Proposal for a new Local Government Pension Scheme in Scotland

Developed by:

Scottish Local Government Pensions Advisory Group (SLOGPAG)

Consisting of representatives of:

The Scottish Executive
COSLA and
Trades Unions

July 2007

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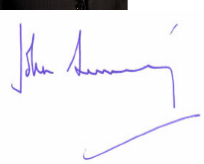
Foreword

Over the last six months, we have been working productively through a tripartite group, comprising the Scottish Executive, COSLA and Trades Unions, to develop proposals for a new Scottish Local Government Pension Scheme. This collaborative approach towards developing a new Scheme to meet Scottish needs represents a new way of working, and the advantages of this open and transparent process are recognised by each of us.

The development of the new pension scheme is part of a wider reform programme across all public service pension schemes. For the local government scheme, the reform process is partly about dealing with the increasing costs of scheme benefits, as a result of members living longer in retirement and drawing the benefits for longer, and ensuring these costs are shared fairly. However, it is also about modernising the scheme to recognise changing social factors, such as an increasing level of partners cohabiting, and changing trends in the local government workforce, such as an increase in the level of employees working part time. A new modernised scheme is required to reflect the broader employment context of its members in the 21st century and to ensure pension benefits are fair and valued by all members – full time and part time workers; managers, administrators and manual workers; and long and short serving employees alike.

We have set out proposals for the new scheme in the attached consultation document. These proposals illustrate a direction of travel and demonstrate where there is general consensus within the group as to the preferred way forward. The proposals do not, however, represent a fait accompli or a commitment by stakeholders to implement the specific benefits described. Indeed, in relation to some aspects of the new scheme, a range of potential options have been outlined to generate debate amongst all stakeholders, gauge reactions and gather views on the proposals to inform the development process. These are areas where we would particularly value your views.

Responses to this consultation exercise are welcomed from all those with an interest in the scheme; from scheme members, employers, administrating authorities and wider stakeholders on a Scottish and UK basis. These views and comments will inform final decisions on the key features of the new Local Government Pension Scheme for Scotland and we look forward to considering these in detail later in the year.

John Swinney MSP
Cabinet Secretary
for Finance and Sustainable Growth

Cllr Pat Watters
President Of COSLA

Trades Unions

SECTION 1

Executive Summary

1. A tripartite group, consisting of representatives from COSLA, Unions and the Scottish Executive, was established in November 2006 to jointly develop the new look Local Government Pension Scheme (LGPS) for Scotland. This group was tasked with developing a new Scottish LGPS in line with Scottish needs, which is fair to all, as well as being legal and affordable over the longer term.

2. The group's proposals for the new scheme are summarised in the following table:

Scheme Feature	Existing LGPS(S) pre December 2006	New LGPS(S) Proposals by 1 April 2009
Type of scheme	Defined benefit final salary scheme, with a normal retirement age of 65. Rule of 85 allowed members to retire with unreduced benefits where age and years of service together exceeded 85.	Defined benefit final salary scheme, with a normal retirement age of 65.
Accrual rates	1/80th plus lump sum (3/80^{ths})	1/60th with option to commute up to 25% of fund value into lump sum.
Death in service arrangements	A lump sum death grant of 2 times final pay.	A lump sum death grant of 3 times final pay. Short term spouses' benefits removed, but increases in partners lump sum to be provided where active, deferred or pensioner member dies.
Ill health benefits	If member permanently incapable of discharging efficiently the duties of employment, benefits paid immediately. If member has 5 or more years' service they are also entitled to enhancement of the benefits.	Two or three entry point ill health provision proposed, where members – (i) have no reasonable prospect of working before scheme normal retirement age of 65; or (ii) are likely to undertake gainful employment before age 65. Possible third tier consisting of employer grant, covering those who are likely to be capable of undertaking gainful employment within a reasonable period. Implementation of certificate of protection to cover circumstance where member takes lower salary due to ill health.
Partner pensions	Dependants benefits payable in respect of widows, widowers and civil partners at a rate of 1/160th	Dependants' benefits payable in respect of widows, widowers, civil partners, plus unmarried partners who cohabit, at rate of 1/160th

Proposal for a new Local Government Pension Scheme in Scotland

Scheme Feature	Existing LGPS(S) pre December 2006	New LGPS(S) Proposals by 1 April 2009
Flexible arrangements in the run-up to retirement	From age 50 with consent, member can reduce hours or move to a lower grade and, with consent, elect to draw the pension benefits already built up whilst still drawing salary for reduced hours/grade. Members can continue paying into the scheme to build up further benefits in the scheme. No limit on the amount of contributions, however tax relief only given on contributions up to 100% of taxable earnings.	Current provisions for flexible retirement to be retained as feature of the new Scottish LGPS. Increased flexibility through being able to draw all *or part* of occupational pension benefits without having to retire completely. In case of flexible retirement, employer consent required to reduce hours or lower grade, but employer consent to access benefits only required in respect of those under age 60. A provision to buy additional pension benefit. Cost-neutral uplift factors for benefits accrued beyond age 65, at no cost to the employer.
Minimum Pension Age (MPA)	In line with the Finance Act 2004, the MPA will change from 50 to 55 years on 6/4/2010.	All new members to have MPA of 55 years. All current members will have MPA of 55 from 6/4/2010.
Contribution rates for scheme members	General contribution rate of 6% except some existing manual employees (5%).	Working assumption is an increase in the employee contribution rate to an average of 6.3%. Employee contribution rate set at tiered variable rates, linked to pensionable pay. Potential options outlined, including a range of bands and contribution rates.
Contribution rates for employers	Employer rate varies as determined by 3-year actuarial valuations.	Contributions rates for employers and scheme members to move towards a 2:1 ratio to ensure new scheme affordable. Overall average new scheme costs estimated at 19.6%, with employee contributions at average of 6.3%. Employer contributions to make up the difference. Commitment to principle of cost sharing to ensure continuity of scheme over the long term.

3. Responses to this consultation exercise will inform final decisions on the new LGPS for Scotland. The aim is to consult on draft regulations for the new scheme by the end of 2007, with a view to agree and legislate for a new LGPS by April 2008. This will allow for implementation of the new scheme in Scotland by April 2009.

SECTION 2

SETTING THE CONTEXT

LEGISLATIVE FRAMEWORK

1. Occupational pensions is a reserved matter and therefore the responsibility of the UK Government, although Scottish Ministers have executively devolved powers to make provision by regulation for public service pension schemes in Scotland (except for the civil service and the MOD). In practice this has generally meant ensuring that scheme regulations are consistent with Scottish administrative and legal requirements. However, Ministers can choose to use executively devolved powers to make more substantial changes (which of course must comply with UK and EU law), such as the development of a Scottish solution to the removal of Rule of 85 from the Local Government Pension Scheme (LGPS). This means in essence that Scottish Ministers have the discretion to develop a LGPS specific to Scottish needs. Notwithstanding the above, changes to public service pension schemes in Scotland need to remain in line with UK and European legislation.

2. Unlike the other public service schemes in Scotland, the LGPS is a *funded* scheme. This means that the 11 fund administering authorities in Scotland are each responsible for the management and investments of the funds as well as for the administration of the scheme. In *unfunded* schemes, member benefits are paid as they arise. In unfunded schemes there are no scheme funds and therefore no investments. However, for the purposes of pension reform, the fact that the LGPS is funded is essentially immaterial. It is clearly important that authorities manage the funds effectively. Although investment performance does not impact directly on scheme members or their benefits, which are guaranteed by statute, this can impact on employers' budgets generally. On the other hand, longevity is a long-term trend that impacts directly and significantly on the costs of providing benefits, and which cannot be 'managed' in the same way. For the LGPS, as is the case for the other public service schemes, the reform process is about dealing with the increasing costs of scheme benefits, as a result of members living longer in retirement and drawing the benefits for longer. The reform process is also about modernising the scheme to recognise changing social factors, such as an increasing level of partners cohabiting, and legislative changes, such as the Disability Discrimination Act 1995.

WHY REFORM THE LGPS?

3. Ensuring the LGPS is sustainable and, thus, viable over the long term is the driving force behind the reform programme The core objective being to develop and implement a first class defined benefit occupational pension scheme for local government that is fair to all, legal and affordable over the longer term.

4. The proposals outlined in this document are made on the basis that they are affordable and provide long term financial security to the scheme. This is a particular necessity given increasing longevity. People are living longer across the whole of the UK. The General Register Office for Scotland's publication "Scotland's Population 2005" states that "…the expectation of life in Scotland has improved greatly over the last 20 years or so, increasing from 69.1 years for males and 75.4 years for females born around 1981 to 74.3 years and 79.4 years respectively for those born around 2004…improvements in life expectancy at birth are projected to continue, rising to 79.2 years for males and 83.7 years for females by 2031".

Although there is no empirical data to demonstrate how increasing longevity and changing social factors, such as health and well being in old age, will impact specifically on the LGPS membership, the trend in increasing longevity that is apparent across Scotland is likely to apply to the LGPS membership.

5. A report prepared for the Scottish Public Pension Agency (SPPA) by Hymans Robertson, Consulting Actuaries, dated December 2005 underlines this. Studies, which relate to LGPS pensioner mortality carried out in Scotland, as well as England and Wales, show that longevity is increasing across the board. Although it is widely accepted that longevity in Scotland is still behind that in England, the studies indicate that this situation is likely to change more quickly in Scotland. The report goes on to point out that as life-spans generally lengthen, pensions are paid for longer and the costs of providing pensions benefits increase. This trend may also apply to the local government workforce and therefore impact on the cost of the Scottish LGPS. These increasing costs may already be illustrated within the scheme valuations. For example, the actuarial valuation report for Fife Council Pension Fund in 2005 showed that the employer contribution rate for scheme benefit costs (excluding costs relating to past investment performance) had increased from 13.9% of payroll in 2002 to 14.2% of payroll by 2005.

6. Over time, a significant increase in the cost of the existing scheme would lead to a long-term funding gap between the cost of the scheme and the level of contributions currently made by employers and members. Under the existing arrangements these costs are directly met by increases in the employer contribution rates, while the member rate remains static, which also results in an imbalance in the way the increasing costs of benefits are met. For the LGPS to continue over the longer term there is a need to redress this imbalance and to improve the level of stability in scheme costs and employer contribution rates.

7. Increasing costs in the LGPS impacts directly on employers, but can also have an impact on council tax payers across Scotland. The reform process aims to ensure that the scheme becomes affordable and fairer across all stakeholders, including employers, scheme members and tax payers in Scotland. However, balance is also required between ensuring affordability whilst providing quality benefits to scheme members.

8. The LGPS needs to modernise to reflect the broader employment context of the local government workforce and wider scheme membership in the 21st century. The local government workforce is changing. Table 1 below (which gives examples from the Actuarial Reports for the Strathclyde and Falkirk Pension Funds for the years 2002 and 2005) illustrates the fact that nowadays there is a general trend, amongst male as well as female members of the scheme, away from the traditional full-time long-serving scheme member of the past towards a more part-time based membership.

Table 1: Sample illustration of LGPS membership over time

	2005 No. of members	% of which P/T	2002 No. of members	% of which P/T
Strathclyde				
Male	33,506	4.2	31,532	2.8
Female	52,635	37.9	43,777	35.5
Falkirk				
Male	4,150	6.8	3,917	4.7
Female	8,293	51.8	6939	46.2

9. The average age of the membership is also increasing. An example is the membership of the Fife Council Fund where the average age of scheme retirees increased from 58.1 in 2002 to 59.6 in 2005. Furthermore, an average LGPS pension of £3,800 suggests that LGPS members may have a relatively short length of service and/or there is a high proportion of members who work part time.

