes the Actuary at the time of a valuation to be unable to continue acceptance of such servicing and repayment of the Debt as an asset of the Scheme, there shall be renegotiation in order to restore such acceptability.*
8. *In the event of a surplus being revealed by an Actuarial Valuation, negotiations for its disposal shall include consideration of using the employers' share to reduce or pay off the Debt.*
9. *As and when the financial position of the States improves there shall be consideration of accelerating or completing repayment of the Debt.*
10. *The recent capital payment by JTL of £14.3m (plus interest) reduced the £192.1m total referred to in (1) by £14.3m and if any other capital payments are similarly made by other Admitted Bodies these shall similarly be taken into account."*

13. Appendix 4

In response to the receipt of a draft copy of the report, the Treasurer made the following observations:

As you will be aware, the long term affordability and sustainability of public sector pensions is being considered in the UK following the publication of the Hutton Report and it is important that the States of Jersey also considers the long term sustainability of its owns public sector pension schemes. It is equally important that the current position is portrayed accurately and in this respect I have the following comments that may add to your draft report and address some factual inaccuracies in the current draft.

Pension Funds are managed for the long term and it is possible to address funding needs over the long term. It is therefore appropriate for the realisation of the pre 87 PECRS debt to be addressed over the long term.

Longevity is increasing which is putting additional pressure on all pension schemes. The public sector pension schemes administered by the States of Jersey are no exception and the liabilities of the scheme are rising due to people living longer. However, a number of other factors including the level of long term interest rates also impact on the level of liabilities which are calculated independently by the Scheme Actuary.

On an actuarial valuation basis the scheme deficit at the last actuarial valuation in 2007 was £63.2 million. This is an independent assessment of the scheme funding position by the Scheme Actuary and it is this that is required to be stated in the PECRS annual accounts. It is the actuarial valuation that is used to assess the long term funding position of the scheme.

The States of Jersey is required to calculate the scheme position on an accounting basis known as Financial Reporting Standard 17 (FRS17). This is calculated on a different basis and is not used for the purpose of establishing the long term affordability or sustainability of the scheme and it would be wrong to use it in that way. The FRS 17 calculation is required to be included within a note to the States of Jersey Accounts under proper accounting practices. Whilst the deficit figure is higher under FRS 17 (£526 million) this is not used to assess the long term affordability of the scheme or any instigation of the default position involving a reduction in future increases to pensions.

Public services in Jersey rely on attracting staff from the UK for some specialist roles particularly in health and education. It is important for the provision of key public services on the Island that the public sector pension schemes offered are part of the Public Sector Transfer Club so as to facilitate an easy transfer of staff to and from the UK. A Technical Working Group has been established comprising of representatives from the Committee of Management and officers from the States of Jersey to develop options for further consideration with the aim of ensuring the long term sustainability and affordability of the public sector pension schemes. This will include consideration of the sharing of risks and costs between the employer and employee.

The pre-2006 debt position of the Jersey Teachers Superannuation Fund is being taken forward by the States Treasury and there are proposals being developed regarding how this will be dealt with over the long term.

Since the summer the Treasury have been discussing with the Committee of Management how the long term sustainability and affordability of PECRS can be achieved. This has resulted in the establishment of the Technical Working Group which will develop options for further consideration. The PECRS deficit at the last actuarial valuation in 2007 was £63.2 million and over the intervening period investment returns and changes to other underlying assumptions will have impacted on the actuarial valuation position. Until the Scheme Actuary has completed the 2010 actuarial valuation the net impact of these changes will not be known.

The estimated accrued benefits shortfall quoted by AON Hewitt in 2009 relates to valuing the scheme on a discontinuance basis. There are no plans to discontinue PECRS. Indeed the Technical Working Group are working on developing options for further consideration that will ensure the long term sustainability and affordability of the scheme. On a continuation basis the same AON Hewitt report in 2009 values the scheme deficit at £63.2 million as at 31 December 2007.

The Independent Actuary is required to estimate future long term investment returns on the basis of the investment strategy adopted. Whilst stock markets have seen rises and falls in recent years the Independent Actuary is required to consider long term investment returns in calculating the actuarial valuation.

The figures shown in the States of Jersey accounts are produced on an FRS17 basis and are not used to assess the long term sustainability and affordability of the scheme

A Technical Working Group has recently been established to bring forward proposals on changes to the scheme for further consideration. This will include developing options that will provide clarity over future arrangements with regard to contributions into the scheme and the sharing of costs, risks and benefits between the employer and the employee. In doing this the Technical Working Group will take into account R117 Public Employees Contributory Retirement Scheme Trust Status presented to the States on 27th September2011. The Technical Working Group will also develop options that seek to ensure pension scheme governance arrangements meet best practice.

The Technical Working Group will also develop options that seek to ensure pension scheme governance arrangements meet best practice. The Treasurer of the States is a member of the Technical Working Group and will be considering the interests of the taxpayer in the developing of options for further discussion on the long term sustainability and affordability of the scheme.

An actuarial valuation as at 31st December 2010 is currently being calculated by the Independent Scheme Actuary. This is being produced in line with best practice which is for triennial actuarial valuations.

The Hutton Report in the UK has made a number recommendations regarding public sector pension provision. However, there has been no suggestion that the UK public sector should move from defined benefit to defined contribution pension schemes.

The Technical Working Group will develop options for further consideration that aim to ensure public sector pension schemes are affordable and sustainable for the long term.

Public services in Jersey rely on attracting staff from the UK for some specialist roles particularly in health and education. There is evidence that it is proving difficult to attract nurses due to the level of salaries currently offered.

In order to continue to attract key workers from the UK and remain in the UK Public Sector Transfer Club it is necessary for public sector pension scheme to remain comparable to their UK equivalent. The Technical Working Group will have regard to the outcomes of the Hutton Report in providing options for changes to the scheme that will continue to facilitate movement of staff to and from the UK.

The publication of R117 Public Employees Contribution Retirement Scheme: Trust Status was completed in accordance with the appropriate governance arrangements of the States.