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pay, pensions and employment solutions

The Local Government Pensions Committee
Secretary: Mike Walker

CIRCULAR

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No. 188 – JULY 2006
NEW LOOK LGPS

Purpose of this Circular

1. This Circular has primarily been issued to let authorities know that a Working Party has been set up by the Local Government Pensions Committee to consider the possible options for a new look LGPS in England and Wales, as outlined in the DCLG consultation paper of 30 June 2006. It is hoped that during week beginning 7 August 2006 the Working Party will prepare information for distribution to authorities in England and Wales which will assist authorities in making a response to the DCLG consultation paper.

2. The Circular also contains new contact details for the LGPC Secretariat.

Background

3. As authorities will be aware, the LGPS Regulations in England and Wales were amended in April 2006 to reflect changes to the HMRC rules governing pension schemes and to remove the 85 year rule from 1 October 2006.

4. Discussions continued between the employers and the unions over extended protection from the removal of the 85 year rule.

5. In order to make progress, the union and employer sides confirmed that they would not object to the level of extended protection that the DCLG consulted upon in the draft amendment regulations issued on 26 May 2006[1] i.e.

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Managing Director Jan Parkinson

[1] The closure date for comments on the draft LGPS (Amendment) (No. 2) Regulations 2006 was 3 July 2006.

- an additional 18 months protection to 31 March 2008 for all **existing scheme members** at 30 September 2006
- to extend full transitional protection to 31 March 2016 for those **existing scheme members** at 30 September 2006 who will be 60 or over and meet the 85 year rule by 31 March 2016 i.e. this extends protection to existing members within 9.5 years of retirement rather than 6.5 years as presently applies
- to provide tapered transitional protection for those **existing scheme members** at 30 September 2006 who will be 60 or over and meet the 85-year rule between 1 April 2016 and 31 March 2020 i.e. full protection for service to 31 March 2008, but tapered protection for service between 1 April 2008 and 31 March 2020. The date of 2020 ties in with the increase in the state retirement age for women which increases to 65 in 2020

6. The unions have not abandoned their desire to attain full protection for existing members and have lodged a judicial review to challenge the Government's view that the 85 year rule would breach the age discrimination legislation. This is not likely to be heard before the Autumn.

A new-look LGPS in England and Wales

7. The progress made on extended protections from the removal of the 85 year rule in England and Wales has allowed the DCLG to start the process of designing a new look LGPS for April 2008.

8. The DCLG issued a consultation paper to all stakeholders on 30 June 2006 which set out possible options for a new look LGPS.

9. The consultation paper of 30 June 2006 starts by working out a benchmark cost for the Scheme.

Cost of present Scheme before removal of the 85 year rule and before the change to allow commutation	22.2% (19.4%)
Cost of present Scheme after removal of the 85 year rule and after the change to allow commutation	20.0% (17.6%)
Government commitment to permit up to 50% of "savings" to be recycled (less 0.2% for cost of additional protections and cost of revocation of April 2005 changes)	
Thus, benchmark cost for new look LGPS is	**20.9% (18.3%)**

10. Having arrived at a benchmark cost, the consultation paper then offers five possible options for a new look LGPS.

Type of Scheme	**Core structure**	**Increase to 3 x salary death benefit**	**Introduction of cohabitee's pension**	**Introduction of two tier ill health retirement**	**Total cost**
A: Updated current final salary scheme (1/80th accrual plus 3/80ths lump sum) with RPI revaluation after leaving	20.0% (17.6%)	0.3% (0.2%)	0.2% (0.2%)	-1.0% (-0.7%)	**19.4% (17.3%)**
B: New 1/60th final salary scheme (and lump sum available by commutation) with RPI revaluation after leaving.	21.5% (18.9%)	0.3% (0.2%)	0.3% (0.2%)	-1.1% (-0.8%)	**20.9% (18.6%)**
C1: CARE scheme with 1.85% accrual and RPI revaluation both during employment and after leaving (with lump sum available by commutation)	21.2% (18.3%)	0.3% (0.2%)	0.3% (0.2%)	-1.1% (-1.0%)	**20.6% (17.7%)**
C2: CARE scheme with 1.65% accrual and RPI + 1.5% revaluation during employment and RPI revaluation after leaving	21.5% (18.9%)	0.3% (0.2%)	0.3% (0.2%)	-1.1% (-0.8%)	**20.5% (18.1%)**