10. It should also be borne in mind that the LGPS covers not only local authority staff but others as well. The Regulations governing the scheme – the Local Government Pension Scheme (Scotland) Regulations 1998 – also provide access to staff of which are listed as scheme employers, such as Scottish Water and the Scottish Environment Protection Agency, as well as to the staff of bodies which are “admitted” to the various local government pension funds. These admitted bodies are very diverse, ranging from the Royal Scottish Academy of Music and Drama and the Scottish Council for the Single Homeless to the Parkhead Youth Project and Children First. There are currently over 600 admitted bodies in the LGPS and numbers increase year by year.

11. LGPS benefits should be valued by all scheme members – full time and part time workers; managers, administrators and manual workers; and long and short tenure employees alike. The new LGPS proposals outlined in this document aim to provide existing and new members with an accessible, high quality pension scheme that they will consider a valuable part of their remuneration package.

THE STORY SO FAR …..

12. The story begins in 2002, with the publication of the Department of Work and Pensions (DWP) Green Paper called ‘Simplicity, security and choice: working and saving for retirement’. That paper proposed reforming all the public sector pension schemes both to ensure their long term sustainability and to ensure people are adequately provided for in retirement. The UK Government announced in 2003 that it intended to proceed with its reform of public service pension schemes and, in 2004, the Scottish Public Pensions Agency (SPPA) consulted with stakeholders on proposed changes to the LGPS in Scotland.

13. A first consultation exercise on the LGPS dealt with certain proposed changes to the scheme in the short term, including the removal of the Rule of 85 and the raising of the minimum pension age from 50 to 55.

Facing the Future

14. At the end of 2004, SPPA issued a second consultation document on the future of the local government pension scheme called 'Facing the Future' which was aimed at securing changes to the scheme to address the affordability issues in the scheme and its future sustainability as a funded, public service pension scheme. The responses to the consultation exercise have been considered in developing the new proposals for the new LGPS in Scotland. General points made included the following:

- It was generally accepted that the age profile and general demographics of the scheme raises issues which need to be investigated further to assess the impact of these on scheme costs (i.e. if people live on average longer, then employer contribution costs are likely to increase). Changes should be identified to address these issues.

- Whilst accepting that the general principles of the new arrangements should be framed to provide consistency across the UK (and all public service schemes for that matter), there was a belief that there should be a distinctive Scottish approach to the development and implementation of the revised Scheme.

- Pensions are a fundamental part of employees' pay, terms and conditions of employment and, where appropriate, there should be consistent approaches across public service schemes. This applies to consistency with the Scottish Teachers scheme, as there are employees in both schemes working alongside each other in schools, and to the NHS scheme, for example in relation to the Joint Futures arrangements which means that NHS and Local Government employees are working side by side.

- The LGPS needs to remain as attractive to prospective and current employees as possible and should, as far as is practicable, have a benefit structure that remains competitive with the other main comparator public service pension schemes.

15. Comments and views were given on particular benefits provided through the LGPS and these comments have also been taken into account in considering specific benefits to be provided in the new LGPS proposals.

The Rule of 85

16. In 2005, Scottish Ministers announced the intention to remove the Rule of 85[1] from the scheme due to it breaching the terms of the EC Directive on equality in the workplace. The Directive deemed that provisions in the rules of occupational pension schemes which are discriminatory on age grounds were unlawful unless they fell within limited exceptions. This led to a joint statement by COSLA and the Unions on the overarching principles for both dealing with the removal of the Rule of 85 and the future development of the local government scheme.

17. The discussions and debate around the removal of the Rule of 85 took place over a number of months and the prolonged discussions on this meant that discussions on the new scheme did not commence until these were completed and a position agreed.

[1] The LGPS has a normal pension age of 65, but under the Rule of 85 members who decided to leave employment before that age and who met the requirements of the Rule could receive an unreduced pension.

18. During the Rule of 85 discussions, COSLA and the Unions held a similar view and worked together in trying to secure a Scottish solution. This was successful and in moving forward in the broader discussions on the new local government pension scheme, COSLA and the Unions have worked closely together in developing the proposals outlined in this paper. The SPPA and the Scottish Executive has continued to be involved to ensure that a full tripartite arrangement has been in place with COSLA and the Unions meeting more frequently and separately to discuss and develop the detail of the proposal.

The tripartite group

19. A tripartite group (called SLOGPAG[2]) was established in November 2006 to jointly develop the new look LGPS for Scotland. The group consisted of representatives of COSLA (on behalf of councils and administering authorities), Unions and the Scottish Executive, each of whom had specific roles and responsibilities as follows:

- The Scottish Executive had responsibility for facilitating the work of the tripartite group, liaising with Ministers, and ensuring proposals aligned with strategic policy issues in relation to local government (including financial aspects).

- The Scottish Public Pension Agency supported the wider Scottish Executive role, whilst also providing advice on regulatory issues and the broader public service pension context (including consistency with other schemes), and validation of the legal, financial and evidential elements of options. SPPA will work in conjunction with OSSE to develop the new scheme regulations.

- COSLA's key role was to discuss with unions the options for, and terms of, the new scheme, preparation of the affordability case and provision of statistical and other evidence from local authorities. COSLA also plays a role in liaising and consulting with local authorities, disseminating outcomes to local authorities, and supporting co-ordination of local authorities' dissemination of outcomes to scheme members.

- Unions had responsibility for discussions with employers the options for, and terms of, the new scheme. Unions also have a role to liaise and consult with trade union members.

- All partners took responsibility for obtaining their own legal and actuarial advice as necessary, and for liaising with appropriate UK bodies.

20. The group was tasked with developing and implementing a new Scottish LGPS that is fair to all, legal and affordable over the longer term, and it has worked proactively and productively to develop a proposal for the new LGPS in line with an agreed timetable. The focus has been to develop a specific scheme in line with Scottish needs, with the aim of launching a consultation exercise on a potential new scheme outline during July 2007. This is the latest chapter in our story so far.

21. Looking forward, the aim is to agree and legislate for a new LGPS by April 2008, which will allow for implementation of the new scheme in Scotland by April 2009. Although

[2] SLOGPAG stands for Scottish Local Government Pensions Advisory Group

this timescale dovetails with the scheme valuation process in Scotland, the main benefit of this will be that COSLA and administering authorities have sufficient time to establish appropriate systems and processes to ensure smooth implementation of the new scheme when it is introduced.

22. The tripartite group's proposals for the LGPS in Scotland are outlined in the following sections.

23. We have raised a series of questions throughout in respect of each proposal and would welcome your views on each. We would appreciate it if you could use the Consultation Response Form provided (Annex A) for your comments as this will aid our analysis of the responses received. The consultation response form is also available to download as a 'word' document to enable respondents to type in their comments and submit them electronically. This can be found on the Local Government Scheme Reforms Page in the Pensions Reform & Taxation area at www.sppa.gov.uk .

SECTION 3

NEW SCHEME PROPOSAL

1. The high level objectives for the reform of the LGPS are as follows:
   - to ensure that the scheme becomes affordable and sustainable over the longer term for employers, scheme members and tax payers;
   - to be a fairer scheme for all stakeholders; and
   - to provide quality benefits to scheme members.

2. An essential element of this proposed package of benefits is that it provides an affordable scheme for the future. The overall cost varies according to the detailed package of benefits to be put in place. However all parties are content that the broad package outlined within this proposal provides the basis of an affordable package. The cost of the proposals, for both employers and employees, is discussed in the next section. Following the consultation exercise, COSLA and the Unions will revisit this aspect with the Scottish Executive before finalisation of the scheme outline later in the year.

3. However, it is also recognised that the LGPS in Scotland has a varied and diverse membership, with a complex set of needs to be met within an affordable package. To meet these needs, the proposed new scheme has been jointly developed to ensure that it remains an attractive element of the remunerative package for local government employees, as well as providing employers with a useful tool to recruit and retain staff. The proposal has therefore been designed to fit the modern and future workforce in and around local government.

4. In working up these proposals, there has been detailed discussion and debate between all partners and a body of actuarial work undertaken to support the discussions. Due consideration was also given to how the reform process has impacted across the wider range of public service pension schemes. This ensured that relevant parallels were made, where appropriate, with the approaches taken by other public service schemes. Within Scotland this will ensure some level of consistency between the experiences of Scottish scheme members who work alongside each other, such as in the case of some members of the LGPS and the Teachers Pension Scheme. There are also benefits to providing a level of consistency with the LGPS in England and Wales, for example, ease of transferability for scheme members. These discussions have enabled the new LGPS proposals to be structured in a way that is most appropriate for the Scottish local government workforce, whilst ensuring schemes are broadly consistent across public services.

5. It should be borne in mind that the proposals in this paper represent the current position and there are some areas still under discussion. These areas are highlighted within the detailed outline for each scheme feature. This paper does not provide the definitive detail on the various benefits and features of the new scheme, rather it provides an in principle view on the direction of travel.

6. Table 2 sets out a summary of the core structure of the proposals for the new LGPS, set alongside current scheme features. Further detail on each of the proposed scheme features is outlined following the table.

Table 2: Summary of existing scheme and new scheme proposals for the LGPS

Scheme Feature	**Current LGPS(S) as of 6 October 2006**	**New LGPS(S) Proposals by 1 April 2009**
Type of scheme	Defined benefit final salary scheme, with a normal retirement age of 65. Rule of 85 allowed members to retire with unreduced benefits where age and years of service together exceeded 85.	Defined benefit final salary scheme, with a normal retirement age of 65.
Accrual rates	$1/80^{th}$ plus lump sum ($3/80^{ths}$)	$1/60^{th}$ with option to commute up to 25% of fund value into lump sum.
Death in service arrangements	A lump sum death grant of 2 times final pay.	A lump sum death grant of 3 times final pay. Short term spouses' benefits removed, but increases in partners lump sum to be provided where active, deferred or pensioner member dies.
Ill health benefits	If member permanently incapable of discharging efficiently the duties of employment, benefits paid immediately. If member has 5 or more years' service they are also entitled to enhancement of the benefits.	Two or three entry point ill health provision proposed, where members – (i) have no reasonable prospect of working before scheme normal retirement age of 65; or (ii) are likely to undertake gainful employment before age 65. Possible third tier consisting of employer grant, covering those who are likely to be capable of undertaking gainful employment within a reasonable period. Implementation of certificate of protection to cover circumstance where member takes lower salary due to ill health.
Partner pensions	Dependants benefits payable in respect of widows, widowers and civil partners at a rate of $1/160^{th}$	Dependants' benefits payable in respect of widows, widowers, civil partners, plus unmarried partners who cohabit, at rate of $1/160^{th}$
Flexible arrangements in the run-up to retirement	From age 50 with consent, members can reduce hours or move to a lower grade and, with consent, elect to draw the pension benefits already built up whilst still drawing salary for reduced hours/grade. Members can continue paying into the scheme to build up further benefits in the scheme. There is no limit on the amount of contributions you can pay. However tax relief will only be given on contributions up to 100% of taxable earnings.	Current provisions for flexible retirement to be retained as feature of the new Scottish LGPS. Increased flexibility through being able to draw all *or part* of occupational pension benefits without having to retire completely. In case of flexible retirement, employer consent required to reduce hours or lower grade, but employer consent to access benefits only required in respect of those under age 60. A provision to buy additional pension benefit. Cost-neutral uplift factors for benefits accrued beyond age 65, at no cost to the employer.

