

T B J Crossley
Head of Local Government and
Firefighters' Pension Schemes

Addressees at Annex B

Zone 2/F8
Ashdown House
123 Victoria Street
London SW1E 6DE

Direct line: 020 7944 5970
Fax: 020 7944 6019

Web sites: www.communities.gov.uk

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Dear Colleagues

LOCAL GOVERNMENT PENSION SCHEME

With Ministers' agreement, I enclose at Annex A a copy of a Statement made to Parliament on 23 November by Phil Woolas MP, Minister for Local Government about the reforms proposed for the Local Government Pension Scheme (the LGPS) in England and Wales.

The Government's overall objectives for the LGPS are set out in the Statement which itself marks the start, of the statutory consultation exercise, to introduce a regulatory framework to provide a new-look LGPS with effect from 1 April 2008.

The Minister's Statement outlines several consistent themes which have underpinned the reform timetable for the LGPS since first announced on 2 December 2005 to Parliament, and subsequently in the department's letter of 5 December to all LGPS interests in England and Wales.

This letter, which marks the start of the necessary statutory consultation exercise, provides information about the form and content of the draft regulations package which will be circulated for comment early next month. Consultees may wish, therefore, to consider the outline elements of the new-look Scheme benefit package set out below, in advance of the actual draft statutory instrument's circulation.

Objectives for reform

The Government has undertaken to ensure that measures to reform the Scheme are affordable, viable and fair to the taxpayers who guarantee the Scheme's statutory pension promise. Ministers have confirmed that it remains essential that the Scheme should also be as flexible and accessible as possible, for both employees and employers, so that it can provide a modern, equality-proofed range of defined benefits, both now and in the future.

It remains a significant objective also to achieve an equitable balance between the level of pension benefits provided by the scheme, and the actual cost of provision from all stakeholders' points of view, including tax payers.

The Statement affirms the Government's intentions to maintain stability in the costs of the Scheme, and to ensure an equitable benefit/cost balance between all stakeholders. Throughout the LGPS reforms process the Government's intention has been to ensure that no additional costs are imposed on council tax payers. It is intended, therefore, to establish an appropriate, statutory-based mechanism for sharing future cost pressures in order to minimise any adverse effects on council tax levels. This is to be in place within the Scheme's statutory framework by March 2009 and so in time to operationally influence, and be influenced by, the 2010 Scheme actuarial valuation exercise. The combined outcome of this important new arrangement will then be taken into account in assessing the results of the valuation exercise, and the eventual outcomes on new Scheme contribution rates, from April 2011.

Elements of a new-look Scheme

An analysis of the responses received to the consultation exercise, *Where Next? – options for a new-look Local Government Pension Scheme in England and Wales*, has now been completed. Overall, the responses affirmed a clear preference, from all Scheme interests, for the retention of a final salary pension benefit package, which is viable, affordable, and fair to Scheme members and taxpayers.

Ministers have concluded, therefore, that such a package should form the basis of the new-look LGPS for introduction in April 2008. There was solid support also for several affordable benefit changes as suggested in the consultation document. In other areas, there was a more diverse range of comments. The responses have been analysed and can be viewed on www.communities.gov.uk/lgps.

To ensure compliance, therefore, with the policy intentions set out in the Parliamentary Statement, and taking account of the responses received, Ministers have agreed to a new-look LGPS benefit package for statutory consultation purposes at this stage.

The following main elements being proposed now are: -

- **final salary pension benefits to be based on 1/60th of salary for each year of pensionable service, with the flexible option to commute pension at the rate of £1 of annual pension for £12 of lump sum up to a maximum tax free lump sum of 25% of the capital value of accrued benefit rights at the date of retirement;**
- **a normal Pension Age (NPA) of 65 for release of unreduced benefits;**
- **earliest age for release of pension to be 55 by 2010 for current members, except on grounds of ill-health;**
- **earliest age for release of pension to be 55 for new joiners from 1 April 2008, except on grounds of ill health;**
- **augmentation of membership/benefits on an objectively justified basis;**

- **the better of the last year's whole time equivalent salary or the 're-valued (in line with the Retail Price Index (RPI)) average of the best three consecutive years' salary in the last ten years of service;**
- **survivor benefits for life, payable to spouses, civil partners and "nominated" dependent partners (opposite and same sex) at a 1/160th accrual;**
- **survivor benefits payable to children at a maximum accrual of 1/160th;**
- **revised ill-health retirement package with no review system, to provide a higher level of benefits for total incapacity, and with different levels of benefits to recognise lesser incapacities;**
- **a death in service tax free lump sum of 3 times salary;**
- **scope for a post-retirement lump sum death benefit, up to a maximum of 10 years;**
- **phased retirement arrangements which would allow LGPS members, under specified circumstances, to draw down some, or all, of their accrued pension rights from the scheme while still continuing to work;**
- **tiered employee contribution rates with 5.5% payable on the first £12,000 of pensionable pay, and 7.5% to be paid on the excess over £12,000, estimated on current membership to produce an average rate of 6.3%;**
- **a facility for Scheme members to purchase up to a maximum £5,000 of additional annual pension; and**
- **a facility for Scheme members to contribute towards their pension in conjunction with external AVC providers.**

III Health benefits

Consultees may find it helpful to have more details about the specific nature of the proposals for augmentation of membership when a member retires on grounds of ill health and which have been built into the costing profile of the consultation package.

