LGPS 2014
EMPLOYER OVERVIEW

This brief overview sets out the main features of the proposed LGPS 2014 which commences from 1st April 2014. This new scheme has resulted from the first phase of the LGPS 2014 project - a process of negotiation between the Local Government Association (LGA) and the local government unions in consultation with government. Full details of the LGPS 2014 proposals including proposed member contributions and examples of benefits are available on the LGPS website (www.lgps.org.uk).

COSTS OF THE LGPS 2014

The design of the LGPS 2014 has been costed by the Government Actuary's Department (GAD) at 19.5% of pensionable payroll. As the employee contribution yield is proposed to remain at 6.5% this gives a notional employer Future Service Rate (FSR) of 13%. This compares with the most recent GAD costs of 21.7% for the current scheme (15.2% employer FSR).

Each LGPS fund will have different individual circumstances for fund actuaries to take in account when determining the FSR. However we would expect to see an average reduction in the FSR in the region of 2%, across the 89 funds in England and Wales. That translates to around £600m per annum across the 89 funds.

This reduction in the FSR would be largely achieved by the link between Normal Pension Age and State Pension Age for all membership in the LGPS 2014 as contained in the design of the LGPS 2014.

An automatic link between State Pension Age and longevity will be announced by the Office of Budget Responsibility later in the summer. This link between longevity and pension age will negate a significant degree of the risk (and potential future cost) currently associated with increasing longevity.

However, the FSR is only one element which goes toward the total employer contribution rate. The other major factor is the past service cost.

The revised scheme design will have no impact on past service costs which will continue to be managed via existing deficit reduction strategies and employer contributions. If assumptions in relation to fund performance prove to have been optimistic at the 2013 valuation then any improvements to the overall employer rate due to the revised design may well be wiped out.

Given the difficult market conditions currently in effect many employers may see the impact of the new scheme design reflected in total contribution rates being not as high as they would otherwise have been rather than seeing a reduction.

FUTURE COST MANAGEMENT

A revised scheme design is just the first part of the process contained in the LGPS 2014 project. A mechanism to manage future costs is still to be agreed. This mechanism will impose a cap and collar on future costs, modifying the scheme design should costs move outside of a tight set of parameters.

The mechanism will operate within the provisions of the upcoming Public Service Pensions Bill and will be included in scheme regulations in place for the 2013 valuation.

Future costs will also be managed by the link between Normal Pension Age and State Pension Age for all membership in the LGPS 2014.

In order to ensure that this link continues to effectively manage risk in the scheme we propose working with fund actuaries to develop an LGPS longevity index. Such an index would enable fund actuaries to track the match between increases to SPA and longevity within the scheme and recommend action should they diverge.

These measures combine to ensure that in future not all of the risk falls on the employer but is shared with employees.

NEW SCHEME BENEFITS

The table below shows the main provisions of the proposed new Local Government Pension Scheme (LGPS 2014) for membership from 1st April 2014.

	LGPS 2014
Basis of Pension	**Career Average Revalued Earnings (CARE)**
Accrual Rate	**1/49th**
Revaluation Rate	**Consumer Price Index (CPI)**
Normal Pension Age	**Equal to the individual member's State Pension Age (minimum 65)**
Contribution Flexibility	**Members can opt to pay 50% contributions for 50% of the pension benefit**

Definition of Pensionable Pay	**Actual pensionable pay - to include non contractual overtime and additional hours for part time staff**
Vesting Period	**2 years**

LGPS 2014 contains some new features. All other benefits remain the same as in the current scheme.

Although some other changes were discussed, including to the ill health tiers, no agreement was reached at this point. However the door remains open to a future review of the ill health provisions.

MAJOR CHANGES FROM THE CURRENT SCHEME

CAREER AVERAGE

The shift to a career average or CARE basis for calculating benefits with a 1/49th accrual rate will be broadly cost equivalent to the current final salary with a 1/60th accrual rate basis of calculation. This is because CPI (Consumer Price Index) is proposed to be the revaluation rate used to increase each year's pension for inflation. CARE pensions are calculated each year then revalued rather than being based on the final year's pensionable pay.