Scheme Feature	Current LGPS(S) as of 6 October 2006	New LGPS(S) Proposals by 1 April 2009
Minimum Pension Age	Finance Act 2004 – MPA will change from 50 to 55 on 6/4/2010.	All new members to have MPA of 55 years. All current members will have MPA of 55 from 6/4/2010.
Contribution rates for scheme members	General contribution rate of 6% except some existing manual employees (5%).	Working assumption is an increase in the employee contribution rate to an average of 6.3%. Employee contribution rate set at tiered variable rates, linked to pensionable pay. Potential options including a range of bands and contribution rates are outlined in the main text.
Contribution rates for employers	Employer rate varies as determined by 3-year actuarial valuations	Contributions rates for employers and scheme members to move towards a 2:1 ratio to ensure new scheme affordable. Overall average scheme costs estimated at 19.6% , with employee contributions at average of 6.3%. Employer contributions to make up the difference. Commitment to principle of cost sharing to ensure continuity of scheme over the long term.

7. As outlined above, the new LGPS proposals have been developed to meet the varied needs of a diverse workforce, balanced with the requirements of employers. Key points include:

- Retaining the current final salary structure benefits many members of the scheme and will minimise the effect of potential changes on existing scheme members. The proposals include an improvement to the accrual rate, and a number of other valued features of the current scheme have been retained.

- The introduction of a tiered employee contribution rate leads to fairer contribution rates for those scheme members at the lower end of the pay scale. As contributions benefit from tax relief, a tiered arrangement of contributions, where members pay a proportion of earnings up to each limit and then higher contributions on earnings above each limit, also improves the perceived fairness of contributions at different salary levels.

- The increased lump sum death in service benefit from two times to three times pay, pensions for partners who cohabit, and better targeted ill-health pension provisions are proposed. These improvements provide better security for scheme members and their dependants in the event of death or inability to work due to serious ill-health.

- The scheme has been designed to help ensure it is both fair and affordable into the future, for example through a commitment towards cost sharing and the incorporation of an increase in the employee contribution rate. It should be noted that this affects a change in the take-home pay of existing scheme members. Improvements have also been made to a number of the benefits provided to members.

- The individual benefits proposed are subject to the overall affordability of the benefit package. This means that if the consultation exercise finds demand for a particular feature to be included or improved within the new scheme, then this may impact on whether proposals to include or improve other specific benefits are affordable.

QUESTION(S) Q1 and Q2

- Are there other types of benefit that you would like to see included as part of the new scheme proposals?
- If it is agreed, following consultation, that certain elements of the scheme outline should be altered, this may lead to an increase in costs that would impact on the overall affordability of the proposal. What changes would you propose in this situation? For example, the member contribution rate could be increased or the level of other scheme benefits could be reduced.

8. Each of the key features of the scheme are now considered in turn.

FEATURES OF NEW LGPS

9. Type of scheme

Current context:

Final salary occupational pension schemes are widely recognised, both by employers and employees alike, as providing an esteemed element of the employee remunerative package and a valuable recruitment and retention tool for scheme employers.

In line with the approaches taken across other public service pension schemes, a range of potential scheme types were considered, for example, a Career Average Re-valued Earnings (CARE) scheme, or a CARE/final salary hybrid scheme, as well as an enhanced final salary scheme. Analysis has shown that each of the various types of scheme have different impacts, in terms of their affordability, the benefits provided, the way they impact on different sections of the workforce, and the ease in which they could be implemented. Whichever type of scheme is selected would result in a range of advantages and disadvantages for different stakeholders. This means, for example, that there is no one particular type of scheme that all stakeholders would agree is fully beneficial to all scheme members.

Proposal:

It is proposed that the scheme should remain a defined benefit final salary scheme. This is consistent with the Joint Statement of Pension Principles outlined by COSLA and the Unions, which stated at an early stage that work should progress in trying to maintain a defined benefit final salary scheme. This is also consistent with the scheme type adopted for the majority of public service pension schemes, including the NHS, Teachers, Police, Fire and LGPS in England and Wales.

The proposed LGPS retains the final-salary nature of the Scheme, in which a pension per annum is paid to scheme members from the normal retirement age of 65 as follows:

Pension p.a. = (accrual rate) x (no years membership) x (final salary)

Under Section 279(1) of the Finance Act 2004, the Minimum Pension Age (MPA) for occupational pension schemes will be increased to 55 from 6 April 2010. In the LGPS the intention is that MPA for new members following the introduction of the new scheme will be 55, but for existing members MPA will remain at 50 until April 2010. Where a member opts to leave employment at or after MPA, and before their 65^{th} birthday, where the benefits are payable those benefits will be reduced in accordance with guidance issued by the Government Actuary's Department.

Issues to consider:

- Although the final salary scheme is widely viewed as a beneficial provision, it tends to be particularly attractive to long-serving staff, particularly those who progress up the earning scale whilst in employment.

- To ensure the proposals cater fairly for the modern workforce, a large proportion of which is of short tenure, tiered employee contribution rates are also proposed (see paragraph 15 below). These provide for and aim to encourage short-tenure, lower salary level staff to join and remain in the scheme.

QUESTION(S) Q3

- Do you agree with the proposal that the new Scottish LGPS should remain a Defined Benefit Final Salary scheme?
- If not, what type of scheme would you prefer and why?

10. Accrual rates

Current context:

The accrual rate defines the proportion of final salary which the member builds up (or accrues) for each year of their membership of the pension scheme. For the LGPS, the accrual rate is currently $1/80^{th}$. This means that members build up pension rights payable per annum in retirement at a rate of $1/80^{th}$ of their final salary per year of scheme membership. This pension is then increased in line with inflation (RPI) in retirement. A lump sum is also payable equivalent in most cases to three times the annual pension.

Proposal:

In developing proposals, various accrual rates were considered. Under the current scheme, the total accrual rate (including both pension and lump sum) is the equivalent of an accrual rate of around $1/64^{th}$. Therefore, improved accrual rates higher than $1/64^{th}$ were considered and costed. It is the preferred view that the accrual rate should be $1/60^{th}$ which is an improved benefit consistent with other public service schemes. This offers the greatest benefit to employees in terms of benefits from the scheme. However, the overall affordability of $1/60^{th}$ needs to be considered as part of the overall package of benefits.

The proposed accrual rate is $1/60^{th}$. Although there is no automatic tax free lump-sum on retirement, there is an option to commute pension, taking up to 25% of the capital value of annual pension benefits (including AVC benefits) as a lump sum. The rate of conversion is £12 for each £1 of annual pension communted.

Issues to consider:

- Recent tax changes allow up to 25% of the annual pension to be converted to lump sum (see case study below).

QUESTION(S) Q4

- Do you agree with the proposal that the accrual rate should be increased to $1/60^{th}$?
- If not, what rate of accrual would you prefer and why? If your preferred rate of accrual is greater than $1/60^{th}$, what changes should be implemented to ensure the scheme remains affordable?

CASE STUDY – COMMUTATION OF PENSION

a) Local Government Employee in Current Scheme

Carole retires in 2008 with 42 years service. Assuming a final salary for calculation purposes of £37,000, an illustration of what her benefits may be follows.

Before commutation:

Pension £37,000 x 42/80 = £19,425

Lump Sum (3 x pension) £58,275

After maximum commutation:

Carole can commute an amount between the current 3/80ths and up to a maximum of 25% of the fund value after commutation into a lump sum. The maximum proportion of pension that can be commuted is therefore 19.64% of pension (this percentage has been calculated by the Government Actuary). Therefore the maximum pension that can be commuted is £3,815 (£19,425 x 19.64%). This would provide an additional lump sum of £45,780 (£3,815 x12) (as every £1 in pension reduction corresponds to an additional £12 of lump sum). This means that Carole could have a maximum lump sum of £104,055 i.e. an additional £45,780 on top of the 3/80ths based lump sum of £58,275.

For every £12 of additional lump sum taken, Carole's pension would be reduced by £1. So, if she decided to increase her lump sum to the maximum amount allowed, her pension would be reduced by £3,815 from £19,425 to £15,610.

Alternatively, Carole could decide to increase her lump sum by say only an additional £24,000 to a total of £82,275. In this case, pension would be reduced from £19,425 a year to £17,425 a year.

Figures have been rounded to nearest pound.

(b) Local Government Employee working within New Scheme Proposals

Jill takes up local government employment in September 2009 and retires in 2051 aged 65 with 42 years service. Assuming a final salary for calculation purposes of £37,000 (using today's values) she would be entitled to the following pension.

Before commutation:

Pension £37,000 x 42/60 = £25,900

Jill can commute up to a maximum of 25% of the fund value after commutation into a lump sum. The maximum proportion of pension that can be commuted is 35.71% (this percentage has been calculated by the Government Actuary and is higher than Jill's because there is no fixed lump sum). Therefore, the maximum proportion of pension that can be commuted is £9,249 (£25,900 x 35.71%). In Jill's case she could have a maximum lump sum of £110,988 (£9,249 x 12). For every £12 of lump sum taken, Jill's pension would be reduced by £1.

Therefore she could commute a maximum of £9,249 of her pension and receive a lump sum of £110,988.

After maximum commutation:

Pension £16,651 (i.e. £25,900 minus £9,249)

Lump Sum £110,988

Figures have been rounded to nearest pound.

11. Death in service arrangements

Current context:

Where a scheme member dies in service, a lump sum is payable by the administering authority. At their absolute discretion, they may make the lump sum payable to or for the benefit of the member's nominee or executors, or any person appearing to them to have been the member's relative or dependant at any time. A nomination would cease to have effect upon the member's marriage or on the formation of a civil partnership.

The current level of death in service is two times final salary.

Proposal:

A death in service benefit of three times final salary is proposed. This reflects practice in other public service schemes, such as the Scottish Teachers scheme and the new England and Wales LGPS.

It is proposed that short-term spouses' pension would be removed. However, in addition to the increase in the death in service provision mentioned above, there would be increases in other partner benefits:

- in the case of death of deferred members, the lump sum would increase from 3 times pension to 5 times pension; and
- in the case of death of pensioner members, the lump sum would increase from 5 times pension to 10 times pension, less any pension already paid, if a pensioner dies before age 75.

QUESTION(S) Q5 and Q6

- Do you agree that death in service benefit should be increased to 3 times final salary?
- If not, what level of death in service benefit would you prefer and why?
- Do you agree with the proposed changes to spouses' benefits? If not, what changes would you prefer and why?

12. Ill health benefits

Current context:

Under the current arrangements, ill-health benefits can be awarded in two circumstances.

Where a member leaves employment by reason of being permanently incapable (i.e. until age 65) of discharging efficiently the duties of that employment, or any other comparable employment, they are entitled to the immediate payment of their benefits. If such a member has 5 or more years' service they are also entitled to enhancement of the benefits.

The second circumstance is where the member is not considered to be entitled to ill-health benefits at the time of leaving employment. This may be either because the condition they suffer from is not deemed to be permanent, or they leave of grounds unconnected with health. They may at some later date become entitled to the early payment of their deferred benefits if they become incapable of discharging efficiently their former duties on the grounds of permanent ill-health. In such cases, benefits are based on accrued service only. There is no enhancement.

Proposal:

A two tier ill benefit scheme underpins these proposals as follows:

(i) where there is no reasonable prospect of undertaking gainful employment before age 65 - accrued pension benefits plus service enhanced by 100% of prospective service to age 65.