There are now three proposed elements: -

- **For those Scheme members judged to be unable to perform local government employment duties but able immediately to undertake gainful employment – accrued rights only;**
- **For those unable to undertake gainful employment on cessation, but likely to be able to do so before normal retirement age –**

accrued rights and augmentation of 25% of prospective service to normal retirement age; and

- **For those unable to undertake gainful employment before normal retirement age – accrued rights and augmentation of 50% of prospective service to normal retirement age**

In the consultation period, interested parties may wish to consider the elements proposed here, being mindful of the fact that any adjustments to any of the elements set out above will have a direct effect on the cost of provision. Consultees may also have views on the most appropriate way of defining the term “gainful employment” in the LGPS Regulations 2007 which will set out the benefit structure.

More details will be forthcoming when the draft regulations are circulated next month as part of the consultation exercise, programmed to extend to the end of February 2007.

Scheme costings

Consultees will wish to know that the benefit consultation package has been reviewed in terms of existing members and new entrant members by the Government’s Actuary’s Department, using the same methodology as their benchmark costings for the Consultation Document. The draft regulatory impact analysis statement will provide full details of the costings but it may be helpful, initially, for Scheme interests to see at this point the headline costings for the changes to basic scheme benefits included within the above package. Savings achieved, following the rule of 85, have been factored into the exercise. The costings are as follows and provide an average existing member and new entrant employer benchmark cost of 13.2% (plus the cost of transitional protection post-2013).

	<u>Existing Members</u>	<u>New Entrants</u>
Total cost	20.5%	18.5%
Less Employee rate average	6.3%	6.3%
	<u>14.2%</u>	<u>12.2%</u>

These costing will provide a starting point from which consultees may choose to vary any of the benefit elements of the package now put forward for analysis and comment within the consultation period.

Protection arrangements for existing Scheme members

Within the new-look LGPS benefits package, arrangements will be provided which not only protect fully the accrued rights for all existing Scheme members, but also the protections provided in the current LGPS framework by the Local Government Pension Scheme (Amendment) (No 2) Regulations 2006 for eligible Scheme members, following the final removal of the rule of 85 from the Scheme with effect from 1 October 2006. The new factors to be used in cases of early payment pension from 1 October 2006 will also be kept under review to take account of potential further improvements in life expectancy.

Scheme Updates

Pension Changes is an information leaflet produced by Communities and Local Government and is now available to download from our website www.communities.gov.uk/lgps. To ensure as broad a response as possible from the membership, it would be helpful if the above link could be placed on all stakeholders' own web pages.

Regular Scheme updates produced by the Department will be available via the new LGPS website. The site is designed to focus all relevant information regarding the new-look Scheme in one easy-to-navigate location. The website features documents specific to the new-look Scheme, as well as offering the opportunity to register for publications and to take part in the interactive forum to be moderated by officials in LGFPS.

Policy Review Group

To assist in the on-going monitoring of the Scheme's regulatory and policy development, Ministers have agreed that a policy review group of key interested parties should be established to focus on strategic issues and establish common ground among stakeholders as a basis for co-operative decision-making on Scheme developments and future changes, changes in Scheme demographics and new cost-sharing arrangements. The work of the group will complement the substantial statutory and non-statutory consultation arrangements which already exist within the current regulatory framework for the Scheme. Arrangements to establish the Group will begin shortly.

One of the first issues the Group may wish to consider, as well as future cost-sharing mechanisms, is the policy development process surrounding the new Pensions Bill and, in particular, the relationship of State retirement age reforms to occupational schemes, such as the LGPS. It is important that the Scheme begins to deal with this issue rather than, as DWP has spelled out in connection with State benefits today, passing an unsustainable burden on the children and grand-children of current members.

Pension arrangements for elected members

There are no plans to amend the current arrangements, in the LGPS framework, which apply to elected members of local authorities in England and Wales.

Next Steps

The new-look Scheme is programmed to be fully operational from 1 April 2008. To achieve this in a satisfactory and informed way, the Government's timetable and programme of reform requires the new regulations to be in place for 1 April 2007. Accordingly, draft regulations which will set out the proposed benefit package for the Scheme will be circulated next month to interested parties in England and Wales to reflect the terms of the Government's Statement, and will set out in more detail the actual draft regulatory framework seen as necessary to give full effect to the new Scheme. A draft regulatory impact analysis will accompany the draft regulations to explain the policy intentions of the proposals, their costs and benefits and other impacts.

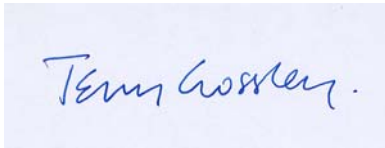
These new benefit provisions will be followed by a separate set of draft regulations dealing with the administration and process aspects of the new Scheme and which have a similar implementation timetable. It is intended that these draft provisions will be considered in

detail with interested parties during the consultation period. Arrangements will be made to begin that process in due course.

Contacts

For enquiries on the content of this letter and the Ministerial Statement, please e-mail Charlotte Hine-Haycock Charlotte.Hine-Haycock@communities.gsi.gov.uk or Nicola Rochester Nicola.Rochester@communities.gsi.gov.uk or telephone 020 7944 6016 in the first instance.

For enquiries on the proposed consultation exercise on new administration regulations please e-mail Margaret Dunleavy Margaret.Dunleavy@communities.gsi.gov.uk or telephone 020 7944 6012 in the first instance.

A rectangular box containing a handwritten signature in blue ink that reads "T B J Crossley".

T B J Crossley