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pay, pensions and employment solutions

The Local Government Pensions Committee
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CIRCULAR

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No. 189 – JULY 2006
NEW LOOK LGPS

Purpose of this Circular

1. As promised in Circular 188, the Working Party convened by the Local Government Pensions Committee (LGPC) has considered the possible options for a new look LGPS in England and Wales, as outlined in the Department for Communities and Local Government (DCLG) consultation paper of 30 June 2006 (see http://www.lge.gov.uk/pensions/content/documents/consultation_new_look.pdf)

2. This Circular provides information which, it is hoped, will help authorities in England and Wales when responding to the DCLG consultation paper. It also includes a questionnaire at appendix 2, the completion and return of which by **21 September 2006** will assist the LGPC and the LGE to make a response to the consultation paper.

Background

3. The DCLG 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%)**

4. Having arrived at a benchmark cost, the consultation paper then offers the following 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 (with lump sum available by commutation)	21.5% (18.9%)	0.3% (0.2%)	0.3% (0.2%)	-1.1% (-0.8%)	**20.5% (18.1%)**
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**[1]				

Notes:

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

b) 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.

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

Responding to the DCLG consultation paper

5. The following information, which includes and builds on the information in the Chapters in the DCLG consultation paper, may be of assistance to authorities in responding to the questions posed in that paper. The deadline for responses to the DCLG is **29 September 2006**. Due to the significance of the issues involved, elected members should be consulted before authorities make a response.

<u>Chapter 6: Type of Scheme – the options</u>

6. The consultation paper sets out a number of options for a new look LGPS (as detailed in paragraph 4 above). It is important to note that the DCLG have said that "Funds and scheme employers are strongly encouraged to use [the information in the consultation paper] to asses the likely impact on their costs, should any of the options detailed [in the consultation paper] apply from 2008". This is because the benchmark costings set out in the table in paragraph 4 above are not a funding recommendation for the Scheme, nor a representative or average Scheme cost. The cost of future service under each of the options for any particular employer may well be different to that shown in the table. The 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 figures in the table in paragraph 4 above as relative costs between the costs of the current and new Schemes, rather than as absolute costs. Furthermore, it is important to note that, at an individual employer level and depending on the make up / career patterns of the workforce, Option A might not necessarily be the cheapest.

7. It is also, perhaps, prudent to note that at the 2004 Fund valuations many of the Funds' actuaries had assumed that all savings from the removal of the 85 year rule would be retained and had not factored in that 50% of the savings would be recycled into the new Scheme[2]. Thus, all else being equal, one might expect that the employers' contribution rates at the 2007 valuation would increase as a result of the recycling by an average, according to annex 1 of the DCLG consultation paper, of circa 0.8%.

8. Each of the Scheme options presented in the consultation paper includes an increase in the death in service lump sum from 2 to 3 times pay, the introduction of partners' pensions for cohabitees (subject to the overarching legal position and timetable), and targeted two-tier ill health retirement provisions. Each of these is considered below.

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[2] The ODPM letter of 30 December 2004 said "In addition, the changes now introduced [removal of the 85 year rule] will help to mitigate the additional pension costs associated with increased longevity and Scheme actuaries will take them into account in the 2004 LGPS valuation exercise, which will set employer contribution rates for the three financial years from April 2005.

9. When we consulted employers at the beginning of 2005 the vast majority were in favour of increasing the lump sum death in service payment to 3 times pay (see appendix 1).

10. Before looking at the question of cohabitees' pensions it is worth making some points about the current provisions for spouses, registered civil partners and children.

11. The current widow's, widower's, civil partner's and children's pension provisions (e.g. short term pension, long term pension, proportion of deceased's benefit payable, whose care eligible children are in, whether pre 6.4.78. / pre 6.4.88. membership counts, etc) are overly complex. These should be significantly simplified in the any new Scheme with all beneficiaries being treated in a fair and equitable way e.g. membership between 1.4.72. and 5.4.88. should count for widowers' pensions as most, but not all, employers have already permitted such membership to count. Consideration will need to be given as to whether membership between 1.4.72. and 5.4.88. should count for civil partners' pensions (to ensure equal treatment with widow's and widower's pensions).

12. In any new Scheme, spouse's/registered civil partner's benefits should be a proportion of the member's pension. If, in Options B, C1 or C2, the proportion were to be 50% of the pre commutation pension, this would result in a significant improvement in the level of survivor pension compared to the current Scheme. Setting the level at 50% of the post commutation[3] pension may act as an incentive for those with a spouse/registered civil partner not to commute. Having different commutation factors depending on marital/partner status may not be practical or desirable. It might, therefore, be better for the fraction to be specified as a lower percentage of the pre commutation pension or, preferably, for the spouse's/registered civil partner's benefit accrual rate to be defined directly (i.e. as a 1/160th accrual rate which would save about 0.4% in respect of existing scheme members, or 0.3% in respect of new members compared to a 1/120th accrual rate).

13. As well as providing survivor benefits to widows, widowers, registered civil partners and children, the consultation document proposes that survivor benefits could be extended to cohabitees.

14. Our historical position has been to support union demands for a change to the Scheme in order to provide for partners' pensions in general. There were two key drivers for supporting change. Firstly, to recognise the problem that same sex partners were not able to enter into a registered partnership and secondly to reflect changes in society (i.e. an increase in "common-law" partners).

15. The first of these obstacles has been removed now that same sex couples are permitted to enter into a civil registration. Registered partners are now entitled to a survivor benefit in the LGPS based on the Scheme member's post 5 April

[3] However, the level of a spouse's/registered partner's/children's pensions following a death in service would need to be considered as there would have been no commutation (but the Scheme would also be providing a death grant of 3 times pay). Also, one assumes that a death in service would generate ill-health enhancement equal to 50% of the membership to age 65 in respect of the deceased member's benefits.

1988 membership. The Scheme member's pension benefits are subject to being split (in the same way as pension sharing on divorce) if the civil registration is brought to an end.

16. This leaves the position of cohabitees to be considered. The consultation document includes cohabitees pensions in the costing of the new scheme options, based on the same principles and criteria as have been adopted for the Civil Service Pension Scheme. The Civil Service Pension Scheme provides a survivor benefit for cohabiting partners provided there is evidence of:

- co-habitation
- an exclusive, long-term committed relationship established for a minimum of 2 years
- financial dependence or interdependence; and
- a valid nomination of a partner with whom there would be no legal bar to marriage or civil registration.

17. It must be recognised that if the LGPS were to go down this route, it would be providing benefits to cohabitees who are not legally recognised for virtually any other purposes by the State. Furthermore, the provision of cohabitees' pensions would introduce a number of inequalities that would need to be considered (particularly if they could leave the Scheme open to challenge) e.g.:

- a married or civilly registered couple do not have to be living together in order for a survivor pension to be paid (they could be living apart)
- a married or civilly registered couple do not have to be in an exclusive, long-term relationship established for a minimum of 2 years in order for a survivor pension to be paid
- a married or civilly registered couple do not have to show financial dependence or interdependence
- a survivor pension would automatically be paid to a married or civilly registered partner; they do not have to have been nominated to receive a pension by their spouse/partner. The lack of a valid nomination form would surely result in disputes where all the other criteria set out in paragraph 16 above are met
- the benefits of a married or civilly registered couple would be subject to pension sharing on divorce or the dissolution of a civil partnership , whereas those of a member with a nominated cohabitee would not be, even though the Scheme will have had a prospective partner's pension liability during the period of the co-habitation
- single members who are not co-habiting are not able to nominate a person to receive a pension upon their death

18. Thus, whilst it is correct to consider the introduction of cohabitees' pensions in a new-look LGPS it must be recognised that there are significant complications. It would probably be wisest, therefore, to await outcomes from the Law Commission's consultation paper no. 179 *Cohabitation*: *The Financial Consequences of Relationship Breakdown* (published on 30 May 2006) before taking a final decision on whether / how cohabitees pensions should be built into a new-look LGPS.