(ii) where it is unlikely that they would be able to undertake gainful employment within a reasonable period of time but likely to be able to do so before age 65 - accrued pension benefits service enhanced by 25% of prospective service to age 65.

Consideration is also being given to providing a third tier, dealing with the circumstances of a person who is capable, within a reasonable period of their employment being terminated, of undertaking gainful employment. The third tier could provide a benefit in the form of a grant, equivalent in value to a pension based upon the accrued service, but without enhancement. This grant would be payable by the employer rather than by the pension fund. It is likely that this provision would be time limited and would also cease on obtaining gainful employment in order for this provision to be feasible and affordable. The cost of this tier would depend on the average period of payment.

Definitions have been developed to support implementation of these tiers as outlined below. In each case, it is intended that judgements should be made on balance of probabilities rather than beyond reasonable doubt and based on what is likely rather than what is possible or probable.

Current ill health benefits	Proposals	Definitions
Criteria: Permanently unfit in job or any comparable job with employer. Permanent is defined as until age 65	**Criteria:** **Tier 1.** No reasonable prospect of undertaking gainful employment before age 65. **Tier 2.** Unlikely to undertake gainful employment within a reasonable period of time but likely to be able to do so before age 65.	**Reasonable prospect:** On balance of probabilities taking into account: • illness / medical condition; • objective assessment of functional capability; • any reasonable adjustments in terms of Disability Discrimination Act (DDA); • age; • the employee is not capable of undertaking paid employment (definition of gainful employment below) prior to reaching age 65. **Gainful employment:** Any type of paid employment for not less than 30 hours per week for a period of not less than 12 months. **Reasonable period:** Taking into account: • illness/ medical condition; • medical prognosis and likely recovery based on successful treatment • age; • a period of at least 3 to 5 years which allows for appropriate treatment to take effect.

The current scheme regulations contain a provision whereby members who suffer a reduction in salary through circumstances outwith their control can apply for a certificate of protection for their accrued service at the previous higher salary. Implementation of this provision should be retained, and should cover persons who step down to lower paid posts as a result of ill-health. This proposal may support government initiatives at Scottish and UK levels to encourage the long term sick back to work and reinforce the provisions of the Disability Discrimination Act.

Issues to consider:

- The underlying rationale of a two or three tier ill-health retirement pension arrangement is that it is better focussed and targeted compared to the present "one size fits all" arrangement. It will provide for a fairer distribution of ill-health benefits.

- The existing arrangements provide that where a member (with at least 5 years' service) is found to be permanently incapable of carrying out efficiently the duties of their employment on the grounds of ill-health, they are entitled to their accrual benefits together with enhancement based upon the length of their service. This takes no account of the member's future potential for further employment. The new arrangement would provide a more equitable distribution of ill-health benefits, such that members who have little or no prospect of obtaining gainful employment before the scheme's normal retirement age of 65 would receive greater enhancement than those who are likely to obtain such employment before that age.

- Under the existing arrangements, ill-health retirement pensions are payable for life. This will remain the case for the first and second tiers of the new arrangements.

- A possible third tier might take the form of a grant paid by the employer and would therefore fall outwith the costs of the LGPS. As the third tier is less tightly defined than the first two tiers, it is more difficult to make assumptions as to the likely numbers involved and cost of this provision. The overall scheme costs assume ill health incidence of 15% and 85% between the first two ill health tiers respectively. The third tier would cost in the order of 0.1-0.2% of payroll depending on the number of members eligible for this benefit and for every year the benefit is paid. If a third tier is included, a review process may need to be introduced. Whether a two or three tier structure is agreed upon, the actual proportions of members who will ultimately fall into each category of the new structure cannot be known with certainty in advance of implementation of the new scheme.

- The number of tiers and the specific criteria applied to each of the tiers will impact on the total cost of the ill health benefits provided. The tripartite group will consider this further before the final scheme outline is agreed.

QUESTION(S) Q7, Q8, Q9 and Q10

- Would you prefer a two or three tier ill health arrangement as outlined above? Why? If neither of these options is preferable, please outline what an alternative arrangement might look like.
- Would any of the three tiers require a criteria to be inserted to reflect permanence until age 65?
- Do you agree with the proposed definitions of 'reasonable prospect', 'gainful employment' and 'reasonable period' to ensure practical application of the tiers?
- Do you agree that implementation of the certificate of protection should be retained and should cover persons who step down to a lower paid post as a result of ill-health?

CASE STUDY 1- ILL-HEALTH RETIREMENT – 1st TIER

Bob is 55, worked in the maintenance department of the local council and has 22 years service. His pay was £18,000 p.a. His work involved a considerable amount of lifting and moving of heavy machinery. Bob developed severe back pains which became worse over time. Bob was examined by the council's medical adviser who certified that he was permanently incapable of carrying out efficiently the duties of that post. The adviser also certified that Bob was unlikely to be able to obtain gainful employment elsewhere before his normal retirement age of 65.

Under the first tier of the proposed ill-health provisions, Bob would be entitled to receive his accrued benefits based upon his service until the date of leaving, 22 years. Added to this service would be the whole of the service between that date and his actual normal retirement age (65), which would be 10 years. His benefits will therefore be calculated as follows –

Pension £18,000 x 32/60 = **£9,600 per annum**

Bob has the option to commute up to a maximum of 25% of the fund value after commutation into a lump sum. For every £12 of lump sum taken, his pension would be reduced by £1 (see Commutation Case Study for fuller explanation)

CASE STUDY 2 - ILL-HEALTH RETIREMENT – 2nd TIER

Mark was aged 45 when he left his job with the HR department of his local government employer, with 15 years service, after a bad fall had left him with long term mobility problems. His salary was £27,000 p.a. The employer's medical adviser certified that on the balance of probabilities he would be permanently incapable of carrying out existing duties (which involved travel) but felt that he would recover sufficiently in the longer term for him to be likely to obtain gainful employment before normal retirement age. In Mark's case, benefits would be calculated on the basis of accrued service of 15 years, plus 25% of the period between the date of leaving and normal retirement age, providing an additional 5 years' service.

Mark's benefits will therefore be –

Pension £27,000 x 20/60 years = **£9,000 per annum**

Mark has the option to commute up to a maximum of 25% of the fund value after commutation into a lump sum. For every £12 of lump sum taken, her pension would be reduced by £1 (see Commutation Case Study for fuller explanation)

13. Partner pensions

Current context:

Partner pensions are currently provided to spouses and civil partners. However, partners who cohabit are not currently eligible for pension benefits within the LGPS.

Over the last 20 years or so there have been major changes in the way families are formed and how people think and feel about families. With effect from 4 May 2006, the Family Law (Scotland) Act 2006 updated the law to reflect the way families live today. As part of the Act, a set of basic rights were introduced to protect cohabitants either when their relationship breaks down, or when a partner dies. The Act provides a set of basic safeguards relating to the sharing of household goods, money and property; financial provision on relationship breakdown and discretionary provision for a surviving cohabitant when a partner dies without a will.

In May 2006, the Law Commission published their consultation paper "Cohabitation: The Financial Consequences of Relationship Breakdown", as a result of being tasked by the Government at UK level to consider how this area of the law could be reformed. The paper considers the case for allowing cohabiting couples to opt into a pension scheme imposing enforceable financial obligations on the parties in the event of their separation. A final report is now being developed by the Law Commission, and is expected by August 2007.

Proposal:

The scheme proposals aim to provide security for scheme members and their dependants in the event of death or inability to work due to serious ill-health retirement.

It is proposed that spouses and civil partner pensions should be retained at a rate of 1/160th.

Potential criteria that may be used to determine a nominated cohabiting partner could include the following elements, which should be in place for a continuous period of at least 2 years:
- The partners are able to marry, or form a civil partnership;
- The partners are living together as if they were husband and wife or as if they were civil partners;
- neither partner is living with a third person as if they were husband and wife or as if they were civil partners, and
- either one partner is financially dependent on the other or both partners are financially interdependent.

The introduction of pensions for partners who cohabit may need to be reconsidered in light of any resulting change in the law, as it is clearly desirable that any provision be compatible and aligned with any reform in law in this area which may emerge. However, for the purposes of this consultation paper, it is proposed that cohabiting partner pensions should be established at a rate of 1/160$^{th.}$ Pension provision should also be backdated to 6 April 1988. This provides a clear, fixed and easy to administer criterion which is broadly in line with other public service scheme practice. In addition, it is proposed that a facility would be introduced for members to purchase pre-April 1988 service, at full cost to the members.

Issues to consider:

- As more women enter the workforce, and more households draw on more than one income, the need to provide partners' pensions reduces, as long as both partners have access to a workplace based pension scheme and are able to build up enough entitlement. There are no propositions here to reduce partners' benefits at this stage, however were partners' provisions to be reduced for married, civil and cohabiting partners, this would reduce the cost of the proposed new scheme.

- The Law Commission final report is due to make final report to Government on reform of the law surrounding relationship breakdown in August 2007.

QUESTION(S) Q11 and Q12

- Do you agree with the proposal to provide partner pensions to spouses, civil partners and cohabiting partners at a rate of 1/160th? If not, what rate(s) would you prefer and why?
- Do you agree with the proposed criteria for defining partners who cohabit? If not, what criteria would you prefer and why?

14. Flexible arrangements in the run up to retirement

Current context:

The traditional approach towards retirement is changing. Employers and employees within the modern workforce for local government need and expect a higher degree of flexibility. There is an overarching move across the workforce towards supporting extended working lives, whilst also giving employees the opportunity to wind down towards retirement.

The current provisions within the LGPS allow scheme members to:

- retire before the scheme's normal retirement age of 65 from 60, or from 50 with employer consent. For scheme members with no 85 year Rule entitlement, their pension will be reduced according to a set of cost-neutral early retirement factors, to reflect the fact that the pension is coming into payment earlier than expected and is likely to be in payment for longer than expected;
- take *flexible retirement* from 50 where the employer gives their consent both to a reduction in hours or grade, and, in the case of those under 60, to the member accessing pension. This will mean that the employee takes payment of their reduced pension before 65, while remaining in employment; or
- continue to accrue service in the LGPS beyond age 65. The pension must be drawn by the day before the member's 75th birthday. Benefits accrued before age 65, which are not taken at or before age 65, are increased in line with inflation (RPI).

New regulations recently introduced following the Finance Act 2004 also brought significant and well supported flexibilities into the scheme, which created an enhanced pension environment. These arrangements enable members to exercise additional control over their choices about saving for their retirement as follows:

- One of the key benefits for members is the option to invest in their pension provision to a higher level. For example, members can invest up to 100% of their salary into their pension scheme, as well as being able to contribute towards concurrent pension arrangements in respect of the same employment.
- There is increased flexibility in terms of members drawing down their pension. Members are able to take up to 25 per cent of the capital value of their annual pension (including AVC benefits) as a tax free lump sum, as an alternative to taking their benefits in the form of annual pension.

Proposal:

It is proposed that current provisions for flexible retirement should be retained as a feature of the new Scottish LGPS, to the benefit of all existing and new members.

It is also proposed to amend the scheme to extend the current flexible retirement option to allow members to draw all *or part* of their occupational pension benefits from the age of 55 (50 until 2010 for existing members) without having to retire completely from that employment. This opportunity to build on existing flexibilities should help to:

- improve work life balance;
- improve the retention of experienced staff with valuable skills; and
- extend working lives.