THE 50/50 OPTION

LGPS 2014 is proposed to contain an option for members to pay 50% of the contributions for a 50% pension whilst retaining the full value of other benefits of the scheme. This is intended to attract non-members on low pay to the scheme and retain members who suffer periods of financial difficulty.

This will be a useful tool in encouraging younger employees to join the scheme thereby managing the risk of increased employer rates brought about by an increased maturity in membership.

Although not having any immediate effect on employer rates (i.e. the employer rate is the same for all members regardless of whether they pay full or 50/50 option) it will have an effect at valuation. For example, a significant take up of this option by existing members would result in a lower employer rate at subsequent valuations. Although an increase in participation by existing non members may result in increased cash costs in the short term these should be mitigated by the resulting impact on overall rates brought about by improvements in membership profile.
However the option is not designed to replace long term membership of the full scheme but is intended to provide a short term alternative to those considering opting out of the scheme.

CONTRIBUTIONS BASED ON ACTUAL PAY FOR PART-TIME STAFF

In LGPS 2014, all members are proposed to have contribution rates determined by reference to their actual – rather than full time equivalent - pay which is not the case in the current scheme. This will mean that some part-time workers will pay a lower contribution rate than in LGPS 2008. It should also result in a simpler definition of pensionable pay for the new scheme that will be easier to calculate and remove many of the current complexities for employers.

However employers will still be required to hold and supply the data necessary to calculate pensionable pay on the current basis for pre 2014 membership.

NEW SCHEME CONTRIBUTIONS

The average member contribution to LGPS 2014 will remain at 6.5% as now. However, it is proposed there will be changes to bands and some rates. The lowest paid would pay the same or less and the highest paid would pay higher contributions on a more progressive scale after tax relief.

The bands and rates will be reviewed prior to the introduction of LGPS 2014 to ensure they obtain a yield of 6.5% of pensionable payroll taking into account any movements in pay up to the review. Please note that the rates quoted after tax relief are indicative and will depend on members' individual circumstances.

PROPOSED CONTRIBUTION BANDS AND RATES FOR APRIL 2014

Pensionable Pay	Headline/Gross Contribution	Contribution After Tax Relief
Up to £13,500	5.5%	4.40%
£13,501 - £21,000	5.8%	4.64%
£21,001 - £34,000	6.5%	5.20%
£34,001 - £43,000	6.8%	5.44%
£43,001 - £60,000	8.5%	5.10%
£60,001 - £85,000	9.9%	5.94%
£85,001 - £100,000	10.5%	6.30%
£100,001 - £150,000	11.4%	6.84%

More than £150,000	**12.5%**	**6.88%**

This is a major shift from the government's initial reference scheme which proposed a 3% increase in the average employee contribution rate i.e. up from 6.5% to 9.5%. At the same time a commitment to protect all members below £15,000 (a third of the membership) from any increases and those below £21,000 (another third) to a maximum increase of 1.5% was given by the government. This would have resulted in rises significantly above 3% for the remaining third of the membership.

A very strong message from members that any increases would result in damaging levels of optants out was very much in mind when reaching this agreement. However forthcoming cost control mechanisms mean that future rises in employee contributions are not ruled out.

PROTECTION OF CURRENT BENEFITS

The new LGPS will start on 1st April 2014. Only membership after that point will be in the new scheme, under the new LGPS 2014 rules.

Existing pensioner and deferred members will not see any change to their benefits.

Employees with membership in the current final salary scheme will retain the link to final salary for all membership built up before 1st April 2014 and the Normal Pension Age as under the current rules for membership up to that date.

Previously agreed protection will continue, including the provisions for those members who were protected against the removal of the Rule of 85 in 2006. There will also be additional protection for members within 10 years of age 65 as at 1st April 2012.

