HM Treasury

Public Expenditure System (PES)

Secretariat 0207 270 6503

PES (2013) 07

2 December 2013

DISCOUNT RATES FOR POST-EMPLOYMENT BENEFITS AND GENERAL PROVISIONS: ANNOUNCEMENT OF RATES

Summary	Notification of the discount rates to be used in valuing post employment benefits liabilities and general provisions as at 31 March 2014, and in preparing the Supplementary Estimate in 2013-14 and Main Estimate for 2014-15.
Action or Information	Action
Deadline	First deadline is 15 January 2014 for Departments to make final adjustments on OSCAR for their Supplementary Estimates for 2013-14. Second indicative deadline is March 2014 for departments to submit data on OSCAR for inclusion in Main Estimates on a pre-budget basis.
Expiry of paper	On issue of revised discount rates in early December 2014

Background

1. The post employment benefit discount rate is used for two main purposes in financial reporting:

- **Unfunded public service pensions schemes** - valuing pension scheme liabilities, calculating the interest costs on the stock of pension scheme liabilities (the equivalent of unwinding the discount as existing liabilities roll forward one year); and calculating the current service cost (the cost of accruing liabilities).

- **Early departure provisions** - valuing early departure provisions and unwinding the discount on those provisions.

2. The general provisions discount rates are used to discount future cash flows related to provisions recognised in accordance with IAS 37.

3. This paper announces the change in these discount rates from 31 March 2014.

New rates to be applied as at 31 March 2014

Post-employment benefits

4. The discount rate for post employment benefits will change from 2.35 percent real to **1.80 percent** real with effect from 31 March 2014.

5. The appropriate interest rate to be used in assessing interest costs of scheme liabilities for 2014-15 is **4.35 percent** (see Annex A: *Financial assumptions based on market conditions as at 30 November 2013* for a list of all necessary figures and a comparison with prior year)

Superannuation Contribution Adjusted for Past Experience (SCAPE) and other discount rates

6. Various arrangements are in place for setting employer pension contributions (or ASLCs) in unfunded schemes that require a discount rate. Most of these arrangements are based on the SCAPE methodology that uses a fixed real discount rate. These arrangements are unaffected by the discount rate used for IAS 19 purposes. Schemes and their actuaries should continue to use existing arrangements.

Local Authorities

7. This guidance does not apply directly to local authority schemes and the unfunded liabilities of police and fire authorities. Those schemes should follow guidance provided by CIPFA.

Funded schemes

8. The application of a discount rate based on returns from AA corporate bonds at 30 November each year will not apply to funded schemes within central government. In accordance with IAS 19, they should use a discount rate based on returns from AA corporate bonds at 31 March each year (or their financial year-end if different).

General provisions

9. There are three rates provided for general provisions:

Short-term rate: A real discount rate to be applied to the cash flows of general provisions in a time boundary of between 0 and up to and including 5 years from the Statement of Financial Position date.

Medium-term rate: A real discount rate to be applied to the cash flows of general provisions in a time boundary of after 5 and up to and including 10 years from the Statement of Financial Position date.

Long-term rate: A real discount rate to be applied to the cash flows of general provisions in a time boundary exceeding 10 years from the Statement of Financial Position date.

10. The real discount rates to be applied at 31 March 2014 to determine the net present values of provisions are[1]:

Rate	Real rate
Short-term	-1.90%
Medium-term	-0.65%
Long-term	2.20%

11. The change in discount rates could result in non-cash negative AME arising from interest income. In accordance with the Consolidated Budgeting Guidance this income can only be used for expenditure relating to provisions or for depreciation of capital assets that have been donated. It cannot be used to fund genuine AME cash expenditure.[2]

[1] Note that the FReM requires that entities only use the real discount rate set by HM Treasury where cash flows related to provisions are expressed in current prices, i.e. cash flows are not uplifted for expected future inflation. Where entities express cash flows related to provisions in nominal prices, the FReM does not mandate either the nominal discount rate or the inflation rate to be used to express cash flows in nominal prices. Where entities do express cash flows related to provisions in nominal prices and cash flows are adjusted in accordance with the expected level of Retail Prices Index (RPI) inflation we recommend the following nominal discount rates and inflation adjustments.

Rate	Nominal rate	Inflation rate
Short-term	0.70%	2.64%
Medium-term	2.35.%	2.99%
Long-term	5.95%	3.67%

[2] Certain regulators have a derogation from the standard budgeting guidance which allows them to score the creation and movement of provisions in DEL rather than AME. These entities will need to ensure that they have sufficient DEL to cover the budgetary impact of any increase in provision balances. If the changes in rates leads to a decrease in provision balances these entities should note that the subsequent DEL income is not permitted to be used to cover additional expenditure in DEL other than that relating to

Timetable

12. Full details of dates and deadlines can be found in the Integrated Financial Information and Monitoring Timetable on the GSI:

http://www.coins.gsi.gov.uk/coins/timetable.html

You will be informed if dates change and the integrated timetable will be amended accordingly.

General

14. PES papers can be accessed online at the Public Spending link on the OSCAR homepage http://www.coins.gsi.gov.uk/coins/pespapers.html. The PES secretariat on 020 7270 6503 can supply further information on PES papers.

Annex A: ***Financial assumptions based on market conditions as at 30 November 2013 related to post employment benefit discount rate***

Market conditions as at	**30 Nov 2013**	**30 Nov 2012**
Nominal discount rate	4.35%	4.10%
Rate of RPI inflation	3.50%	2.70%
Rate of CPI inflation	2.50%	1.70%
Discount rate net of CPI	1.80%	2.35%

provisions or for depreciation of donated capital assets. It cannot be used to fund genuine DEL cash expenditure.