To encourage members to have greater control over their retirement options, proposals introduce more flexible and appropriate arrangements for buying additional pension benefit compared to the existing past and current added years (PAY/CAY) provisions. This will be achieved by enabling members, or their employers on their behalf, to buy additional annual pension benefit of up to £5,000.

In addition, where a member continues to work and accrue benefits beyond age 65 the value of those benefits will be *increased* by cost-neutral uplift factors.

For workforce planning reasons, a member applying for flexible retirement is required to obtain employer consent to reduce hours or lower grade. Where such consent is given, however, it is proposed that subsequent employer consent to access benefits would only be necessary in the case of applicants who are under age 60. Releasing benefits early in such cases gives rise to a strain on the fund, part of the cost of which may fall to the employer.

Work is ongoing to develop guidance on the application of the flexible retirement arrangements to ensure best practice. New actuarial tables for early retirement will also be produced for the new scheme.

<u>Issues to consider:</u>

- Supporting and enabling flexible retirement is a key element of meeting the requirements of the modern workforce. There may be other cost neutral proposals that could also be implemented to support better flexible retirement practices across the local government workforce and wider scheme membership.

QUESTION(S) Q13, Q14 and Q15

- Do you agree that the current flexible retirement provisions should be retained?
- Do you agree that increased flexibility should be provided through being able to draw all *or part* of occupational pension benefits without having to retire completely?
- Do you agree with the provision to buy additional pension benefit, and cost-neutral uplift factors for benefits accrued beyond age 65?
- What other cost neutral provisions would you like to see made available to support flexible retirement?

CASE STUDY - FLEXIBLE RETIREMENT

Based on the new scheme proposals, Jean is able to draw all or part of her occupational pension benefits without having to retire completely. Jean reduces her hours to half-time from age 61 and her annual salary drops from £30,000 to £15,000. She continues to work for another 4 years and accrues more service.

In November 2009 at age 61 Jean has accrued 16 years service and decides to take 50% as pension at this time. Pension is therefore calculated on half service, 8 years. Pension will be subject to **actuarial reduction**.

Pension

£30,000 x 8/60 = £4,000 x 0.81 (*ARB factor) = **£3,240** plus an ongoing salary of £15,000.

Jean has the option to commute up to a maximum of 25% of the fund value after commutation into a lump sum. For every £12 of lump sum taken, her pension would be reduced by £1. Jean decides not to commute any of the pension into a lump sum.

She works for another 4 years and at age 65 retires completely. Final salary, assumed for calculation purposes, at age 65 is £18,000. The extra 4 years service (at half-time) is the equivalent of 2 years of fulltime service and that service is combined with the residual service of 8 years, making a total of 10 years, thus her additional benefits are calculated as follows –

Pension for Residual service:

£18,000 x 2 = £36,000 (full-time equivalent salary) x 8/60 = **£4,800** (no ARB)

Plus:

Pension on part-time salary of £18,000 in respect of service accrued from age 61 to 65, calculated on full-time equivalent service and salary at an accrual rate of 1/60 –

£18,000 x 2 = £36,000(full-time equivalent salary) x 2/60 = **£1,200**

New additional Pension = £6,000

Jean can commute up to a maximum of 25% of the fund value after commutation into a lump sum. The maximum proportion of pension that can be commuted is 35.71% (this percentage has been calculated by the Government Actuary). Therefore, the maximum proportion of pension that can be commuted is £2,143 (£6,000 x 35.71%). In Jean's case she could have a maximum lump sum of £25,716 (£2,143 x 12). For every £12 of lump sum taken, Jean's pension would be reduced by £1.

<u>After maximum commutation</u>:

Pension £3,857 (£6,000 minus £2,143) plus pension drawn in 2009
Lump Sum: £25,716

(Figures have been rounded to nearest pound.)

The first part of the pension drawn in 2009 would increase in value each year in April in line with inflation. If pension increases since 2009 amounted to 10%, the pension that came into payment in 2009 would be £3,563 pa by age 65.

* ARB – Actuarially Reduced Benefit – These factors have been provided by the Government Actuary's Department. They are subject to change from time to time.

15. Contribution rates for scheme members

Current context:

Further information on overarching scheme costs is outlined within the next section.

The LGPS currently has a general member contribution rate of 6%, except for some existing employees (former manual workers) who have a contribution rate of 5%.

Proposal:

As a working assumption, it is proposed that the average contribution rate for scheme members is **6.3%.**

To ensure a more equitable scheme and a fairer rate across all salary scales, it is proposed that the new LGPS should move away from a single contribution rate and should have in place a tiered member contribution rate system based on pensionable pay. This would operate in a similar fashion to the current tax banding system i.e. a certain percentage of pensionable pay is payable up to a particular salary band, with a separate contribution rate payable on any salary above this, etc. The implementation of a tiered contribution system in this way would limit the 'cliff edge' possibilities within a straightforward banding system, where any employee moving between salary bands may be faced with a considerable increase in pension contribution rates.

Details are still to be finalised as to; the preferred number of contribution tiers; the basis of earnings (including the calculation of contributions for part time staff); and also what the appropriate salary bandings should be within these tiers. However, three illustrative options are outlined below. The rates and bands proposed ensure that the new scheme proposals are affordable.

Option 1: Three tier member contribution rate.

The table below shows marginal rates. For Option 1, this means that everyone will pay 5.5% on the first £18,000 and then pay 8.5% on earnings above £18,000, etc. The same mechanism applies to each of the three Options.

Pensionable Pay	% Rate
On earning up to and including £18,000	5.50%
On earnings above £18,000 and up to £40,000	8.50%
On earnings above £40,000	11.00%

The table below shows what the actual average earnings would be for a range of salary levels and also shows the average rate after adjusting for tax. Tax adjustment assumes a Basic Rate tax allowance for 2007/8, and is calculated at 2008/09 tax rates. Again, the same mechanism applies to all three Options.

Pensionable Pay	Average Contribution Rate	Average rate net of Tax
£12,000	5.50%	4.40%
£14,000	5.50%	4.40%
£16,000	5.50%	4.40%
£18,000	5.50%	4.40%
£20,000	5.80%	4.64%
£25,000	6.34%	5.07%
£30,000	6.70%	5.36%
£35,000	6.96%	5.57%
£40,000	7.15%	5.72%
£45,000	7.58%	4.55%
£50,000	7.92%	4.75%
£60,000	8.43%	5.06%
£70,000	8.80%	5.28%
£80,000	9.08%	5.45%
£90,000	9.29%	5.57%
£100,000	9.46%	5.68%

Option 2: Five tier member contribution rate.

Pensionable Pay	% Rate
On earning up to and including £12,000	5.50%
On earnings above £12,000 and up to £18,000	6.50%
On earnings above £18,000 and up to £38,000	7.50%
On earnings above £38,000 and up to £75,000	9.00%
On earnings above £75,000	10.00%

Pensionable Pay	Average Contribution Rate	Average rate net of Tax
£12,000	5.50%	4.40%
£14,000	5.64%	4.51%
£16,000	5.75%	4.60%
£18,000	5.83%	4.67%
£20,000	6.00%	4.80%
£25,000	6.30%	5.04%
£30,000	6.50%	5.20%
£35,000	6.64%	5.31%
£40,000	6.83%	5.46%
£45,000	7.07%	4.24%
£50,000	7.26%	4.36%
£60,000	7.55%	4.53%
£70,000	7.76%	4.65%
£80,000	7.98%	4.79%
£90,000	8.20%	4.92%
£100,000	8.38%	5.03%

Option 3: Seven tier member contribution rate.

Pensionable Pay	% Rate
On earning up to and including £12,000	5.50%
On earnings above £12,000 and up to £14,000	5.75%
On earnings above £14,000 and up to £18,000	6.50%
On earnings above £18,000 and up to £30,000	7.50%
On earnings above £30,000 and up to £40,000	8.50%
On earnings above £40,000 and up to £75,000	9.50%
On earnings above £75,000	10.50%

Pensionable Pay	Average Contribution Rate	Average rate net of Tax
£12,000	5.50%	4.40%
£14,000	5.54%	4.43%
£16,000	5.66%	4.53%
£18,000	5.75%	4.60%
£20,000	5.93%	4.74%
£25,000	6.24%	4.99%
£30,000	6.45%	5.16%
£35,000	6.74%	5.39%
£40,000	6.96%	5.57%
£45,000	7.24%	4.35%
£50,000	7.47%	4.48%
£60,000	7.81%	4.69%
£70,000	8.05%	4.83%
£80,000	8.29%	4.98%
£90,000	8.54%	5.12%
£100,000	8.74%	5.24%

Issues to consider:

- A new average contribution rate for scheme members ensures the new scheme is affordable. There is a balance to be struck between the level of benefits provided and the cost to scheme members and employers of providing these benefits.

- The introduction of a tiered employee contribution rate contributes towards ensuring a fairer rate of contributions across scheme members. For example, it means that individuals towards the lower end of the pay scale contribute proportionally less than higher earners.

- The introduction of a tiered employee contribution rate may affect the take-home pay for scheme members from the date of implementation for the new scheme. This may increase or decrease in comparison with the contribution rate they currently pay, depending on the salary of that period and which mechanism is incorporated into the new scheme. Views are sought on which approach is preferable for the new scheme.

- There may be difficulties implementing and administering a tiered contribution rate system. For example, current salary payroll systems might not currently be compatible operationally with a tiered contribution system, and these systems would therefore require modification and amendment, which may have significant cost implications. These complexities should not be a reason to dismiss the implementation of any tiered contribution rate system, but the practicalities and potential cost implications will require further consideration once the detailed proposals are further established and agreed. Views are sought on this issue.

QUESTION(S) Q16, Q17 and Q18

- Do you agree that the proposed employee contribution rate is fair, given the level of benefits proposed? If not, please explain why and what your preference would be.
- Do you agree that the LGPS should incorporate a tiered contribution rate system? Why?
- Which of the illustrative tiered contribution rate options do you feel is preferable and why? If none of these seem suitable, please provide details of an alternative mechanism.
- What implementation costs and issues do we need to be aware of, and what solutions are there to operationally implementing a tiered contribution system? For example, how should contributions be determined where a member has more that one salaried job within the local government workforce?

16. Contribution rates for employers

Current context:

The key driving force behind the programme of reform is to ensure that the scheme is viable over the longer term. Information on overall scheme costs is outlined within the next section.

Proposal:

There is general agreement about moving towards a principle of adopting an approximate 2:1 cost sharing ratio between employer and member contribution rates. The exact level of employer contribution rates will depend on the overall cost package once the benefit structure is agreed. However, the costs of any scheme deficit arising prior to the implementation of the new scheme in April 2009 and the cost of the investment risk should continue to fall on the employer, and the movement towards the 2:1 cost sharing principle is proposed for taking forward the new benefit scheme only.

Issues to consider:

- Dividing contributions between employers and scheme members on an approximate 2:1 ratio eases the financial burden on employers and tax payers, whilst ensuring the new scheme proposals, including the proposed new benefits, are both valued by, and affordable for, members and employers.

QUESTION(S) Q19

- Do you agree with the move towards a 2:1 ratio between employer and member contribution rates? If not, what would you prefer and why?

OTHER FEATURES OF THE PROPOSED LGPS SCHEME:

17. Transfer options between the current and new scheme

Proposal:

There are two potential transfer options for members when the new scheme is implemented.