19. With regard to a two-tier ill health retirement system, please see paragraphs 50 to 62 below.

The Options for a new-look LGPS

Option A: An updated current scheme, with additional benefit improvements

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%)**

20. This is a lower-cost option than Options B and C. The reduction in costs generated by the move to two-tier ill health pension provision actually means it costs less than the current scheme at 1 October 2006 (i.e. without the 85 year rule), despite the improvements to death in service benefits and cohabitees pensions. This option would therefore, other things being equal, require a lower contribution rate from employers and/or employees than would be the case for Options B and C. Of course, if Option A were the preferred option one would expect the unions to seek improvements to the package as they will point to the fact that the cost of Option A in relation to existing Scheme members is 19.4% compared to the benchmark cost of 20.9% (see paragraph 3 above).

21. A final salary scheme is a valuable recruitment and retention tool for scheme employers, as it tends to focus benefits on longer-serving staff, particularly on those who progress up the earnings scale whilst in employment. It is an especially attractive option for these individuals, both currently and in the future. However, it may provide lower value benefits than a CARE scheme would for employees whose pay increases are less than the CARE scheme's revaluation rate under Option C2 (RPI plus 1.5% per annum). The position of comparison with Option C1 is more complicated with members under C1 having a higher accrual rate but with benefits being revalued in line with increases in RPI only. Such a scheme would benefit short-term staff compared to the other options.

22. Retaining the current final salary structure will minimise the effect of the change on existing scheme members. It also overcomes the difficulties associated with converting current membership into the new scheme (see paragraphs 63 to 65 below). Conversely, retaining the current final salary structure may not be seen to be innovative or modern.

23. Authorities will also wish to consider the fact that their employees will be working alongside teachers, firefighters, police officers, and NHS employees, for whom the pension arrangements are (or appear likely to be) final salary pension schemes[4].

24. From an administration point of view, a final salary scheme is perhaps more cumbersome to administer, compared to a CARE scheme, in respect of casual and part time employees (due to the need to record changes in hours and calculate whole time equivalent pay in a final salary scheme). However, the nature of a CARE scheme means that it will be vitally important for accurate pay data to be provided by employers, and checked and cleansed by administering authorities on an annual basis (including the need to "add back" pay for those employees who during the year were on reduced pay due to sickness, maternity, authorised leave of absence, etc).

25. From an actuarial point of view when setting the employers' contribution rates, retaining a Scheme offering a 1/80th pension and a 3/80ths lump sum (i.e. Option A), rather than a 1/60th pension with a lump sum by commutation (i.e. Option B), provides more certainty as it is known that at least a minimum of 3/80ths will be taken as a lump sum (with any extra being taken by commutation).

Option B: A new final salary scheme with an improved accrual rate

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
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%)**

26. It is difficult to compare the value of the current 1/80th pension and 3/80ths lump sum structure to one in which there is no automatic lump sum. However, on the basis of assumptions consistent with those underlying the benchmark costings, the current structure is approximately equal in value to an accrual rate of 1/64.5

[4] The proposed scheme for new NHS employees would be based on the average of the best 3 revalued consecutive years pay in the last 10 years. The Teachers scheme is looking at final salary or, if better, the average of the best 3 revalued consecutive years pay in the last 10 years.

(close to 1.55%). Therefore, moving to a 1/60th (1.67%) accrual rate represents an improvement in the member's benefits of 7.5% (1/60 divided by 1/64.5)[5].

27. Option B actually costs 0% (0.3% for new members) more than the target benchmark for a new-look scheme with 50% of the savings from the removal of the 85 year rule and commutation recycled into benefit improvements. In order to ensure the scheme's affordability to employers, it would be likely that an increase in employee contribution rate would be necessary. As Option B costs more than Options C1, C2 and particularly A, this increase would be likely to be larger.

28. Retaining a final salary structure will minimise the effect of the change on existing scheme members and, indeed, Option B would slightly improve the accrual rate, but there would still be potential difficulties associated with converting current membership into the new scheme (see paragraphs 63 to 65 below).

29. Paragraphs 21 and 23-25 above equally apply to Option B.

Option C: A new, career average scheme

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
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	21.5% (18.9%)	0.3% (0.2%)	0.3% (0.2%)	-1.1% (-0.8%)	**20.5% (18.1%)**

[5] If we were to use more conservative assumptions (i.e. that the pension has a value of 15 times the lump sum rather than 12 times) then, for members who take all their benefits in the form of pension but no lump sum, the equivalent accrual rate is closer to 1/66.7, equal to a 10% improvement.

and RPI revaluation after leaving (with lump sum available by commutation)					

30. Options C1 and C2 move from a final salary scheme to a career average scheme. They cost 0.3% (0.6%) and 0.4% (0.2%) less than the target benchmark for a new-look scheme with 50% of the savings from the removal of the 85 year rule and commutation recycled into benefit improvements. In order to ensure the scheme's affordability to employers, it would be likely that an increase in employee contribution rate from its current rate of 6% would be necessary. This increase would be likely to be more than that which would be required for Option A, but less than that which would be required for Option B, because of their relative costs.

31. As with a final salary scheme, a career-average LGPS would retain the nature of the LGPS as a good quality, defined benefit government-sponsored scheme. However, the difference from a final salary scheme is that rather than the benefits being calculated by reference to the member's pay at or near retirement, they would instead be calculated by reference to the average earnings over the member's whole service. The individual years' earnings would be revalued in line with an index. (e.g. by RPI or by RPI + 1.5%)

32. Option C1 is the more usual CARE design. Due to the higher accrual rate, it has a greater redistributive effect (and is thus more beneficial) than Option C2 for short service scheme members. Option C2 is more similar to a final salary benefit compared to Option C1 but the revaluation rate of RPI plus 1.5% could be expensive compared to a final salary scheme if salary increases are closer to RPI in the future. Whilst RPI plus 1.5% is close to the historic salary increases, this trend could change.

33. Some employees would be better off under C1 and/or C2 than under a final salary structure. A CARE scheme may provide higher value benefits than a final salary scheme would for employees whose pay increases are less than the CARE scheme's revaluation rate under Option C2 (RPI plus 1.5% per annum). Comparing Option C1 with a final salary scheme is more complicated with members under CARE having a higher accrual rate but with benefits being revalued in line with increases in RPI only.