PENSION PROTECTION ON TRANSFER

It is proposed that the provisions of the current scheme are extended to ensure that all staff whose employment is compulsorily transferred will still be able to retain membership of the LGPS when transferred.

This is an undertaking given by government in all of the public service pension scheme Heads of Agreement. However as many of these schemes do not have the Admitted Body Status provisions of the LGPS the exact impact of this undertaking is still to be determined.

Local Government Association

The Leaders of:

- County Councils (England)
- District Councils (England)
- Metropolitan Borough Councils (England)
- Unitary Councils (England)
- County and County Borough Councils in Wales
- London Borough Councils
- South Yorkshire Pension Authority
- Tameside Metropolitan Borough Council
- Wirral Metropolitan Borough Council
- Bradford Metropolitan City Council
- South Tyneside Metropolitan Borough Council
- Wolverhampton Metropolitan Borough Council
- London Pension Fund Authority
- Environment Agency

Regional Employers Directors
Town Clerk, City of London Corporation
Clerk, South Yorkshire PTA
Clerk, West Midlands PTA
Fire and Rescue Authorities in England and Wales
Police Authorities in England and Wales
National Probation Service for England and Wales

Association of Colleges
Universities and Colleges Employers Association
Association of Consulting Actuaries
Association of District Treasurers
Society of County Treasurers
Society of Welsh Treasurers
Society of Metropolitan Treasurers
Society of London Treasurers

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Audit Commission

ALACE
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SOLACE
CIPFA
ALAMA

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Barnett Waddingham
Aon/Hewitt
Mercer
Hymans Robertson

27th June 2012

Dear Colleagues

Local Government Pension Scheme 2014 employer consultation

On 31st May the LGA and local government unions, with the support of government, announced that agreement had been reached on proposals for a revised Local Government Pension Scheme (LGPS) to be implemented from 1st April 2014. We write now to seek your support for these proposals which we believe provide a solid base for an affordable, fair and sustainable scheme.

As government has confirmed that a favourable outcome of this consultation (together with those being undertaken by the local government unions) will enable them to move directly to a statutory consultation in the autumn we would urge you to respond to this consultation.

In order to ensure that all scheme employers have the opportunity to be part of this consultation we would ask that regional employer organisations and LGPS administering authorities confirm that this letter has been forwarded to all employers within their organisation or fund.

It should be stated at this point that the process of reform was only ever designed to address the future cost of the LGPS. There was no remit to consider or recommend any action to be taken in respect of past service costs and deficits.

The process undertaken to reach agreement and more information on the proposals including

a) an employer focused Overview document (also attached with this letter) and
b) an FAQ document which will be updated throughout the consultation

can be found at www.lgps.org.uk.

The proposals were agreed as a result of a process of reform that commenced with the publication of the report of the Independent Public Service Pensions Commission (chaired by Lord Hutton) in March of 2011. The report set out a number of recommendations that the government accepted as the basis for reform.

Local Government House, Smith Square, London SW1P 3HZ **T** 020 7664 3000 **F** 020 7664 3030 **E** info@local.gov.uk www.local.gov.uk

The major driver for reform outlined in the report was the increasing burden being placed on pension schemes from improved longevity. In the foreward to the report Lord Hutton stated;

'As I set out in my interim report rising life expectancy has led to a substantial increase in the proportion of adult life that a public service worker can expect to spend in retirement. To adjust to this change I am recommending that Normal Pension Age is linked to State Pension Age and tracks planned increases [to the State Pension Age]....

This link to State Pension Age will address rising longevity, the main risk to the sustainability of public service pensions.'

These proposals contain such a link between the LGPS pension age and State Pension Age and we, like Lord Hutton, consider that achieves the long term sustainability sought by this process,

Lord Hutton's report set out a number of other recommendations on benefit design. The first of these being a move from final salary to career average revalued earnings (CARE) for all service in the new scheme while maintaining the final salary link for existing service. The purpose of this change was not cost, rather (according to Lord Hutton's forward);

'I believe this is the fairest way of spreading the effect of change across the generations, and represents the quickest way of ending the in-built bias against those public service employees whose pay stays low over their career, inherent in final salary schemes.'