Transfer Option 1 is that all existing members of the LGPS transfer their current benefits across to the new scheme. This ensures that all members of the LGPS receive the same type of benefits and makes the benefits package easier to understand, as well as easing future administrative complexities. Transfer values would need to be determined for any transfer of existing members to the new scheme, and to ensure that members continue to 'hold what they had' and do not suffer any detriment by the transfer. A cost neutral transfer would mean that the actual level of member benefits would be transferred to new scheme (see case study below for details of how this could work in practice). A more pragmatic transfer basis could be developed but may involve additional costs. For example, an enhanced transfer rate (e.g. year for year basis) could be considered, although this would require further consideration as it is likely to involve additional costs for the scheme.

Issues to consider:

- Transferring the actual level of accrued benefits for each member to the new scheme would provide a cost neutral transfer option. However, due to the improved accrual rate in the new scheme proposals, this would mean that existing members transferring to the new scheme may be 'due' slightly fewer years of accrued benefit then they currently have (as one year of accrued benefit would be worth more in retirement in the new scheme). This may have presentational difficulties and, on the surface, some individuals may feel they were worse off with this approach.

Transfer Option 2 means that on establishment of the new scheme, a line would be drawn with the old scheme, i.e. the old scheme would stop when the new scheme starts. Existing members would automatically accrue pension in accordance with the new scheme for future service and would have two pension calculations (for old and new scheme entitlement respectively) at the same time when they retire. Individuals who retain Rule of 85 transitional protection would accrue at the new rate, but would also be able to retire on an unreduced pension when the Rule is met.

Issues to consider:

- Members would require two calculations to determine their level of pension, but presentationally, there is clear retention of the Rule of 85 transitional protection arrangements. Three calculations may be necessary for members retiring before age 65 with service prior to March 2008 (i.e. prior to the removal of Rule of 85), between March 2008 and 2009, and service after 2009.

QUESTION(S) Q20

- Which transfer option do you prefer and why? If neither, please give details of your preferred alternative approach.
- If Option 1 is preferred, please give your views on whether you would wish the actual level of member benefits to be transferred, or for an enhanced transfer rate to be applied. If an enhanced transfer rate is to be applied, and this results in the scheme becoming unaffordable, what changes should be implemented to ensure the scheme remains affordable? For example, other benefits could be reduced or member contribution rates could be increased?

CASE STUDY - TRANSFER OPTION 1

For Transfer Option Number 1, all existing members of the LGPS transfer their current benefits across to the new scheme.

A cost neutral transfer option would involve transferring the actual level of accrued benefits for each member to the new scheme. Members will get 1/60 of final pensionable pay for each year of reckonable service. However, due to the improved accrual rate in the new scheme proposals, this would mean that existing members transferring to the new scheme may be 'due' slightly fewer years of accrued benefit then they currently have (as one year of accrued benefit would be worth more in retirement in the new scheme

David has 12 years' service in the old scheme which is transferred to the new scheme on 1st April 2009. The actuarially equivalent factor for conversion is 0.9375 (this factor has been calculated by the Government Actuary). This means that he will transfer 11.25 years (0.9375x12 = 11.25) to the new scheme. David accrues a further 8 years service from 1st April 2009.

David retires with 19.25 years' reckonable service (11.25 + 8 = 19.25). His final pensionable pay is £30,000.

Before commutation:

Pension = 19.25/60 x £30,000 = £ 9,625 per annum.

David can commute up to a maximum of 25% of the fund value after commutation into a lump sum. The maximum proportion of pension that can be commuted is 35.71% (this percentage has been calculated by the Government Actuary). Therefore, the maximum proportion of pension that can be commuted is £3,437 (£9,625x35.71%). In David's case he could have a maximum lump sum of £41,244 (£3,437x12). For every £12 of lump sum taken, David's pension would be reduced by £1

After maximum commutation:

Pension = £6,188 (ie £9,625 minus £3,437)

Lump Sum £41,244

…………………………………………………

Under the 1998 Regulations David's pension would have been calculated as follows:

David retires with 20 years' reckonable service. His final pensionable pay is £30,000

Before commutation:

Pension = 20/80 x £30,000 = £ 7,500 per annum

Lump sum = 3 x £ 7,500 = £22,500

After maximum commutation:

David can commute an amount between the current 3/80th and up to a maximum of 25% of the fund value after commutation into a lump sum. The maximum proportion of pension that can be commuted is therefore 19.64% of his pension (this percentage has been calculated by the Government Actuary). Therefore the maximum pension that can be commuted is £1,473 (£7,500 x 19.64%). This would provide an additional lump sum of £17,676 (£1,473 x 12). This means that David could have a maximum lump sum of £40,176 ie an additional £17,676 on top of the 3/80th based lump sum of £22,500.

For every £12 of additional lump sum taken, David's pension would be reduced by £1. If David decided to increase his lump sum to the maximum amount allowed, his pension would be reduced by £1,473 from £7,500 to £6,027 per annum.

Pension = £6,027

Lump Sum £40,176

These figures have been rounded to the nearest £

18. Transparency in data sharing

As part of a wider drive to ensure transparency, and to assist with future workforce planning and pension modelling arrangements, COSLA and SPPA are reviewing the data collection and collation processes currently in place for the LGPS. The aim is to ensure that robust and comprehensive methods are in place for collating and making available information about scheme membership and workforce, which is routinely provided by local authorities to the Scottish Executive. This will ensure that policy decisions continue to be made on an informed basis and enables us to continue to take a collaborative approach towards developing and implementing a world class LGPS for Scotland.

19. Governance

The tripartite group encourages and supports good practice in open and transparent governance arrangements in the LGPS, including the best practice advisory, consultation and communication arrangements adopted by a number of Scottish funds. However, it was also recognised that to complement the new collaborative approach towards the LGPS it would be beneficial, in principle, to review the scheme's governance arrangements to ensure that these support excellence in scheme performance.

A range of potential options exist that may strengthen governance and consultative processes across the scheme at local and national level, including for example:

- Establishment of employee representatives or member nominated representatives with observer status and/or decision making capacity on bodies and committees within the LGPS.
- Development and implementation of good practice equality proofing mechanisms and guidance

- Clear and transparent national governance structures for the LGPS building on the current tripartite group arrangements that were established for developing the new scheme.

QUESTION(S) Q21

- Do you agree that the LGPS scheme governance arrangements should be reviewed? Why? If so, who should undertake this review and what should the specific focus of the review be?
- Please give any views on the value and/or practicalities of the potential actions which may be implemented to strengthen governance and consultative processes across the LGPS, for example member nominated representative participation on scheme committees, development and implementation of equality proofing good practice, and a national tripartite group to oversee the LGPS.
- Please detail any other suggestions and comments you have on LGPS governance arrangements.

20. Equality Impact Assessment

What is an equality impact assessment?

An equality impact assessment is all about considering how policy (i.e. activities, functions, strategies, programmes, and services or processes) may impact, either positively or negatively, on different sectors of the population in different ways.

The first stage is to identify who will be affected by the policy and any specific requirements which need to considered. More than that, there is a statutory duty for public sector bodies to consider and address the impact of policy on particular groups (disabled people, women & men and different ethnic groups).

The Local Government Pension Scheme

We are committed to promoting equality of opportunity. This is being undertaken as an integral element of the development of a new scheme that is both viable and sustainable over the longer term.

Specific needs of individuals and groups of people are often identified through consultation. The consultation exercise ‘Facing the Future’ for the LGPS involved a range of stakeholders, including employers, and local government employees. COSLA and Unions responded on behalf of their members, and some scheme members also responded to the consultation exercise individually. All issues raised through that consultation exercise have informed the development of the new scheme. More recently, the new scheme proposals have been jointly developed by the tripartite group, which has helped to ensure relevant equality issues are considered as part of the development process. Proactive contact has also been made with relevant equality groups, e.g. Age Concern Scotland, Equal Opportunities Scotland, Disability Rights Scotland, Inclusion Scotland, Scottish Interfaith Council and various other organisations to ensure that any existing relevant information that is currently available from wider sources is taken into account throughout the development process.

However, it is also for individual employers and members/employees to bring attention to any equality issues that arise from these proposals. This consultation exercise on the proposed new LGPS provides an opportunity to raise equality issues, in order that full consideration can be given to these before final decisions are taken on the new LGPS for Scotland.

QUESTION(S) Q22
• Are you aware of any equality issues that arise from the new scheme proposals?

21. The next section examines the overall cost of the new scheme proposals.

SECTION 4

NEW SCHEME COSTS

Developing an affordable set of proposals

1. The driving force behind the reform process for the LGPS is to ensure the scheme for the future is affordable, sustainable and fair to employees, employers and to the taxpayer. The new scheme costs are therefore an essential element of the new scheme proposals.

2. To ensure a robust analysis of the relative costs involved, an agreed costing method and series of assumptions were agreed at an early stage by the tripartite group. The method and assumptions were developed by actuaries on behalf of COSLA and these are set out below. There were some differences between the different actuaries working on behalf of Trades Unions and the Scottish Executive, in terms of costs and assumptions used, however these did not impact significantly on the overall costs. In addition, it should be borne in mind that the main focus of the costing calculations is to compare the relative costs of the new benefit structure to the existing scheme. Therefore, if slightly different assumptions were used, the difference in costs between the existing and new schemes may well be broadly the same. Actuaries have confirmed that, generally, the method is robust and that the scheme benefits costs are robust on the basis of the assumptions used. The details outlined below are drawn from the work undertaken for COSLA by Barnett Waddingham, Consulting Actuaries.

3. In considering the costs that have been calculated, there are a number of important aspects to bear in mind in as follows:

- The costs are the total costs which would be met by contributions from both employee and employer.

- The actuarial methodology adopted in determining the costs is methodology appropriate for benefit costing purposes to enable development of the new scheme (i.e. the 'Attained Age Method'). This is not necessarily the same methodology that would be adopted for funding purposes (i.e. setting levels of employer contributions), which would be undertaken by individual fund actuaries. In practice, the levels of funding contributions would most likely lie somewhere between the cost of providing benefits to new entrants and existing scheme members.

- The costs represent the cost of providing benefits for service after 31 March 2009 and so do not make any allowance for funding any deficits or surpluses. The proposals and actuarial calculations focus specifically on the future cost of scheme benefits. As discussed in Section 2, longevity is one of the key influences on affordability of the LGPS and the cost of benefits.

Data sources

4. The "raw" active membership data submitted for the 2005 actuarial valuations of all of the Scottish Funds as at 31 March 2005 has been used as the basis for calculating the costs of the new scheme proposals for existing members.

5. The membership data as at 31 March 2009 will inevitably be different to the data as at 31 March 2005 and so in completing these calculations it is effectively assumed that the membership profiles as at 31 March 2009 are the same as they were four years earlier. Experience would suggest that the shape of the active membership of funds does not change materially in the short term unless eligibility conditions are changed.

6. Actuaries have also completed costings for an assumed "new entrant" profile.

Membership summary

7. Table 3 below sets out a summary of the membership data used.

Table 3: Scottish LGPS membership data 2005

Number*	**Existing Members**	**New entrants**
Males	76,577	3,301
Females	126,545	8,947
Total	**203,122**	**12,248**
Actual Pay (£ '000s)		
Males	1,572,691	55,665
Females	1,678,984	94,437
Total	**3,251,675**	**150,102**
Average Pay (£)		
Males	20,537	16,863
Females	13,268	10,555
Total	16,008	12,255
Average Age		
Males	45.9	39.0
Females	43.5	36.7
Total	**44.5**	**37.5**

* Numbers based on raw data and excluding active members over age 65.