34. So, based on the above, and in comparison to a final salary scheme, a career-average scheme tends to redistribute benefits towards shorter serving staff and / or to staff whose pay over time does not increase by more than the scheme revaluation rate. The flip side of this is that longer serving, career staff are likely to receive a lower benefit under a CARE scheme than under a comparable final salary scheme. At appendix 3 we set out some sample figures comparing Option C1 with Option B, just to illustrate how a CARE scheme and a final salary scheme might compare.

35. One of the key questions, therefore, is to consider whether, as an employer, you wish the scheme to be part of the remuneration package for attracting / retaining / rewarding longer serving, career staff or whether you wish the scheme to have a redistributive effect as outlined in the preceding paragraph. If the latter, the change in the structure of the pension scheme and its cost to certain employees might lead to demands for related compensatory changes to pay from those for whom a shift to a CARE scheme would be detrimental.

36. Authorities will also wish to consider the fact that their employees will be working alongside teachers, firefighters, police officers, and NHS employees, for whom the pension arrangements are (or appear likely to be) final salary pension schemes[6].

37. The arguments for introducing a CARE scheme appear to be that:

- it will have a redistributive effect towards the lower paid and / or those whose pay does not rise by more than the CARE scheme's revaluation rate, and for late joiners and early leavers who may not have time to achieve promotions;
- it is still a defined benefit scheme and therefore still provides employees with some certainty;
- the administration of part-timer and multiple/flexible working pattern benefits can be somewhat simpler than under a final salary scheme. However, the nature of a CARE scheme means that it will be vitally important for accurate pay data to be provided by employers, and checked and cleansed by administering authorities on an annual basis (including the need to "add back" pay for those employees who during the year were on reduced pay due to sickness, maternity, authorised leave of absence, etc);
- there is no need for certificates of protection where members' pay is reduced;
- employees have less need to worry if their earnings fluctuate and/or fall off as they approach retirement which, in itself, could encourage a more flexible approach to retirement;
- from the employee's perspective, the imponderables of whether or not it is beneficial to aggregate separate periods of local government pension rights would be removed;
- from the employer's perspective, compared to a final salary scheme, it avoids expensive liabilities being incurred in those cases where a member transfers from one LGPS Fund to another on a significantly higher salary (the costs of which are not met by the amount of the transfer value being received). Furthermore, a CARE scheme would negate the "strain" costs associated with promotions within an authority i.e. if an employee is promoted from a £15,000 post to a £20,000 post,

[6] The proposed scheme for new NHS employees would be based on the average of the best 3 revalued consecutive years pay in the last 10 years. The Teachers scheme is looking at final salary or, if better, the average of the best 3 revalued consecutive years pay in the last 10 years.

not only does the value of future service benefits in a final salary scheme increase but the value of all the accrued past service benefits increases by a third. With a CARE scheme only the value of future benefits would increase as a result of the promotion;

- from an employer's perspective, to the extent that the revaluation index is less than actual earnings increases, the benefits under a CARE system, and therefore the associated costs, will tend to be lower than under a final salary scheme, unless this is compensated for by a higher accrual rate;

- it is not accurate to portray a final salary scheme as benefiting all 'high flyers'. Those who come into local government at a middle management or senior level from outside of local government and who do not subsequently get promoted do not unduly benefit from a final salary scheme. Indeed, such people could benefit from a CARE scheme;

Conversely:

- a CARE scheme would not be attractive to employees who have a career in local government and who obtain future promotions. They could receive a significantly lower benefit under a CARE scheme than under a comparable final salary scheme, particularly if the promotions were to occur in their later years. This is not just an issue for senior officers; it would equally affect, for example, a craft worker being promoted to foreman;

- employees who get promoted, particularly if they have been on lower pay for most of their career and get promoted in the latter years of employment, will see a significant drop in their replacement income on retirement. For example, under the present final salary scheme a member could expect a half pay pension after 40 years scheme membership whereas, under a CARE scheme, the replacement income could be considerably less. This is an issue for scheme members if they wish to plan and budget for their retirement. They will need to have a view at the outset of their employment about what level they may rise to in their career in local government in order to consider what replacement income level they wish to target. This will be extremely difficult to determine early on in a person's career;

- a CARE scheme is less attractive than a final salary scheme when employees are considering whether or not to apply for promotion within the employer. It is therefore of less benefit to employers in terms of retaining and developing staff;

- whilst it is argued that a CARE scheme is fairer to those with flat career structures, the incremental progression for lower paid staff as a result of Single Status now partially negates this argument;

- it is argued that a CARE scheme would be more beneficial to women who take a career break. However, many women who take a career break to raise a family or who take a lower paid, lower graded, job whilst bringing up a family, eventually return to the workforce full-time and eventually gain promotion. If so, a final salary scheme would be of more benefit to such employees than a CARE scheme;

- selling a CARE scheme to staff could be difficult when the press has been portraying a final salary scheme as the 'jewel in the pensions crown'. We would need a very good story to tell to persuade staff to the contrary;

- in a final salary scheme, the proportion of the employer contribution to meet the cost of benefits is higher for older workers than for younger workers. A CARE scheme would exacerbate this (due to a higher accrual rate) and the proportion of the employer contribution necessary to meet cost of benefits for older workers would be even larger. This could be an issue with an ageing workforce;

- a CARE scheme would be less attractive to career employees (including many of the hard to fill posts within local government) than a final salary scheme. As the pay rates for middle and senior management are less than is paid to their counterparts in the private sector, whereas the opposite is true in respect of the lower paid staff in local government, a move to a CARE scheme could eventually necessitate a rebalancing of the pay structures within local government;

- some argue that a CARE scheme is more difficult to explain to employees;

- moving to a CARE scheme would create potential difficulties associated with converting membership for current scheme members into the new scheme (see paragraphs 63 to 65 below);

- authorities will also wish to consider the fact that their employees will be working alongside teachers, firefighters, police officers, and NHS employees, for whom the pension arrangements are (or appear likely to be) final salary pension schemes[7].

Option D: A new, hybrid scheme

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**
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**[8] **Note**: the Scheme could permit employers to meet some or all of the additional 3% cost on behalf of employees (but see paragraphs 66 and 67 below)				

38. Option D would be based on Option C1 or C2, so the evaluation for these options also applies here. Additionally, the final salary choice would mean that those existing scheme members who wished to continue in a final salary scheme, could, while not reducing the quality of the career-average scheme which could be provided for the rest of the workforce.

[7] The proposed scheme for new NHS employees would be based on the average of the best 3 revalued consecutive years pay in the last 10 years. The Teachers scheme is looking at final salary or, if better, the average of the best 3 revalued consecutive years pay in the last 10 years.

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

39. This flexibility would be valuable to employers in recruiting and retaining long serving, high progression staff, who stand to benefit most from a final salary scheme relative to a career-average scheme.

40. However, introducing choice into the LGPS will mean that some individuals may choose what could turn out to be "the wrong option" – because of their patterns of promotion and salary growth turning out to be different to how they had thought when they decided which scheme to enter. There would be a need for clear communication to scheme members, which would set out their options, without advising, potentially incorrectly, on which to opt for at the point of decision.

41. The alternative would be to allow scheme members multiple opportunities to switch between the career-average and final salary options. However, this could result in the additional cost of the final salary option possibly rising to as much as 6% because of the effect of selection. As this cost would be likely to be prohibitive, scheme members should have one opportunity, possibly at the outset of their employment, to elect to pay extra contributions.