(with lump sum available by commutation)					
D: a new hybrid CARE / final salary arrangement	As whichever of **C** is offered plus around an additional 3% contribution from those employees who wish to join the final salary arrangement i.e. **B**[2]				

Notes:

a) the benchmark costings are not a funding recommendation for the Scheme, nor a representative or average Scheme cost. This is because DCLG do not consider it appropriate to produce average or representative costings centrally for a Scheme run by 89 separate funds in England and Wales, each with their own profile and individual challenges. Funds will take different approaches to valuing their individual assets and liabilities, and will make different recommendations for contribution rates for employers in their Fund. It is probably easier to consider the above figures as relative costs between the costs of the current and new Schemes, rather than as absolute costs.

b) the figures relate solely to future accrual. They do not take into account any past service deficits Funds may have.

c) the figures in brackets relate to the new entrants cost as a percentage of pensionable payroll. Over time, as existing members leave, the benchmark cost could be reasonably expected to move towards the figure in brackets.

11. The consultation paper asks for responses by **29 September 2006** to a number of key questions. These are set out in annexes 2 and 3 of the consultation paper and, in essence, ask the following questions:

- which of the new look schemes would employers support and why?
- what should the respective employee and employer contribution rates be for future service?
- should employee contributions be tiered based on the level of earnings?
- should a cost sharing mechanism (between employers and employees) be built into the scheme?
- should the level of commutation savings be kept under review?
- should a two tier ill health provision be built into the scheme and, if so, how should this work?
- would employers support extensions to the current flexible retirement provisions?
- should existing scheme members be transferred into the new scheme and, if so, how?
- should employers be allowed to opt into the provision of extra benefits for employees on a cost sharing basis?

[2] DCLG has confirmed that the costing relates to option B.

Next steps

12. The LGPC has reconvened the Working Party that previously considered the various LGPS Stocktake papers issued by the ODPM / DCLG since August 2001. It is hoped that during week beginning 7 August the Working Party will prepare information for authorities in England and Wales which will assist them in making a response to the DCLG consultation paper. The Working Party will be considering the pros and cons of each of the options discussed in the DCLG consultation paper.

13. Once the DCLG has received and analysed responses to the consultation paper, draft "new scheme" regulations will be issued in November 2007, with final regulations being made in April 2007. The new look Scheme would come into operation from April 2008.

Developments in Scotland

14. The Scottish Public Pensions Agency issued a letter and draft regulations on 29 June 2006. The amendments set out in the draft regulations will introduce various tax changes to the Scheme in Scotland (as in England and Wales) and remove the 85 year rule from 1 October 2006. However, the protections being consulted on in Scotland are:

    - transitional protection to 31 March 2008 for all **existing members** at 30 September 2006, i.e. 18 months transitional protection up to introduction of new Scheme
    - extended transitional protection to 31 March 2020 for those **existing members** at 30 September 2006 who will be 60 or over and meet the 85 year rule by 31 March 2020, i.e. this extends protection to existing members within 13.5 years of retirement

15. As will be noted, the proposed protection for older members in Scotland is better than that for older members in England and Wales.

16. The documents that accompany the draft Scottish regulation say "The draft regulations describe the Scottish Executive's preferred option. Having taken into account all the circumstances, the Scottish Ministers believe that it is appropriate to provide transitional provisions in respect of some existing members in order to protect reasonable expectations they may have regarding the application of the Rule of 85. The Scottish Ministers believe [the draft regulations] amount to a proportionate way to balance those expectations against the need to remove the discriminatory provision." However, the documents do say that the additional protections will mean that there is "less money available in the new look scheme for benefit improvements".

Change of contact details

17. Please note that we are now based at Local Government House, Smith Square, London, SW1P 3HZ.

18. Our contact details are as follows:

Terry Edwards, Head of Pensions, tel 020 7187 7346 or 01954 202787
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Terry Edwards
Head of Pensions
July 2006

Distribution sheet

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