AGENDA ITEM 7

FALKIRK COUNCIL

Subject:	**LOCAL GOVERNMENT PENSION SCHEME REFORM IN ENGLAND AND WALES**
Meeting:	**PENSIONS COMMITTEE**
Date:	**13 SEPTEMBER 2012**
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1. INTRODUCTION

1.1 This report updates the Pensions Committee about proposed reform of the Local Government Pension Scheme (LGPS) in England and Wales.

2. BACKGROUND

2.1 The Committee will be aware of the UK Government's policy of reforming public sector pension schemes. The process began in 2010, with UK Treasury seeking annual savings of £1.8b from public sector schemes, and continued in 2011 with the publication of the Hutton report.

2.2 The savings objective has led to significant contribution increases for members of unfunded schemes such as the teachers, police and fire schemes. However, the funded nature of the LGPS (and the risk of opting out) has persuaded the Government that savings from the LGPS can be delivered by some means other than solely contribution increases.

2.3 The UK Government has therefore accepted a joint submission from the Local Government Association, Unison and the GMB regarding the future shape of the LGPS in England and Wales - detailed proposals being announced on 31 May 2012. The aim is to have the statutory regulations in place by April, 2013 and the new look scheme operational from April, 2014.

2.4 The position in Scotland remains unclear as it is not known to what extent the Scottish Government will wish to imitate the new England and Wales LGPS. Notwithstanding the outcome of the independence referendum, there may be some elements of reform that have to be adopted in Scotland, as they will have a UK wide application. These include the replacing of final salary schemes with career average arrangements and the linking of scheme retirement age to State Pension Age.

3. THE NEW SCHEME

3.1 The main elements of LGPS 2014 (E&W) have been agreed as follows:

- Career Average Revalued Earnings (i.e. not final salary)
- Accrual Rate of 1/49th
- Revaluation rate – CPI (Consumer Price Index)
- Normal Retirement Age linked to State Pension Age
- Tiered Employee Contributions
- Average Employee Contributions to be 6.5%
- Employer Contributions to be within defined ranges ("cap and collar")
- Part time employee contributions to be based on actual pay
- Overtime payments and additional part time hours to be pensionable
- All staff subject to outsourcing will be able to retain LGPS membership
- Benefits prior to April, 2014 protected and linked to both final salary and current retirement age rules
- Additional protection for those within 10 years of age 65 at April, 2012
- 50/50 option (you pay ½ contributions and get ½ benefits)
- Other provisions remain the same (e.g. death in service, ill health, etc)

4. COMPARISON WITH CURRENT SCHEME

4.1 The current LGPS has been costed at 21.7% of pay. The new scheme has been costed at 19.5% of pay, split as follows:

Employees average contribution	-	6.5% of pay
Employer average contribution	-	13.0% of pay

These figures do not take into account any extra contributions being paid by employers to repair funding deficits.

4.2 The 2% savings from the new scheme are being delivered mainly by linking normal retirement age to the increasing state pension age. Unfortunately, the investment environment since the last round of actuarial valuations (in particular the low gilt yields) means that even with a newer, cheaper scheme, a reduction in employers' contributions is still unlikely at the next valuation.

4.3 An additional measure to contain future employer costs – known as the "cap and collar" - is likely to be prescribed within the upcoming Public Services Pensions Bill.

4.4 Compared to the current scheme (and based on earnings and inflation projections by the Government Actuary and HM Treasury), the proposals are likely to be (i) less favourable to younger scheme members, (ii) neutral for those in their mid-forties and (iii) an improvement for those in their late fifties. This effect is demonstrated in the table below:

Case Study	Current LGPS	LGPS 2014
Employee age 25 (in 2014), Retirement age 68	£15,900 p.a.	£11,300 p.a. (71% of current LGPS)
Employee age 45 (in 2014), Retirement age 67	£7,700 p.a.	£7,100 p.a. (92% of current LGPS)
Employee age 58 (in 2014), Retirement age 65	£2,300 p.a.	£2,600 p.a. (113% of current LGPS)

4.5 Despite the improved accrual rate (1/49th from 1/60th), this is not considered enough to compensate the younger person for their new benefits being linked to CPI rather than final salary.

4.6 The proposal that part time employees pay a contribution rate that is based on actual pay (rather than full time pay) means that many will receive a reduction in contribution rates which will have to be paid for by contribution increases at the mid to higher pay levels.

4.7 The "50/50" option is an attempt to encourage individuals for whom contributions have become too high to remain in the scheme and still accrue some rights. However, there is a risk that if too many members go 50/50, insufficient benefits are accrued and ultimately more reliance is placed on State benefits.

5. GOVERNANCE DEVELOPMENTS

5.1 In order to meet Hutton's recommendation for improved governance amongst public sector schemes, an LGPS Governance Working Group has been established to consider options. One approach being mooted would result in the establishment of an independent governance board with its own secretariat and staff to monitor and improve LGPS performance. The board could be funded from the fee which Funds currently pay to the Local Government Pensions Committee for specialist pensions information and guidance.

6. CONCLUSION

6.1 The proposals arguably represent the most radical attempt yet to reform the LGPS and to place it on a sustainable footing. The timetable for implementing the new arrangements by 2014 are especially challenging given the systems and documentation changes that will be necessary.

6.2 Concerns have been voiced by informed commentators that the agreed package may not deliver the type of savings needed to satisfy Government objectives and that within a short time further reforms may be needed. There is also the concern that the burden of paying for the changes seems to be falling on younger members.

6.3 The Scottish Government is not party to this agreement, but has previously stated it wishes the scheme to be sustainable in the long term and fair to all stakeholders. Assuming that some reform takes place in Scotland, it is hoped that further analysis is undertaken to ensure that the reforms actually deliver the results expected and that the burden of cost falls more evenly across all age ranges.

7. RECOMMENDATION

7.1 The Pensions Committee is asked to note the developments in the reform process for the Local Government Pension Scheme in England and Wales.

Chief Finance Officer

Date: 4 September 2012

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<u>LIST OF BACKGROUND PAPERS</u>

1. The New LGPS 2014 Project – joint press release by the Local Government Association (LGA) and Trade Unions (available at www.lgps.org.uk).

Any person wishing to inspect the above background papers should telephone Falkirk (01324) 506304 and ask for Alastair McGirr.