42. One possible issue with Option D is staff perception i.e. if employees are told that membership of the final salary scheme costs 3% more than the CARE scheme, the perception will be that the CARE scheme is inferior (and that staff who join the CARE scheme are, in some way, getting an inferior deal even though, in reality, the additional 3% would be to cover the cost of selection by those staff for whom a final salary scheme would be most appropriate i.e. those who will obtain promotions during their career in local government).

Other options

43. The consultation paper has set out a number of possible options for a new look LGPS. However, if authorities believe there are better alternatives these may also be put forward in the authority's response to the consultation paper. For example

- a hybrid CARE / final salary scheme where earnings up to a specified level (say £12,000) are subject to the CARE scheme and earnings above that level are subject to the final salary scheme
- a hybrid CARE / final salary scheme where, for example, for the first 5 years of employment a CARE scheme applies and, after 5 years, the final salary scheme applies
- a low cost scheme for those employees not joining the main LGPS e.g. a Defined Contribution (Money-Purchase) Scheme with a 0% employee contribution and a 4% employer contribution or a defined benefit scheme with a low accrual rate and a low member contribution rate.

General

44. Local government needs to attract and retain the calibre of staff required to deliver high quality, effective services. It is important to recognise the value of the pension scheme as a positive aid in the recruitment, retention and reward of staff in a job market where there is competition for skilled employees and for young people entering the workforce. The LGPS therefore needs to remain as attractive to prospective and current employees as possible in relation to both the private sector and the other main comparator public sector pension schemes whilst at the same time remaining affordable and sustainable. This ties in with the Local Government Pay and Workforce Strategy, developed by the ODPM (now the DCLG) and the Employers' Organisation for local government (now the LGE), which says that local government employers should have a pay and rewards system that is sufficient to attract, retain and motivate staff as well as being fair and affordable. As private and public sector organisations compete for the best people in a proportionately diminishing pool of labour, salary may not be the only consideration – good terms and conditions, including pensions, will play their part.

Chapter 7: Flexible and early retirement

45. The consultation paper asks which of the following five extensions to the current flexible retirement provisions employers would support:

    a. Allow scheme members to make extra contributions to offset any reduction in their pension in the case that they wish to retire early. These extra contributions could be calculated according to cost neutral buy-back factors;

    Comment: there seems no reason not to allow members to pay extra contributions to offset any reduction in their pension in the case that they wish to retire early. However, the mechanism needs to be a simple one to administer and for employees to understand. Authorities have previously supported a "how much will it cost me to buy an additional £100 p.a. of pension?" approach (see appendix 1).

    b. Extend flexible retirement from age 60 to the scheme's minimum retirement age (currently 50, but this will need to increase to 55 by 2010);

    Comment: there is no need to make this change as the scheme rules already permit flexible retirement from age 50.

    c. Remove the requirement for employees to obtain employer consent for flexible retirement;
    d. Remove the requirement for employees to take a reduction in hours or grade in order to take flexible retirement;

    *Comment on **c** and **d**: Provided it is cost neutral for employers, there appears to be no reason why employees should not be able to choose when to draw accrued benefits at any time between 50 (rising to 55 by 2010) and 75.There should be no need for employer consent or for there to be a reduction in hours or grade.*

e. Benefits accrued *after* age 65 also to be *increased* by cost-neutral uplift factors when a member elects to take payment of them after age 65.

Comment: it would seem to be appropriate to also uplift benefits accrued after age 65 as part of the move to encourage employees to work longer / draw benefits later.

Chapter 11: Employee and employer contribution rates

46. The consultation paper asks the following questions:

C4 What should the average employee contribution rate be in the new-look scheme?

Comment: This will of course depend on the type of scheme and the balance between existing and new employees. For example, looking at Option A, the total cost for existing members is estimated at 19.4% and for new members as 17.3%. If the employers' contributions were 13% (see comment on ***C6*** *below) then the employees average contribution rate would need to be 6.4% for existing employees who, initially, will form the vast majority of scheme members in the new scheme. The LGA position is that employees' contributions ought, on average, to be 7%.*

C5 Should the employee contribution rate be tiered, so that a lower contribution rate would be payable on pensionable pay below a certain cut off point? Would this depend on which Option was implemented, and if so, how and why?

Comment: Depending on the level of their earnings and career path/working pattern, an employee could under the current pensions system, due to the combination of the employee contribution rate (6%) and the level (if any) of any tax relief and reduced national insurance contributions[9]*, be better off* ***not*** *joining the local government pension scheme*[10]*. The employee could rely instead on the State Second Pension and the Pension Credit*[11]*. If the earners in a household have always had a low lifetime income, retirement saving may simply be an inappropriate activity for them because current consumption needs will be a very high proportion of their current income leaving little, if any, money to commit to savings. Under the current system, means-tested benefits will, for such people, replace a large proportion of earned income when the earner retires and the Institute of Fiscal Studies comments*[12] *that, in this situation, a reliance on government-provided retirement income may well be a rational decision. This point is recognised in paragraph 35 of Chapter 5 of Simplicity, security and choice: working and saving for retirement, in which it is pointed out that*

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[9] The cost of joining the LGPS for lower paid employees who are not paying tax or National Insurance is a full 6% of pay as they will receive no tax relief on their contributions and no reduction in NI contributions.

[10] Of course, people on lower pay may not always remain on lower pay and so a decision not to join the LGPS may turn out to only initially have been a reasonable decision. This may be particularly true in respect of women undertaking part time lower paid work whilst bringing up a family who then subsequently move to a position offering more hours/pay.

[11] For 2006/2007, single pensioners will receive a minimum income of £114.05 per week (couples will receive a minimum income of £174.05 per week)

[12] See Briefing Note 29: Retirement, Pensions and the Adequacy of Saving: A Guide to the Debate on the IFS website at http://www.ifs.org.uk/bns/bn29.pdf

"those on moderate incomes [should] identify their financial priorities and [only] save where it seems sensible to do so."

Whilst recognising the above we also appreciate that the propositions outlined in the DCLG consultation paper are a way of seeking to encourage more employees to join the Scheme, to equality proof the scheme, and to help mitigate some of the issues created by the current State pension and taxation systems. These aims, in themselves, are laudable. However, there are a number of matters which employers will also need to consider when making their response to the consultation document, as detailed below:

- *encouraging the lower paid to join the Scheme by offering a reduced contribution rate on earnings below a specified level may result in employees joining the Scheme who may not be best served by doing so, due to the impact of the Pension Credit. Until the State creates a position whereby there is no disincentive to save towards a pension, is there merit in designing a scheme to attract the lower paid to join?*

- *there is little evidence that offering employees a lower contribution rate (other than a 0% rate) on earnings below a specified level would necessarily encourage the vast majority of current non-joiners to join the scheme. The Institute for Fiscal Studies has shown[13] that the bulk of the 'unpensioned' are not paying into a pension scheme because of other urgent calls on their money (not because of the level of the contribution rate). The LGPC survey of 554 non Scheme members (see Annex 5 of LGPC Circular 130 at* http://www.lge.gov.uk/pensions/content/circulars.html*) supports the findings of the Institute of Fiscal Studies. Furthermore, the data in the tables in annex 1 of the DCLG consultation paper show that, if we were to target an average 7% employee contribution rate, this would require a contribution rate of 5.5% on earnings below £7,185 and 8.0% on earnings above that figure; or a contribution rate of 6.0% on earnings below £12,000 and 8.5% on earnings above that figure. It is difficult to see how such figures would encourage more employees to join the Scheme.*

