employersorganisation

Initial employer proposals for amendments to the Local Government Pension Scheme Regulations 1997 from April 2006

Background

1. Following the last Tripartite Committee meeting on 30th June 2005 the Deputy Prime Minister (DPM) tasked the employers and unions to come forward with proposals by the end of September detailing, for his consideration:

   a) how, based on factual data, the cost of revocation of the April 2005 changes to the LGPS in England and Wales should be met, and
   b) what changes should be made to the LGPS from April 2006 to achieve this.

2. Failure by the employers and unions to reach an agreement on proposals to put to the DPM could mean that the DPM would have to impose a solution from April 2006.

3. The employers have carefully considered the longevity and demographic report commissioned by the ODPM which showed that:

   - the working population in the economy is falling, whilst the pensioner population is increasing and living for longer
   - since the early 1970s, there has been a 31% improvement in the life expectancy for male pensioners retiring at 65 and 18% for female pensioners. Local government pensioners retiring in normal health can expect, on average, to live 2 to 4 years longer than pensioners in the rest of the economy
   - even if changes introduced by the Deputy Prime Minister in April 2005 (and then revoked), which standardised the retirement age at 65 by removing the 85 year rule, were to be reintroduced from April 2006, the savings generated would not offset the additional pension costs incurred as a result of the increased in longevity since the early 1970's
   - the number of scheme members retiring after they have met the 85 year rule would add approximately 6 months to the average age of retirement of all retirees.

4. We have also considered the Government's legal advice that the removal of the 85 year rule is necessary (from October 2006 at the latest) in order to comply with the forthcoming Age Discrimination legislation.

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5. Following the issue of LGPC Circular 175, information on the cost of the revocation, originally estimated at £400 million, is being prepared by Pension Funds and this information is to be supplied to the ODPM by the end of September.

6. The EO has, as promised, requested data from all LGPS Funds showing

   - the average retirement age of all LGPS pensioners broken down by employer type and by sex (M/F)
   - the average retirement age of all LGPS pensioners retiring in the year to 31.3.05. broken down by employer type and by sex (M/F)
   - the average pension for all LGPS pensioners broken down by employer type, by sex (M/F), and by type of pension
   - the average pension, and the average service and average pay on which the pensions were calculated, for all pensioners retiring in the year to 31.3.05. broken down by employer type, by sex (M/F), and by type of pension

   A summary of the data collated so far has been supplied to the unions. The summary will be updated to include the data from any further returns received from LGPS Funds.

Proposals

7. In our view the longevity/demographic report and the Government's legal advice adds considerable weight to the employers' position that, in order to ensure that we have a scheme that is affordable, sustainable, and fair to our workforce as well as to employers and taxpayers and to ensure that we comply with Age Discrimination legislation, the 85 year rule must be removed and further adjustments to the benefit structure or an increase in employee contributions is required.

8. The following initial proposals are designed, as requested by the DPM and without prejudice to our negotiating position, to deal with the cost of the revocation of the April 2005 changes whilst at the same time giving scheme members more choice and flexibility[1]. This will pave the way for further discussions about a new-look pension scheme for the future by helping to stabilise the cost of the present scheme.

22 September 2005

[1] The initial proposals were intended for consideration by the unions in preparation for, and to help inform debate at, the next Tripartite Committee meeting

What do the employers want?	Why?	What does this save?
Removal of the 85 year rule from April 2006 (so that Normal Retirement Date is standardised at age 65)	a) to deal with increased longevity and the demographics of an ageing workforce b) recognises Government's stated position of moving NRD in public sector schemes to 65 c) needs to be removed from Scheme to comply with Age Discrimination legislation (and it could also be argued that the 85 year rule is discriminatory on the grounds of sex as women tend to have less service than men due to family commitments)	Reduces average employers' rates (according to GAD) by 1.6% - 2% (and by 2% to 2.5% by 2013) – but these figures might reduce by, at most, 0.25% on account of average retirements occurring approximately 6 months after those assumed by actuaries when preparing Fund valuations. Any changes to the actuarial reduction factors could negate some of the savings that would accrue from the removal of the 85 year rule (compared to if the current actuarial reduction factors were retained) and will need to be factored into the equation.
No phased protection for older workers	Fairer and more equitable to all members i.e. it has proportionate effect in that those closer to retirement will in any event have less service after 'A' day that will be subject to reduction if drawn before 65 than those who are younger. Overcomes the current	The 2% - 2.5% savings mentioned above would occur immediately rather than being phased in.