These proposals contain such a move to CARE for all service from 2014. The accrual rate proposed of 1/49th with a revaluation rate of the Consumer Price Index (CPI) has been costed by the Government Actuary's Department (GAD) as being broadly the same as the current 1/60^{ths} final salary accrual rate. The www.lgps.org.uk site contains a set of worked examples that show how the benefits from the new scheme compare with those of the current scheme.

Lord Hutton did include a recommendation to increase employee contributions to public sector schemes. Although this will be implemented for the unfunded schemes we have not proposed any increase in the overall yield from employee contributions which will remain at 6.5% of pensionable payroll. However we have proposed a shift to rates that are more progressive net of tax relief and moving to rates for part time employees based on actual rather than full time equivalent pay. Both of these changes have resulted in increases for higher rate tax payers but 95% of employees will not face higher contribution rates.

In reaching the proposal on contribution rates we were mindful of the impact that significant levels of optants out, amongst a workforce that have not had a pay rise in three years and are in the main low paid, could have on fund cash flows and resultant maturity profiles. More information on this option can be found in the employer overview document attached.

Finally we have proposed a 50/50 option that is designed to provide an alternative to opting out for mainly younger and lower paid staff (particularly once automatic enrolment is in place) and if successful should address the increasing maturity of the scheme membership.

Taken together the changes we are proposing have been costed by GAD at a future service total of 19.5% (6.5% employee and 13% employer) compared with 21.7% for the current scheme with the majority of the reduction coming from the move to State Pension Age.

Future scheme costs will be controlled via a cost management mechanism which will be introduced alongside the scheme design changes. The mechanism will contain triggers and responses designed to ensure that future scheme costs do not breach defined 'cap and collar' limits. Details of the mechanism will follow the publication of the Public Service Pensions Bill in the autumn.

The form attached with this letter asks that you indicate your general support (or not) for these proposals. We are aware that not all employers will like all the proposals and that, in different circumstances, different choices may have been possible. However we consider these proposals to be the best possible outcome of a process of negotiation that had the further aim of reaching agreement with unions in order to avoid a drawn out period of industrial unrest and uncertainty amongst scheme members. In such circumstances we would hope you agree that achieving the central objective of the link to State Pension Age is worthy of your support.

Should the outcome of the consultation be positive, government will move forward with a statutory consultation in the autumn. If not, the government will have to take its own view on the next steps. However in that case any introduction of a new scheme by 2014 would be far from certain.

Yours sincerely

Mayor Sir Steve Bullock: Chair LGA Workforce Board (Labour)

Cllr Steve Comer: LGA Pensions lead team (Liberal Democrat)

Cllr Roger Phillips: LGA Pensions lead team (Conservative)

LGPS 2014 Proposals- Employer consultation form

Please be aware that only one form should be returned for each employer with participating scheme members. If multiple forms are returned they will be excluded from the consultation (see note 1).

Forms provided without a valid email address and phone number will be also be excluded as we will be auditing responses to ensure they originate from a bona fide LGPS employer

Forms should be returned by 27th July, either sent to

Elaine English
Workforce Team
Local Government Association
Local Government House
Smith Square, London, SW1P 3HZ

Or scanned and emailed to Elaine.english@local.gov.uk. In either case forms must be signed by an authorised employer representative.

Employer name		
Name of LGPS fund in which the employer participates [1]		
Number of employees participating in the LGPS on 30th June 2012		
Authorised representative	Print name	
	Sign	
	Email	
	Telephone	
As an overall package the employer named above (please tick)		
Supports		
Does not support		
the proposals agreed by the LGA and local government unions for a reformed LGPS		

[1] This field should be completed in all cases and is the name of the local fund that you are a participant in. If you have multiple admission agreements and participate in more than one fund please provide only one response naming one of the funds but provide the total number of participating employees across all funds in the box below

Comments