- *would a lower contribution rate be open to age or sex discrimination claims e.g. would the majority of employees benefiting from a lower rate be women or would more young employees have a larger proportion of earnings below the lower earnings contribution point than older employees?*

- *offering a lower contribution rate on earnings below a specified level would be of some benefit to lower paid staff. However, the Local Government Pay Commission commented at paragraph 112 of their report that "those at the bottom of the earnings distribution [in local government] are better paid, in general, than their whole economy counterparts while those at the top of the distribution are lower paid than their counterparts." Offering a lower contribution rate to lower paid staff, thereby further increasing the overall remuneration package for lower paid staff, might ultimately require a re-balancing of the pay element of the overall remuneration package for higher paid staff.*

[13] Partnership in Pensions; an Assessment: Institute for Fiscal Studies, 1999.

- *if, as a result of a lower contribution rate on earnings below a specified level, the overall contribution rate for higher paid staff has to increase (in consequence of more of the present non-joining lower paid staff deciding to join), this could lead to salary drift which would, of course, lead to increased employer costs – not only in terms of additional salary but also in terms of the additional pension and national insurance on-costs on that additional salary*

- *decisions would need to be taken as to whether the pay of employees with multiple jobs should be aggregated to determine which contribution band their pay fell into. Morally, a person with the same overall income from two local government jobs should pay the same contributions as a person receiving the same income from one job. However, difficulties arise if a person has more than one job and these are with different employers (in the same Fund or in different Funds). How would one ensure that the pay figures were aggregated?*

- *around one third of local government employees do not presently join the LGPS. These tend to be the lower paid workers and younger members of staff. If these are encouraged to join the LGPS by a lower contribution rate on earnings below a specified level, the employer will need to meet the cost of the employer contribution to the Fund on their salary. The pay bill for these new scheme joiners will therefore increase considerably. Also, the higher contribution rates for those on higher salaries may not offset the pension cost of the increased numbers of people joining at the lower contribution rate. There will clearly be different impacts on employers depending on the make up and salaries of their workforce and on the number of current lower paid non-joiners who decide to opt into the Scheme. Employers with higher than average pay rates could gain from the consultation document proposition (because their employees would be meeting a relatively higher share of the overall pension cost) whereas the opposite would be true of employers with lower than average pay rates.*

- *also, a very minor point, but nonetheless one that would have to be dealt with if there was a move to a banded employee contribution rate, is that there would be valuation certificate and payroll implications for those employers whose contribution rates are currently expressed as a percentage of the employees' contribution rate.*

Note: the proposal in the NHS is that the NHS Pension Scheme should adopt tiered member contribution rates of 5% / 6.5% / 7.5% / 8.5% with steps at various levels of earnings (currently, the 5% rate would apply to those earning up to £15,107 and the 8.5% to those earning £100,000+). Those currently paying the 5% manual worker rate would move onto the contribution rate appropriate to their pay point.

C6 What would an affordable employer contribution rate be in the new-look scheme, in relation to the employer rates being paid by scheme employers for future service costs under the current scheme?

Comment: the LGA position is that the employer contribution rate in the new look scheme should be no more than 13% with a starting base position of a 2:1 split *between employers and employees contributions (but see next section below re cost sharing).*

Chapter 12: Future cost sharing between employers and employees

47. The consultation paper asks whether authorities would support or oppose the principle of introducing a future cost sharing mechanism into the LGPS.

48. In our view, the design of the Scheme needs to be robust and flexible enough to manage a fair sharing of relevant risk between employers and employees. The Teachers and NHS Scheme proposals will limit employer contributions to a maximum of 14%[14]. It would seem appropriate to build a "safety valve" mechanism into the LGPS to deal with the effects of changing longevity.

49. This could be achieved in the following manner:

- the new scheme will be designed with a certain anticipated level of cost in mind. This will be established by actuarial calculations which will look at the cost of the proposed benefit structure for a given profile of new entrants. The actual cost of the scheme from time to time will vary as the age distribution of members varies, and the past service position fluctuates with investment returns (and indeed would currently represent a far higher than 2:1 ratio), but these initial costings provide a benchmark 'anticipated cost' of the benefit structure, against which future changes can be measured. Let's assume that this is 20%.

- should the benchmark cost reduce below 20% in future due to long term demographic changes, then employer and employee contribution rates could be proportionately reduced.

- should the benchmark cost increase above 20% due to these same demographic changes, then the additional cost should be met by employees through either a reduction in accrual rate for future service (but not past service), or a change in NRD for future service (but not past service), or a change in the employees' contribution rate. Note: adjusting the employees' contribution rate could pick up the increasing cost of past as well as future service, but it would also have a direct effect on take home pay with possible consequences for pay negotiations.

- if the benchmark cost changes due to alteration of financial assumptions, the benefit or cost of this will fall to the employers alone.

- changes to the benchmark cost should be reassessed by GAD after every second valuation by reviewing data supplied to them on actual longevity experience across all Funds

[14] The 14% employer contribution cap in the NHS Pension Scheme would relate to risk factors that increase the value of the scheme to members (including "demographic" factors such as longevity, retention, pay progression, average retirement age, incidence of ill health retirement and changes to the way benefits are calculated under scheme rules).

Chapter 8: Two-tier ill-health pension provisions

50. We understand that the rationale for wishing to move to a two tier ill-health retirement pension arrangement is that it could be better focussed and targeted compared to the present "one size fits all" ill health retirement arrangements which may, in some cases, be putting unfair pressure on medical practitioners and local government employers and managers who are asked to make life long decisions at a single point in time.

51. Nevertheless, we are not wholly convinced of the need to change from the existing ill health regime in the LGPS. Clearly, pension benefits are only the tail end of a long process. If employers were to place greater emphasis on such good practices as health care during employment, career planning (to avoid burn out / stress), rehabilitation, retraining, and redeployment, the number of health cases leading to termination of employment and subsequent payment of pension benefits could fall. Indeed, the numbers of ill health retirements in England and Wales have fallen dramatically in recent years, from circa 35,000 in 1995/96 to 9,808 in 2001/02, 7,515 in 2002/03 and 6,784 in 2003/04.

52. Nevertheless, it seems likely that a tiered arrangement is to be introduced. Certainly, this seems to be the way other pubic sector schemes are moving.

The top-tier

53. The DCLG consultation paper indicates that the top tier would apply to those permanently unable to undertake any gainful or regular employment and would provide a benefit based on actual membership plus 50% of notional membership between the date of leaving and age 65. Whilst this would provide a reasonable benefit to those who fall into the top tier, we would draw two matters to the attention of employers. Firstly, employees who are aged 59 years 122 days or older would, even in the top tier, receive less benefits than under the current system e.g. an employee aged 59 years and 122 days would, under the current Scheme, get 6 2/3 years enhancement; whilst under the proposed top tier of the new scheme they would get 3 1/3 years enhancement. Secondly, a top tier enhancement of 50% of notional membership between the date of leaving and age 65 could prove expensive to a small employer with few scheme members if, unfortunately, such an employer has to retire a younger person under the top tier arrangement and is not in a 'pool' of employers when the employer's contribution rate is assessed at the triennial valuation.