	'cliff-edge' approach to protection. The savings from not having protections could be used to partially offset the cost of revocation. Moving away from the Government's White Paper commitment that those within 10 years of retirement would not be affected by the change in NRD to 65 is, arguably, justifiable. We already have an NRD of 65 – the 85 year rule simply determines the amount of reduction applied if benefits are drawn before 65. Also, the DPM has said that "nothing is ruled in or out". We recognise, however, that this could be controversial due to the expectation of protection that older workers have following the Government's White Paper commitment (and the protection that they were given under the April 2005 changes which, admittedly, have now been revoked).	
Increase minimum age able to draw benefits from 50 to 55 (other than on health grounds)	It is the Government's stated policy and the Finance Act 2004 requires all schemes to increase the minimum age from 50 to 55 by 2010.	Raising the minimum age would not result in a saving to Funds (as the employers have to pay the capital cost of early retirements into the Funds), but those capital costs do, of course, have to be met by employers.
Increase in employee contribution rate by 1% to 7% (6% for protected manual workers) for 2006/07 and	Helps to pay for increased life expectancy and recovers the cost of revocation over the remaining lifetime of the triennial valuation period (Pay bill of £19 billion x 1% = £190 million for 2 years = £380 million).	Meets cost of revocation.

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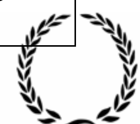
Incentive for people to remain in employment for longer	e.g. employees to be able to remain in the LGPS beyond age 65 with an actuarial increase to benefits where payment is deferred beyond age 65.	Although incentives might initially appear to cost money, and an actuarial increase to benefits if drawn after age 65 could nullify any possible savings from delayed retirements after that age (depending on level of increase), the net result of keeping members in employment for longer could be beneficial, e.g. skill retention and reduced training/recruitment costs.

What can employers give in return?	**Comments**
Flexible retirement (linked to reducing hours / reducing grade)	This is a flexibility that employees / unions want and will also be a useful tool for employers in managing the ageing workforce. Flexible retirement would need to be at the employer's discretion, in accordance with an employer policy, with all accrued rights (at Phase 1) to be taken, and with employer ability to waive any actuarial reduction in whole or in part. Note: the actuarial reduction should be based on shortfall to age 65 or, for protected service, the later of age 60 or the date the 85 year rule would have been attained. This ensures cost neutrality for employers, (unless the employer agrees to waive the reduction in whole or in part). If flexible retirement is introduced it will mean that the current abatement rules in the LGPS will probably have to be removed (i.e. the rules under which a pension in payment is reduced if a pensioner's earnings from re-employment in local government plus their pension exceeds their former pay before retirement). The amount of abatement savings 'lost' by the employers will depend on the number of



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	pensioners who are re-employed / take flexible retirement. However, flexible retirement would probably be a non-starter if the abatement rules were to be retained.
Ability to buy-out the actuarial reduction to benefits paid before 65 (by voluntarily paying increased employee contributions)	Feedback from the roadshows indicates that scheme members are not averse to the removal of the 85 year rule per se. What they object to is the removal of the ability to still retire at 60 with an unreduced pension. As the 85 year rule has to be removed from the scheme, offering members the right to buy-out the reduction seems a reasonable way forward. The amount the employee would have to pay would need to be actuarially assessed. Also, a discretion could be provided for employers to share the cost of buying-out the reduction similar to the current shared cost AVC arrangements. The method of paying extra contributions would need to be determined so that people who carried on in work beyond age 60 would get an appropriate return for the contributions they had made.
Remove the current 15% contribution limit	Fits in with Inland Revenue changes from April 2006. Allows those who want to buy out reduction (see box above) to pay as much in contributions as they wish (up to max of 100% of pay). However, we would need to retain either a 10% additional contribution limit for added years contracts or limit the maximum added years to, say, 6 years 243 days, and limit the maximum annual added years purchase to say 1 year. (This is to protect employer interests as these contracts are deemed to be fully paid for if the employee retires on health grounds or dies in service. A limit on annual added years purchase is also needed to protect funds from very high purchases from employees who, for example, are aware of an impending substantial pay increase).
Removal of the 40 years at 60 / 45 years at 65 service limits	Fits in with Inland Revenue changes from April 2006. Benefits long serving scheme members. But we would need to remove the current scheme rule that allows employers to reduce or waive employee contributions after 40 years.
Ability to take up to 25% of value of benefits as a lump sum	This is an additional flexibility for members. However, we would wish to ensure that members take a minimum 3/80ths lump sum.