Source: *"New Look Scottish LGPS Actuarial Costings – Update",* Barnett Waddingham (January 2007)

Actuarial Assumptions

8. With the exception of pensioner mortality, the financial and demographic assumptions are broadly typical of the assumptions adopted by the Scottish Funds at the 2005 valuations. See table 4 below. The post retirement mortality assumption is based on projections to 2045 and essentially includes an allowance for some improvements in mortality.

9. As a result of the Finance Act 2004, it is possible at retirement to opt for, or 'commute', a cash sum equal to 25% of the capital value of accrued pension rights. This provides scope for a higher lump sum than the fixed 3/80ths provided in the past. The

assumption used is that 50% of retirees will retain the 3/80ths lump sum and 50% will opt for the maximum. A degree of sensitivity analysis has also been undertaken on this assumption.

Table 4: Assumptions used to cost new scheme proposals

Assumptions	**COSLA Costings**		**2005 LGPS Valuations**	
	Nominal % p.a.	**Real % p.a.**	**Real-Range % p.a.**	**Real-Average (1) % p.a.**
Price Increases	3.0%	-		
Salary Increases	4.5%	1.5%	1.50% to 1.75%	1.53%
Discount Rate	6.5%	3.5%	3.40% to 3.70%	3.44%

(1) Weighted by payroll

Source: *"New Look Scottish LGPS Actuarial Costings – Update",* Barnett Waddingham (January 2007)

Costs of new scheme proposals

10. The costs of the existing scheme are outlined in Table 5. These costs include maintaining the Rule of 85 and also assuming commutation as a result of the Finance Act 2004.

Table 5: Costs of existing LGPS

Total Contribution Rate: Existing Members	Total Contribution Rate: New Entrants	Average Scheme Cost
20.3%	19.3%	19.8%

11. Although there are a large number of clear similarities between the Scottish and English/Welsh schemes, the new schemes have been designed specifically for the relative countries. There are some differences which serve to make the two sets of costs not directly comparable, such as the different costing methodology adopted and variances within the benefits proposed in the new scheme. A reconciliation between the two schemes has not been carried out.

12. The cost of the new scheme proposals are outlined in Table 6 below. These costs are based on the proposals detailed in this consultation document, and also include the savings released from removing the Rule of 85. The costs include Rule of 85 transitional protection for existing members until 2020, as well as savings arising from future commutation of pension for lump sum.

Table 6: Costs of new LGPS proposals

	Existing Members	New Entrants	Average Scheme Cost
Contribution rate for new scheme proposals	20.4%	18.8%	19.6%

The costs of the new scheme proposals do not include the cost of the potential third tier option as part of the proposed ill health benefits due to this being in the form of an employer grant.

As they currently stand, the average cost of the proposals is approximately 19.6%. Employer contributions make up the difference between the member contribution rate and the overall cost of the scheme. As a working assumption, the employee contribution rate would be 6.3%. The cost sharing ratio for employers and members is, therefore, initially more than 2:1, however this will become closer over time as the Rule of 85 transitional protection arrangements are worked out of the scheme.

The overall package of benefits that is agreed following consultation will have to be carefully pieced together to ensure that it remains affordable.

QUESTION(S) Q23, Q24 and Q25

- Do you agree with the assumptions used to underpin the development of the new scheme proposals? If not, please give evidence to support alternative assumptions.
- Do you agree that the proposed employer contribution rate is fair, given the level of benefits proposed? If not, please explain why and what your preference would be.
- Do you think the contributions are affordable in the long term?

Ensuring sustainability over the longer term

Context

13. The principle of cost-sharing means that any future changes in the cost of the pension scheme should be shared by employees and employers. This provides a mechanism for spreading the financial risk of significant changes which may impact on scheme affordability. This is an agreed principle across other public sector pension schemes, such as the Scottish NHS and Teachers schemes, where it is seen as an essential element in achieving sustainability of schemes over the longer term.

Proposal

14. There is broad agreement on moving forward to a cost sharing scheme, but that this should equally embrace the concept of cost savings should they arise.

15. To ensure that the scheme is affordable, contribution rates for employers and scheme members are agreed when the scheme is initially developed to ensure the proposed benefits are within the cost envelope for the scheme.

16. It can also be assumed that, on the basis that the scheme has been developed to be affordable on the basis of agreed actuarial assumptions, the total costs for the scheme should not be expected to increase exponentially in the short term. However, to ensure the scheme can continue over the longer term, employers and members share the impact of changes in scheme cost.

17. Whilst the detail has not been worked up, the tripartite group is content to consider a 'trigger' in the guidance which would lead to further discussions should the cost sharing ratio for the new scheme look as if it is shifting significantly. The cost sharing ratio would be assessed every second or third valuation to determine whether there has been any significant change.

18. This is a simplistic description of how cost sharing might work within the LGPS and, in practice, the practicalities are particularly complex for a funded scheme. In order to develop a potential cost sharing mechanism for the LGPS, a number of issues need to be considered as outlined below.

<u>Issues to be considered:</u>

- As the LGPS is a funded scheme, with 11 individual funds, 3-yearly valuations are carried out for each fund by an independent actuary appointed by a fund administering authority. These assess the financial position of funds and future liabilities, and set necessary future contribution rates (currently any increase in costs are carried by an increase in the employer rate). Local cost sharing arrangements could lead to differences in employee contribution rates in different geographical areas of Scotland. To ensure the LGPS is retained as a national scheme, it would therefore make more sense for cost sharing decisions to be taken at national level. However, this may lead to difficulties agreeing how cost changes should be applied in light of regional differences in scheme costs. Furthermore, it may still lead to differences in employee contribution rates at national level in comparison with the LGPS in England and Wales.

- Other public service schemes have based cost sharing mechanisms on costs relating to scheme benefits (e.g. lump sum conversion rates, changes in the usage of ill health provisions, etc) and demographic factors (e.g. changes in longevity and retirement patterns). Other assumptions impact on the cost of pensions and employer contribution rates, e.g. changes in the long term investment return expectations and discount rates. Changes in these could be excluded from the cost sharing mechanism and any changes funded only by employers. On the other hand, all factors impacting on costs could be incorporated into the cost sharing mechanism, therefore giving wider ownership to the overall performance of the scheme. This, in turn, may also require more open and participative governance arrangements for scheme funds.

- To help ensure longer term affordability, both the teachers and NHS pension scheme in Scotland have introduced a cap on the level of employer contribution rate. This means that if scheme costs continue to increase, once this cap is reached any further increase in costs would affect only the employee contribution rate. Views are sought on whether this would be beneficial for the LGPS. Introducing a cap means the scheme is sustainable for longer, which reduces the possibility of the scheme benefits having to be revised further to ensure affordability for employers and tax payers over the forthcoming period. However, on the other hand, to retain the proposed level of benefits may impact adversely on the employee contribution rate.

- With all potential cost sharing mechanisms, there are issues around ensuring the appropriate systems and processes required to implement any given mechanism are in place.

- Finally, cost sharing mechanisms would not necessarily negate the requirement to consider increasing the Scheme normal pension age in due course in line with the DWP pension white paper, which reflects changing demographics on a UK basis.

QUESTION(S) Q26, Q27, Q28 and Q29

- Do you agree that a cost sharing mechanism is sensible? If not, why not?
- Do you agree that cost sharing should be based on the cost of benefit provision only, or both this and fund investment elements?
- Please give your views on whether a ‘cap’ should be placed on employer contribution rates to improve sustainability of the LGPS over the longer term.
- Please give your views on how the principle of cost sharing could be implemented in the LGPS, and any other cost sharing issues that would need to be taken into account.

CONCLUSION

The tripartite group, consisting of representatives from COSLA, Trades Unions and the Scottish Executive has proactively developed this joint set of proposals for the new LGPS in Scotland to meet Scottish needs. The aim is to agree a final outline for a new scheme by the end of the year in order to implement this by April 2009. As well as being affordable and sustainable, the aim is to develop a scheme that is fairer for all stakeholders, whilst providing quality benefits to scheme members.

It should be noted that the proposals set out in this document illustrate a direction of travel and are provided to generate debate and gather views. They do not, therefore, represent a fait accompli or a guarantee by stakeholders that all details of the proposals will be implemented in full.

The responses from all interests to this consultation exercise will be taken into account in order to shape the final version of the new scheme to be agreed for Scotland. However, it should be recognised that ‘picking and mixing’ the provision of specific benefits directly impacts on the affordability of the whole scheme. If any one aspect of the scheme is changed, this may require changes in another area to balance costs.

The tripartite group welcomes all views and comments by 31 October 2007.

SECTION 5

NEXT STEPS / TIMETABLE

THE NEW SCHEME

1. It is intended that the new scheme comes into effect on 1 April 2009 with regards to both new entrants and future accruals for existing scheme members.

2. In order to meet this deadline, the following programmed steps are necessary:

July – Oct 2007	Consultation exercise
31 Oct 2007	Deadline for responses to this consultation exercise
November 2007	Consideration of comments received from consultation exercise and decisions to be made on new scheme outline
Dec 2007 to Feb 2008	Consultation on draft regulations for the new scheme
April 2008	Regulations to be laid in the Scottish Parliament
April 2009	Regulations governing the new scheme take full effect

CONSULTATION RESPONSES

3. Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with the access to information regimes (these are primarily the Freedom of Information (Scotland) Act 2002 (FOISA) and the Data Protection Act 1998 (DPA).

4. To ensure that your response is treated according to your wishes, please ensure that you complete and return the enclosed Respondent Information and Response Form as part of the consultation questionnaire (Annex A).

5. The completed Respondent Information Form and response should be returned, by the deadline of **31 October 2007**, to Jean Steel, Policy Officer, Scottish Public Pensions Agency, 7 Tweedside Park, Tweedbank, Galashiels TD1 3TE. Electronic responses can be sent to locgovpensionsreform@scotland.gsi.gov.uk.

6. Following the closing date, all responses will be analysed and considered, along with any other available evidence, to enable a decision to be reached on the content of the new Local Government Scheme in Scotland. In due course, feedback will be issued on the responses made to this consultation process, and the aim is for draft regulations for the new scheme to be prepared for consultation by the end of the year.

Annex A

PROPOSALS FOR A NEW LOCAL GOVERNMENT PENSION SCHEME IN SCOTLAND

CONSULTATION RESPONSE FORM

The closing date for this consultation is 31st October 2007. Your comments must reach us by that date

Please ensure that you also complete the Respondent Information Form to ensure we handle your response according to your wishes.

Responses can be returned either by post to:

Jean Steel
Policy Officer
Scottish Public Pensions Agency
7 Tweedside Park
Tweedbank
Galashiels
TD1 3TE

or e-mail to: locgovpensionsreform@scotland.gsi.gov.uk

This questionnaire can be downloaded as a 'word' document from the Local Government Scheme Reforms page in the Pensions Reforms & Taxation area at www.sppa.gov.uk to enable respondents to complete and return their responses electronically.

The Scottish Executive Consultation Process

Consultation is an essential and important aspect of Scottish Executive working methods. Given the wide-ranging areas of work of the Scottish Executive, there are many varied types of consultation. However, in general, Scottish Executive consultation exercises aim to provide opportunities for all those who wish to express their opinions on a proposed area of work to do so in ways which will inform and enhance that work.

The Scottish Executive encourages consultation that is thorough, effective and appropriate to the issue under consideration and the nature of the target audience. Consultation exercises take account of a wide range of factors, and no two exercises are likely to be the same.