54. The consultation paper says that consideration could be given as to whether local authority employers should have the facility to award more than 50% enhancement in individual cases where more generous awards can be justified on compassionate grounds. The LGPC Working Party feels that this could introduce inconsistency of approach across the country within what is meant to be a national scheme and should, therefore not be supported.

The second tier

55. The second tier would provide an unenhanced pension to those incapable of performing the duties of their own job but who are capable of undertaking other "regular employment". The consultation paper does not specify whether the definition for the second tier will extend to incapable of performing the duties of their own job *and any available comparable employment with the employer* but who are capable of undertaking other "regular employment".

56. The consultation paper suggests that the second tier could be broken down into a set of sub-tiers, each offering a different level of benefit (to reflect that across employees falling within the second tier there would be a wide range of incapacities and prospective job opportunities). The view of the LGPC is that the scheme should be kept as simple as possible and that more than two tiers should be avoided.

57. A drawback of having multiple tiers is that it could lead to numerous appeals from members seeking to be placed into a higher tier in order to increase the amount of enhancement they are awarded, thereby increasing the administrative and appeal burden. Having only two tiers might make matters clearer as there would be an obvious difference between those tiers i.e. to get into the top tier the member would have to be very seriously incapacitated and permanently unable to undertake any gainful or regular employment.

Review of ill health awards

58. The consultation paper discusses the possibility of reviewing ill health pensions and adjusting them in the light of changes in a person's circumstances. We would argue that, for the sake of consistency of application and ease of administration, a burdensome review arrangement should be avoided, particularly as it is anticipated that the majority of ill health retirees would fall into the second tier (no enhancement of benefits). This would mean that once a level of benefit had been awarded, it would remain in payment for life.

59. Instigating a review of those in the top-tier who, at leaving, were deemed by the appropriate medical adviser to be so ill as to be incapable until at least age 65 of any gainful or regular employment seems to be somewhat excessive i.e. the administrative burden and the anxiety caused, relative to the number of cases where a person would fall out of the first tier definition, seems unwarranted. Furthermore, if the enhanced element is to be withdrawn, a mechanism to do so would need to be found that complies with paragraph 2(4) of Schedule 28 to the Finance Act 2004 (possibly by paying the enhancement as a separate pension to the basic pension).

Definition of capable of undertaking other regular employment

60. Although chapter 8 of the consultation paper does not explicitly say so, we assume that "permanently" incapable will, as now, mean permanently incapable until age 65.

61. The consultation paper asks for views on how to define whether someone is capable of undertaking other "regular employment". The paper provides an example from the Firefighters' Pension Scheme which defines regular employment as being "not less than 30 hours per week on average over a twelve month period". Such a definition has a number of drawbacks e.g.

- to cater for those employees who are part time at the date of retirement, such wording would need to be tweaked to "not less than 30 hours per week, or the number of contractual hours at the date of ill health retirement if less, on average over a twelve month period"
- more importantly, a Chief Executive retiring on health grounds might be capable of regularly sitting as a model for the art class for 30 hours per week. This might be "regular employment" but would it really constitute "gainful employment"?

62. It might, therefore be better to consider linking the definition of "regular employment" to the degree to which the person's ill health affects their earnings capacity i.e. to fall into the top-tier, the question could be "is their ill health likely to permanently (to age 65) restrict their earnings capacity to below a specified percentage of their current earnings (say to below 25%)?

Chapter 13: Existing scheme members in new-look scheme

63. To ensure a simplified, single framework for the future, all employees who are contributing to the current LGPS on the date the new scheme commences could be automatically transferred to the new scheme[15]. However, as recognised in chapter 13 of the consultation document, there are no easy ways to achieve the conversion of accrued rights into membership in the new scheme. From an employer perspective, any transfer terms ought to be on a cost neutral basis.

64. Of course, if Option A (i.e. retaining a tweaked version of the current Scheme) was taken forward, there would be no conversion issues to address. From that specific point of view, Option A is the simplest option.

65. Another simple alternative is to retain Option A for existing Scheme members but give them the right to opt to move into whatever other new scheme is set up on what would, for employers, be a cost neutral basis. In such a scenario, existing members can then make a personal choice and, if they decide to move to the new scheme for future service, they can decide whether to transfer their accrued benefits into the new scheme on the available transfer terms or keep their accrued rights in Scheme A as a deferred benefit. A break of, say, more than a month and a day[16] would preclude a person from continued membership in Option A.

[15] Deferred and pensioner members, at the date the new scheme commences, would retain benefits in the current LGPS.

[16] The Teachers and NHS Pension Schemes are looking at keeping the right to join the "old" scheme if the break is less than 5 years but this is because, unlike in the LGPS, the "old" scheme will retain a normal retirement date of 60, not 65.

Chapter 14: Scope of scheme employers' discretions

66. The consultation paper says that several administering authorities, in the light of their relatively more beneficial funding position, have suggested that specific optional scope could be provided in the new-look Scheme for LGPS employers. This would allow employers to opt to provide specific, additional benefits over and above the national benefit package for the Scheme.

67. The LGPC is not supportive of this as it believes one of the strengths of the Scheme is that it is a national Scheme and a standard benefit package should be retained.

And finally

68. At appendix 1 to this Circular you will find a table of responses from employers to the questionnaire included in LGPC Circular 168 of January 2005. The table shows the numbers of employers at that time who agreed (or disagreed) with statements in relation to the proposals set out in the ODPM consultation paper *Facing the future –Principles and propositions for an affordable and sustainable Local Government Pension Scheme in England and Wales*.The table has been included as an appendix to this Circular as we thought the views expressed last year might be of interest to authorities when considering their response to the current DCLG consultation paper.

69. At appendix 2 to this Circular is a brief questionnaire which we would be grateful if LGPS employers in England and Wales could complete and return by **21 September 2006** to help us prepare a response to the DCLG consultation paper.

Actions for administering authorities in England and Wales

70. Administering authorities in England and Wales are asked to copy this Circular to employers in their Fund (other than to Local Authorities to whom this Circular has been sent direct), or bring the Circular to the attention of employers by directing them to the Circular on the LGPC website at http://www.lge.gov.uk/pensions/content/circulars.html or, in some other way, bring the main messages in this Circular to the attention of the employers in their Fund.

