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Leicestershire County Council

EMPLOYMENT COMMITTEE – 8 DECEMBER 2011

REPORT OF THE DIRECTOR OF CORPORATE RESOURCES

CONSULTATION ON POSSIBLE CHANGES TO THE LOCAL GOVERNMENT PENSION SCHEME (LGPS)

Purpose of the Report

1. To seek Committee approval in respect of the authority's proposed response to a consultation being run by the Department of Communities and Local Government (CLG) in respect of proposed increases to employee contribution rates and changes to scheme accrual rates, effective from 1st April 2012. The CLG consultation document is included as Appendix A.

Background

2. Soon after being elected the Government asked Lord Hutton to undertake a review of Public Sector Pensions and his final report, which the Government fully endorsed, was issued in March 2011. It has been stated that the required changes highlighted by Lord Hutton's review would be implemented during the term of this Parliament and the introduction date for new public sector schemes is expected to be 1st April 2015.

3. Separate to the Hutton review was a requirement by the Government to make short term savings within each separate public sector scheme, with the saving for the LGPS being £900m by the 2014/15 financial year. This saving equates to an average rise of 3.2% in employee contributions, from the current average of 6.4% across the LGPS.

4. The LGPS is the only public sector pension scheme which is 'funded' – in other words, it has assets which are invested in such a way as to pay for future benefits. Given this 'special' feature of the LGPS, the Government allowed the CLG to consider other options that would make the required short-term savings without the need to increase the contribution rate so much.

5. It is particularly difficult to produce the required savings within the LGPS through only employee contribution increases for two reasons – the first is that the average contribution rate is already quite high at 6.4% (but varying between 5.5% and 7.5% based on full time equivalent salary), but the more meaningful issue is that the LGPS has significant numbers of relatively low earners (almost 45% of members earn below a full time equivalent salary of £19,400) and the Government has clearly stated a desire to protect the lower paid.

6. The CLG issued a consultation with two proposed approaches to making the required savings by 2014/15, and both involve a combination of changes to employee contribution rates and the rate at which a pension entitlement is accrued.

Interestingly one approach makes a total saving of £1.8bn over the three years between 2012/13 and 2014/15 (£180m in year 1, £720m in year 2 and £900m in year 3) whilst the other saves only £1.26bn over the same period (£120m in year 1, £240m in year 2 and £900m in year 3). The inescapable conclusion from this is that it is the 2014/15 saving that is considered the ultimate goal, with the two years before that being considered merely as 'staging posts' on the way to this goal.

7. In early November HM Treasury issued a report entitled 'Public Service Pensions: good pensions that last' in which it laid out a broad scheme design for the future for public sector pension schemes. Some of these design features seem to be contradictory to the proposals included in the CLG consultation – for example HM Treasury state that a 1/60th accrual rate for every year of service (in line with the current accrual rate of the LGPS) should be the standard, but both CLG proposals include a worse accrual rate than this.

8. It seems reasonable to assume that the CLG proposals take the HM Treasury report as the basis of the design of the LGPS – despite the fact that the HM Treasury report was issued a month *after* the CLG consultation – and amend it to something which is more relevant to the LGPS. One example of this would be the proposal of a worse accrual rate than 1/60th but lower employee contribution rate increases being possible as a result.

<u>Leicestershire County Council response to CLG consultation</u>

9. Leicestershire County Council fulfils two roles within the LGPS – it is an employer with over 12,500 active members (although this will reduce as more schools convert to academies) and it also administers the scheme for the 60+ employing bodies who are part of it. The proposed response to the consultation (included as appendix B) is made primarily as an employer but also touches briefly on matters that could be considered to be more administrative in nature.

10. One major aspect of the response relates to the fact that, as a new LGPS is expected from 1st April 2015, it is thought appropriate that the interim changes over the next three years – designed primarily to make the required cash savings - are a clear progression towards the new scheme. The response supports postponing changes, if this is necessary, while the 2015 scheme is agreed in order to avoid the need to makes changes that are simply reversed in a few years time.

11. Any significant increase in employee contribution rates is likely to lead to existing members opting-out of the LGPS, particularly given the economic environment that has seen disposable income come under significant pressure for many people. This brings challenges to the Fund – accelerating its maturity and decreasing available cash flow – but is also contrary to Government policy which attempts to encourage individuals to make provision for their own retirement income. The response supports a solution which reduces the possibility of opt-outs by amending accrual rates as part of the required savings, and even suggests that a larger change to accrual rates should be considered as this would mean that lower employee contribution increases would be required.

12. The Government has clearly stated that it wishes to protect the low paid from the impact of significantly higher employee contribution rates, and the CLG consultation takes this into account in the proposed new salary bandings for contribution rates.

With the LGPS having high numbers of relatively low paid membership, this protection pushes the requirement for disproportionately high employee contribution rates increases onto the modest and higher paid membership. The proposed response suggests that the contribution bandings overemphasise protection for the lower paid and that this is unfair on other members. It is probable that this overemphasis on protection is based partly on stated Government policy and partly on the fear of significant opt-outs from existing members, and it is considered inequitable that this fear should dictate contribution bandings without any real justification on the basis of the cost of providing benefits.

13. The CLG has also suggested that a technical amendment to the LGPS regulations should be made to allow employers to benefit from a reduction in their contribution rate, to the extent of the savings generated by the proposed amendments. This is not considered a sensible proposal given the significant underfunding issue within the LGPS at present – in effect such an amendment will provide some short-term relief for employers at a time that budgets are tight, but this will be at the expense of significant extra cost in the long-term. Pensions are a genuine long-term issue and should be treated as such.

Recommendation

14. The Employment Committee is recommended to approve the proposed response to the CLG consultation, included as Appendix B to this report.

Background Papers

None.

Circulation Under the Local Issues Alert Procedure

None.

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List of Appendices

Appendix A – Letter from CLG
Appendix B – County Council response to Consultation

Equal Opportunities Implications

None.