Typically Scottish Executive consultations involve a written paper inviting answers to specific questions or more general views about the material presented. Written papers are distributed to organisations and individuals with an interest in the issue, and they are also placed on the Scottish Executive web site enabling a wider audience to access the paper and submit their responses (in this instance the document is available through the SPPA website). Consultation exercises may also involve seeking views in a number of different ways, such as through public meetings, focus groups or questionnaire exercises. Copies of all the written responses received to a consultation exercise (except those where the individual or organisation requested confidentiality) are placed in the Scottish Executive library at Saughton House, Edinburgh (Y Spur, Saughton House, Broomhouse Drive, Edinburgh, EH11 3XD, telephone 0131 244 4565).

All consultation papers and related publications (eg, analysis of response reports) can be accessed on the Scottish Public Pensions Agency website in the Pension Reforms and Taxation area

The views and suggestions detailed in consultation responses are analysed and used as part of the decision making process, along with a range of other available information and evidence. Depending on the nature of the consultation exercise the responses received may:

- indicate the need for policy development or review
- inform the development of a particular policy
- help decisions to be made between alternative policy proposals
- be used to finalise legislation before it is implemented

Final decisions on the issues under consideration will also take account of a range of other factors, including other available information and research evidence.

While details of particular circumstances described in a response to a consultation exercise may usefully inform the policy process, consultation exercises cannot address individual concerns and comments, which should be directed to the relevant public body.

RESPONDENT INFORMATION FORM: NEW LOCAL GOVERNMENT PENSION SCHEME IN SCOTLAND

Please complete the details below and return it with your response. This will help ensure we handle your response appropriately. Thank you for your help.

NAME: ORGANISATION NAME: (if appropriate)	POSTAL ADDRESS

1. Are you responding: (please insert a 'x' in one box)

(a) as an individual		go to Q2a/b and then Q4
(b) on behalf of a group / organisation		go to Q3 and then Q4

INDIVIDUALS

2a. Do you agree to your response being made available to the public (in the Scottish Executive library)

Yes (go to 2b below)		
No, not at all		We will treat your response as confidential

2b Where confidentiality is not requested, we will make your response available to the public on the following basis.

Yes, make my response, name and address all available	
Yes, make my response available, but not my name or address	
Yes, make my response and name available, but not my address	

ON BEHALF OF GROUPS OR ORGANISATIONS

3. The name and address of your organisation will be made available to the public (in the Scottish Executive library). Are you also content for your response to be made available?

Yes		**No**		We will treat your response as confidential

SHARING RESPONSES / FUTURE ENGAGEMENT

4. We will share your response internally with other Scottish Executive policy teams who may be addressing the issues you discuss. They may wish to contact you again in the future, but we require your permission to do so. Are you content for the Scottish Executive to contact you again in the future in relation to this consultation response?

Yes		**No**	

We would be grateful if you would use this consultation questionnaire for your comments as this will aid our analysis of the responses received.

Please insert an 'X' in either of the 'Yes' / 'No' or other choice boxes throughout the document.

NB: The space allocated to each section for your comments may seem limited, but if you are completing this electronically the space will expand as you insert text.

Q 1(a) Are there other benefits that you would like to see included as part of the new scheme proposals?	**YES**	**NO**
Q 1(b) If you have answered 'YES' please give details below		

If it is agreed, following consultation, that certain elements of the scheme outline should be altered, this may lead to an increase in costs that would impact on the overall affordability of the proposal. What changes would you propose in this situation? For example, the member contribution rate could be increased or the level of other scheme benefits could be reduced. It would be helpful to know your views, therefore, about the level of importance that you would place on each given feature within the new scheme proposals, in order to ensure that benefits that are most important to stakeholders would be retained.

Q 2 Please order the following features of the proposals according to the level of importance that you would place on their provision, by inserting the numbers 1 to 10 in the box beside each feature, where '1' is 'most important' and '10' is 'least important'.

Scheme Feature	**Priority No.**
Type of Scheme - Final salary scheme	
Accrual rate	

Death in Service Arrangements	
Ill Health benefits	
Partner Pensions	
Flexible Arrangements in run-up to retirement	
Contribution Rates for Employers	
Contribution Rates for Scheme Members	
Transfer Options between current and new scheme	
Other – please give details	

TYPE OF SCHEME

Q 3(a) Do you agree with the proposal that the new LGPS should remain a Defined Benefit Final Salary scheme?	**YES**	**NO**
Q 3(b) If you have answered 'NO', what type of scheme would you prefer and why?		

ACCRUAL RATES

Q 4(a) Do you agree with the proposal that the accrual rate should be increased to 1/60th?	**YES**	**NO**
Q 4(b) If you have answered 'NO' what rate of accrual would you prefer and why?		
Q 4(c) If your preferred rate of accrual is greater than 1/60th, what changes should be implemented to ensure the scheme remains affordable?		

DEATH IN SERVICE ARRANGEMENTS

Q 5(a) Do you agree that the death in service benefit should be increased to 3 x final pay?	**YES**	**NO**
Q 5(b) If you have answered 'NO', what level of death in service benefit would you prefer and why?		

Q 6(a) Do you agree with the proposed changes to spouses' pensions?	**YES**	**NO**
Q 6(b) If you have answered 'NO', what changes to the spouses' benefit would you prefer and why?		

ILL HEALTH BENEFITS

Q 7(a) Would you prefer a two or three tier ill health arrangement?	**Other**	**2 Tier**	**3 Tier**
Q 7(b) If you have chosen 2 or 3 tier, please explain why you have made this choice			
Q 7(c) If neither of these options are preferable, please outline what an alternative arrangement might look like.			

Q 8(a) Would any of the 3 tiers require a criteria to be inserted to reflect permanence until age 65?	**Tier 1**		**Tier 2**		**Tier 3**	
	Y	**N**	**Y**	**N**	**Y**	**N**

Q 8(b) Please explain why you have come to this conclusion.

Q 9(a) Do you agree with the proposed definitions of 'reasonable prospect', 'gainful employment' and 'reasonable period'?	**YES**	**NO**
Q 9(b) If you have answered 'NO', can you please comment on each definition?		

Q 10(a) Do you agree that implementation of certificate of protection provision should cover persons who step down to lower paid posts as a result of ill-health?	**YES**	**NO**
Q 10(b) If you have answered 'NO', can you please explain why?		

PARTNER PENSIONS

Q 11(a) Do you agree to the proposal to provide partner pensions to spouses, civil partners and cohabiting partners at a rate of 1/160th?	YES	NO
Q 11(b) If you have answered 'NO', what rate(s) would you prefer and why?		

Q 12(a) Do you agree with the proposed criteria for defining partners who cohabit?	YES	NO
Q 12(b) If you have answered 'NO', what criteria would you prefer and why?		

FLEXIBLE ARRANGEMENTS IN THE RUN-UP TO RETIREMENT

Q 13(a) Do you agree that current flexible retirement provisions should be retained?	YES	NO
Q 13(b) If you have answered 'NO', which provisions should be removed, and why?		

Q 14(a) Do you agree that increased flexibility should be provided through being able to draw all or part of occupational pension benefits without having to retire completely?	YES	NO
Q 14(b) If you have answered 'NO', please explain why		

Q 15(a) Do you agree with the provision to buy additional pension benefit, and cost-neutral uplift factors for benefits accrued beyond age 65?	YES	NO
Q 15(b) If you have answered 'NO', please explain why		
Q 15(c) What other cost neutral provisions would you like to see made available to support flexible retirement?		

CONTRIBUTION RATES FOR SCHEME MEMBERS

Q 16(a) Do you agree that the proposed employee contribution rate is fair, given the level of benefits proposed?	**YES**	**NO**
Q 16(b) If you have answered 'NO' please explain why and what your preference would be?		

Q 17(a) Do you agree that the LGPS should incorporate a tiered contribution rate system	**YES**	**NO**
Q 17(b) If you have answered 'NO' please explain why?		

Q 18(a) Which of the illustrative tiered contribution rate options do you feel is preferable?	**OPTION**			
	1	**2**	**3**	**Other**
Q 18(b) If you have chosen Option 1, 2 or 3, please explain why you prefer this option?				

Q 18(c) If none of these options seem suitable, please provide details of an alternative mechanism.
Q 18(d) What implementation costs and issues do we need to be aware of, and what solutions are there to operationally implementing a tiered contribution system. For example, how should contributions be determined where a member has more than one salaried job within the local government workforce?

CONTRIBUTION RATES FOR EMPLOYERS

Q 19(a) Do you agree with the move towards a 2:1 ratio between employer and member contributions rate?	**YES**	**NO**
Q 19(b) If not, what would you prefer and why?		

TRANSFER OPTIONS BETWEEN THE CURRENT AND NEW SCHEME

Q 20(a) Which transfer option do you prefer?	OPTION		
	Other	1	2

Q 20(b) Why have you chosen this option?

Q 20(c) If neither, please give details of your preferred alternative approach.

Q 20(d) If Option 1 is preferred, please give your views on whether you would wish the actual level of member benefits to be transferred, or for an enhanced transfer rate to be applied. If an enhanced transfer rate is to be applied, and this results in the scheme becoming unaffordable, what changes should be implemented to ensure the scheme remains affordable? For example, other benefits could be reduced or member contribution rates could be increased.

GOVERNANCE

Q 21(a) Do you agree that the LGPS scheme governance arrangements should be reviewed?	YES	NO
Q 21(b) Why have you chosen this option?		
Q 21(c) If you have answered 'YES' who should undertake this review and what should the specific focus of the review be?		
Q 21(d) Please give any views on the value and/or practicalities of the potential actions which may be implemented to strengthen governance and consultative processes across the LGPS, for example member nominated representative participation on scheme committees, development and implementation of equality proofing good practice, and a national tripartite group to oversee the LGPS.		
Q 21(e) Please detail any other suggestions and comments you have on LGPS governance arrangements.		

EQUALITY IMPACT ASSESSMENT

Q 22(a) Are you aware of any equality issues that arise from the new scheme proposals?	**YES**	**NO**
Q 22(b) If you have answered 'YES' please give details below.		

ACTUARIAL ASSUMPTIONS

Q 23(a) Do you agree with the assumptions used to underpin the development of the new scheme proposals?	**YES**	**NO**
Q 23(b) If you have answered 'NO', please give evidence to support alternative assumptions.		

Q 24(a) Do you agree that the proposed employer contribution rate is fair, given the level of benefits proposed?	**YES**	**NO**
Q 24(b) If you have answered 'NO', please explain why and what your preference would be.		

Q 25(a) Do you think the contributions are affordable in the long term?	**YES**	**NO**
Q 25(b) Please explain why you have reached this conclusion.		

ENSURING SUSTAINABILITY OVER THE LONGER TERM

Q 26(a) Do you agree that a cost sharing mechanism is sensible?	**YES**	**NO**
Q 26(b) If you have answered 'NO' Please explain why.		

Q 27(a) Do you agree that cost sharing should be based on the cost of benefit provision, or both this and fund investment elements?	**BENEFITS ONLY**	**BENEFITS AND INVESTMENT**
Q 27(b) Please explain which option you prefer and why?		

Q 28 Please give your views on whether a 'cap' should be placed on employer contribution rates to improve sustainability of the LGPS over the longer term.
Q 29 Please give your views on how the principle of cost sharing could be implemented in the LGPS and any other cost sharing issues that would need to be taken into account.

ANY OTHER COMMENTS

Q 30 Please outline any other comments you have to make, either on specific scheme benefits or the proposed benefit package generally.

Thank you for taking the time to let us have your views.

We do not intend to acknowledge individual responses unless you place an 'X' in the box below.

Please acknowledge this reply	