Terry Edwards
Head of Pensions
August 2006

Appendix 1

Based on the views presented in Annex B please indicate your agreement or otherwise with the following key points being made in the EO/LGPC draft response to the Green Papers		
	Agree	Disagree
Q.1. The Scheme forms part of the overall remuneration package and there is a balance to be struck within that overall package between pay and pensions (deferred pay) **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	148 16 23 14 27	0 0 1 0 0
Q.2. The LGPS should have a benefit structure broadly in line with that in other comparator public sector schemes **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	143 16 24 13 25	5 0 0 1 2
Q.3. With regard to the cost of the Scheme, please indicate which of the three options below you most support. Within your preferred option please indicate your preferred sub-option (where appropriate):		

Q.3. Option 1 We are supportive of targeting an employer contribution rate in respect of future service accrual that is equivalent to that under the current Scheme (after the effects of the removal of the 85 year rule from the current Scheme have been taken into account); or **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	75 11 15 8 10	
Q.3. Option 2 We are cautious about targeting an employer contribution rate for future service accrual that is equivalent to that under the current Scheme (after the effects of the removal of the 85 year rule from the current Scheme have been taken into account). Targeting a slightly lower employer rate (of, say, a reduction of 1%) would be justified, would be more acceptable to employers (and to Council tax payers) and would be more likely to ensure the longer term affordability and sustainability of the Scheme. **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies** This could be achieved by:	66 5 9 6 14	
Q.3. Sub-Option 2A: reducing the value of the benefits package outlined in the Green Paper by a target figure of 1% whilst retaining an average employee contribution rate of 7%; or **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	23 3 4 1 4	
Q.3. Sub-Option 2B: retaining the value of the benefits package outlined in the Green Paper but increasing the average employee contribution rate by 1% (i.e. from 7% to 8%) **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	42 2 5 5 10	

Q.3. Option 3 As per option 2 but with a larger reduction in employer contribution to be achieved via: **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	4 0 0 0 **6**	
Q.3. Sub-Option 3A: target a larger reduction in the benefit package (to save more than 1%) **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	1 0 0 0 3	
Q.3. Sub-Option 3B: target a larger increase in the employee contribution rate (beyond 8%) **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	2 0 0 0 3	
Q.3. Sub-Option 3C: target both a larger increase in the employee contribution rate and a larger reduction in benefits **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	1 0 0 0 0	
Q.4. A new-look LGPS should be a final salary Defined Benefit scheme. **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	131 16 24 14 25	15 0 0 0 2
This should be open to:		
a) employees **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc**	130 16 24	0 0 0

Town and Parish Councils **Admitted Bodies**	14 25	0 0
b) councillors **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	 100 12 n/a 7 n/a	 26 2 n/a 7 n/a
There should be no Defined Contribution scheme as a top-up to the main scheme **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	 99 11 15 9 16	 31 4 6 5 7
There should be no Defined Contribution scheme as an alternative to the main scheme **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	 114 12 19 7 20	 13 2 2 3 4
There should be no facility for members to purchase added years **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	 61 7 7 2 11	 58 7 14 9 13
There should be a facility for members to purchase additional scheme benefits based on an actuarially set charge for purchasing £100 of annual pension **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	 109 13 20 9 19	 23 2 1 1 6
Q.7. The employee/councillor contribution rate should be the same for all scheme members (not a graded/banded contribution rate dependent on the level of earnings) **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	 129 14 23 12 21	 15 2 1 2 6

Q.9. The accrual rate per year of membership and the commutation rate should be no less favourable than the other main comparator public sector pension schemes **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	140 16 23 14 26	1 0 1 0 1
Q.10. The Scheme should have a Scheme Retirement Age (SRA) of 65. Benefits taken before SRA should be subject to an actuarial reduction, other than in the case of ill health retirement, whilst benefits drawn after SRA should be subject to an actuarial increase **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	131 15 21 14 24	11 1 3 0 3
Q.13. Benefits payable on redundancy/efficiency retirement prior to Scheme Retirement Age (SRA) should be payable at the employee's choice, at an actuarially reduced rate. **Local authorities (1 authority agrees for efficiency but disagrees for redundancy)** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	125 15 23 13 25	14 1 1 1 2
• The employer should have the option to waive or reduce the actuarial reduction at the employer's cost **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	118 14 22 10 22	9 2 2 3 4
Q.14. We are in favour of a two tier ill health system ***[If you disagree with the above statement, go to question 15]*** **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	118 15 18 8 19	23 1 5 5 6

• We agree that the benefits of those who are certified as being permanently incapable of any gainful employment should be based on their prospective service to age 65 **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	95 12 15 7 19	15 (but 2 support 50% enhancement) 1 2 1 1
With regard to the second tier, please tick the box which represents your favoured option:		
Q.14. Option 1 We are generally in favour of a second tier of un-enhanced ill health retirement benefits payable for life, but we are not convinced of the equity of a review system; or **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	48 4 6 2 3	
Q.14. Option 2 We are generally in favour of a second tier of un-enhanced ill health retirement benefits but believe these should only be payable for a limited period of time, say 2 years; or **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	47 6 10 2 13	
Q.14. Option 3 We believe there should be no second tier of ill health retirement benefits. Instead, the member would be provided with a deferred pension and the employer could make a one off lump sum termination payment **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	19 4 1 2 3	
Q.15. The death in service lump sum should be 3 times final pensionable pay **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc**	133 15 22	**9** 1 2

Town and Parish Councils **Admitted Bodies**	10 26	4 1
Q.16. There should be no short term survivor pensions **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	81 12 12 3 16	58 4 12 9 10
Q.17. We are supportive of the introduction of partners' pensions (particularly if, as seems likely, the other public sector schemes are moving towards their introduction) **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	139 16 22 12 25	6 0 2 1 1
• But we feel there are a number of equity issues surrounding the proposals contained in the Green Paper which need to be considered **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	130 14 20 10 23	4 0 0 0 1
Q.18. A surviving spouse's/partner's pension should not be reduced if there is a large age differential between the couple **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	124 16 17 8 23	16 0 7 4 4
Q.20. We are not in favour of adjusting a person's period of accrued membership if they move between jobs in local government, or if they move into a different salary band (if tiered employee contributions are introduced), in order to take account of the differences in pay levels **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	133 16 23 13 25	4 0 1 1 2
Q.22. Transferring existing scheme members from the current Scheme to a new-look LGPS has merit, as all contributors would then be in a single Scheme, but only if the service conversion is workable, fair and equitable **Local authorities**	120	19

Other scheduled bodies **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	15 21 14 27	1 3 0 0
Q.25. If you do not agree with the first statement in **Q.4.** above (i.e. the LGPS should be a final salary Defined Benefit scheme for both employees and councillors) what alternative would you prefer?		
• A final salary Defined Benefit scheme for employees plus a career average Defined Benefit scheme for councillors, or **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	 16	
• A career average Defined Benefit scheme for all employees and councillors, or **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	 8 1	
• Defined Contribution scheme for all employees and councillors, or **Local authorities** **Other scheduled bodies** **FE/HE/Universities/Schools, etc** **Town and Parish Councils** **Admitted Bodies**	 2	
• Other (please specify) DC for employees / nothing for councillors **Local authorities** Final salary up to £50k salary, DC on excess **Local authorities** Career average for employees only **Local authorities**	 1 1 1	

Appendix 2

Question	Answer	
	Yes	**No**
1. Which new scheme option do you support?		
A: Updated current final salary scheme (1/80th accrual plus 3/80ths lump sum) with RPI revaluation after leaving		
B: New 1/60th final salary scheme (and lump sum available by commutation) with RPI revaluation after leaving.		
C1: CARE scheme with 1.85% accrual and RPI revaluation both during employment and after leaving (with lump sum available by commutation)		
C2: CARE scheme with 1.65% accrual and RPI + 1.5% revaluation during employment and RPI revaluation after leaving (with lump sum available by commutation)		
D: a new hybrid CARE / final salary arrangement		
Other - please specify:		
2. Which of the extensions to the flexible retirement provisions would you support?		
a. Allow scheme members to make extra contributions to offset any reduction in their pension in the case that they wish to retire early. These extra contributions could be calculated according to cost neutral buy-back factors;		
b. Extend flexible retirement from age 60 to the scheme's minimum retirement age (currently 50, but this will need to increase to 55 by 2010); *Comment: there is no need to make this change as the scheme rules already permit flexible retirement from age 50.*	N/A	N/A
c. Remove the requirement for employees to obtain employer consent for flexible retirement;		
d. Remove the requirement for employees to take a reduction in hours or grade in order to take flexible retirement;		
e. Benefits accrued *after* age 65 also to be *increased* by cost-neutral uplift factors when a member elects to take payment of them after age 65.		
3. Do you agree that in the initial design of the new-look LGPS the employers' contribution rate for future service should be no more than 13%?		
If not, what percentage rate would you wish to target? Please specify:		
4. Do you agree that in the initial design of the new-look LGPS the average employees' contribution rate should be targeted at 7%?		
If not, what percentage rate would you wish to target? Please specify:		
5. Do you support a tiered employee contribution rate?		
If so, do you think the tier should be set at £7185 (the basic rate tax figure)		
Or at £12,000		
Or at some other rate (please specify):		
6. Do you agree that there should be a cost sharing mechanism built into the LGPS?		
If so:		

Do you agree that this should be as set out in this Circular (i.e. Circular 189)?		
Or by some other mechanism (please specify):		
Do you agree that this should be assessed by the Government Actuary following every second valuation and based on all Funds experience?		
What size increase / decrease in the demographic assumptions should trigger a review – please specify (e.g. changes which, cumulatively, would change the underlying employee contribution by at least 0.5%)		
Should any resulting change in cost be met by:		
a. a change in the accrual rate for future scheme membership (but not accrued membership)?		
b. a change in the normal retirement date for future scheme membership (but not accrued membership)?		
c. a change in the employees' contribution rate?		
6. Do you support a move to a two-tier ill health arrangement?		
If yes:		
Should ill health enhancement at the top tier be based on 50% of prospective membership between leaving and age 65?		
If not, what should it be based on (please specify)		
Do you agree there should be no enhancement at the second tier?		
Do you support a review mechanism for the top tier?		
Do you support a review mechanism for the second tier?		
Do you think there should be more than two tiers?		
If so, how many (please specify)		
Should any movement into the top-tier be allowed?		
Should members be able to apply for ill health retirement whilst they are still employed (rather than the current system of the employer terminating employment and then deciding whether ill health benefits are / are not payable)?		
Do you agree that to fall within the top tier an employee's earnings capacity should be reduced by more than a specified percentage?		
If so, should that percentage be a 75% reduction?		
Or some other percentage (please specify):		
If not, how do you think the assessment of whether or not an employee falls into the top-tier should be assessed (please specify):		
7. Do you agree that cohabitees' pensions should be introduced into the new-look LGPS?		
If so, should this be from		
a. the beginning of the new-look scheme?		
b. the date the "law of the land" is changed to recognise cohabitees?		
8. Do you agree that spouse's pensions should accrue at a specified rate (e.g. $1/160^{th}$) – see paragraph 12 of this Circular		

9. If Option A (retention of the existing Scheme) is not the scheme taken forward by the DCLG, do you agree that existing scheme members should be compulsorily moved into the new look scheme for future service?		
If yes, which of the options set out in the consultation paper would you support in relation to existing members accrued service		
a. give all existing members at 31 March 2008 an actuarially equivalent period of service in the new-look Scheme, according to a formula to be set by the Government Actuary?		
b. give existing scheme members at 31 March 2008 more credit in the new-look scheme than they would receive under (a)?		
c. treat all accrued service of existing scheme members at 31 March 2008 as a benefit to be payable on retirement , under terms of the current scheme, based on the final salary at retirement?		
d. Other – please specify:		
10. Do you agree with the LGPC position that there should be no facility for individual employers to opt to provide specific additional benefits (above the national core benefits)?		

Signed ……………………………………………………………… Date ……………………..

Name (in capitals) ………………………………………………………………………………

Position …………………………………………………………………………………………

Name of employer ………………………………………………………………………………

Please complete and return this questionnaire to LGPC, Local Government Employers, Local Government House, Smith Square, London, SW1P 3HZ by **21 September 2006**.

Appendix 3

Comparison of Option B with Option C1

In order to try to get across the difference between final salary and CARE options we have prepared some illustrative comparative figures for Options B and C1.

The table below illustrates a person who joins with a salary of £20,000. It shows what the accrued pension would be on leaving under both the final salary (Option B) and CARE (Option C1) and illustrates the redistributive effect of moving to CARE. There are three salary profiles - one increasing in line with inflation; one increasing at an annual rate of 1.5% above Inflation; and one increasing at 3% above inflation. In working out the CARE salary it has been assumed that the increases are uniform over the period of membership.

	Salary - 0% above inflation				Salary - 1.5% above inflation				Salary - 3% above inflation			
Years of Service at Date of Leaving	Salary (in real terms)	Average Salary for CARE	Final Salary Pension (1/60th)	CARE Pension (1.85%)	Salary (in real terms)	Average Salary for CARE	Final Salary Pension (1/60th)	CARE Pension (1.85%)	Salary (in real terms)	Average Salary for CARE	Final Salary Pension (1/60th)	CARE Pension (1.85%)
0	20,000	20,000	-	-	20,000	20,000	-	-	20,000	20,000	-	-
5	20,000	20,000	1,667	1,850	21,546	20,773	1,795	1,921	23,185	21,593	1,932	1,997
10	20,000	20,000	3,333	3,700	23,211	21,605	3,868	3,997	26,878	23,439	4,480	4,336
15	20,000	20,000	5,000	5,550	25,005	22,502	6,251	6,244	31,159	25,580	7,790	7,098
20	20,000	20,000	6,667	7,400	26,937	23,469	8,979	8,683	36,122	28,061	12,041	10,383
25	20,000	20,000	8,333	9,250	29,019	24,509	12,091	11,336	41,876	30,938	17,448	14,309
30	20,000	20,000	10,000	11,100	31,262	25,631	15,631	14,225	48,545	34,273	24,273	19,021
35	20,000	20,000	11,667	12,950	33,678	26,839	19,645	17,378	56,277	38,139	32,828	24,695
40	20,000	20,000	13,333	14,800	36,280	28,140	24,187	20,824	65,241	42,620	43,494	31,539

As can be seen from the table:

- if salary increases are uniform and equal to inflation then the CARE pension under Option C1 is always the better option.
- if salary increases are uniform and 1.5% above inflation then the CARE pension under Option C1 is better for members whose service is less than 15 years
- if salary increases are uniform and 3% above inflation then the CARE pension under Option C1 is better for members whose service is less than around 7 years

What this means from the employers' point of view is that the C1 CARE option could cost more than the final salary option if there is an increasing trend towards shorter periods of working for local government or if salary increases outstrip inflation by some margin. The opposite of these is also obviously true.

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