Local Government Pension Scheme, 2008 reforms

Standard Note: SN/BT/4115

Last updated: 13 January 2011

Author: Djuna Thurley

Business and Transport Section

The Local Government Pension Scheme (LGPS) is a funded, statutory, final salary public service pension scheme. Like many other public sector pension schemes, it has recently been reformed. A "new look" scheme was introduced in England and Wales in April 2008, has an accrual rate of $1/60^{th}$ (compared to the previous $1/80^{th}$ rate and an automatic lump sum with a $3/80^{th}$ accrual). Contribution rates are tiered according to earnings, with the intention of a greater yield overall without imposing too great a burden on lower paid workers. Survivors' benefits available to spouses and civil partners have been extended to cohabiting partners. There are now three tiers of ill-health benefits. Consideration has been given to how a "cost-capping and sharing" mechanism could be introduced.

This note covers developments since 2006. For more recent developments, see SNBT 5823 *Local Government Pension Scheme, 2010 onwards.* Developments before this date are in SN/BT/2940, *Local Government Pension Scheme: changes 2001-2005.* The rule of 85 is covered in more detail in a separate standard note, *SN/BT/4002*, *Local Government Pension Scheme: 85 year rule.*

Contents

1 Background

1.1 Framework of the scheme

The Local Government Pension Scheme (LGPS) is a registered, funded, statutory, public service pension scheme. It is contracted-out of the State Second Pension. Its rules are in regulations made under section 7 of the *Superannuation Act 1972*. The scheme is sponsored centrally by the Department for Communities and Local Government (DCLG), which is responsible for the scheme's stewardship and maintaining its regulatory framework.[1] The Secretary of State is required to consult before making regulations.[2] It is administered, managed and funded at local level.[3] There are 89 pension funds in the Local Government Pension Scheme in England and Wales.[4]

Local government employees in Scotland are covered by a separate, but very similar, scheme. It is regulated by the Scottish Public Pensions Agency (SPPA), an Executive Agency of the Scottish Executive, but administered by fund administering authorities, of which there are 11 in Scotland. Like the scheme in England and Wales, the rules of the Scottish scheme are defined in a series of regulations made under section 7 of the *Superannuation Act 1972*. Key features of the reformed scheme introduced from April 2009 were:

- retention of a normal retirement age of 65 but with flexibility to work reduced hours
- beyond 65 while taking part of their pension
- employee contribution rates increased to an average of 6.3%. Contributions will be tiered so lower paid staff pay less and higher paid staff more for the benefits they draw
- lower average employers' contribution rates, reduced from 13.9% to 13.3%
- the new LGPS will mirror other schemes in providing 1/60th of final salary for each year in service
- modernised partners' pensions - lump sum death in service grants increase from two to three times final pay and cohabiting partners now able to receive benefits.[5]

More information on the scheme in Scotland, see the SPPA website.

2 Scheme rules

The main provisions relating to benefits, membership and employee contributions are in the *Local Government Pension Scheme (Benefits, Membership and Contributions) Regulations 2007* (SI 2007 No. 1166), as amended. The administrative arrangements and processes are in the *Local Government Pension Scheme (Administration) Regulations 2008* (SI 2008/239), as amended. A short description of the conditions of membership and the main benefits that

1 ODPM, *Facing the future - Principles and propositions for an affordable and sustainable Local Government Pension Scheme in England and Wales*, October 2004
2 Superannuation Act 1972, s7 (5)
3 ODPM, *Facing the future - Principles and propositions for an affordable and sustainable Local Government Pension Scheme in England and Wales*, October 2004
4 Ibid
5 The Scottish Government Press Release, Fairer and Affordable Local Government Pension Scheme, 14 February 2008

apply was issued by LGPS in April 2008.[6] More detailed information can be found in a series of scheme guides.[7]

Briefly, the LGPS is available to all employees in local government, or in other organizations that have chosen to participate in it. Teachers, police officers, firefighters and employees eligible to join another statutory pension scheme are not allowed to join the LGPS. Employees of local government (other than town and parish councils, to which special arrangements apply), automatically become members of the LGPS unless they opt not to join or have previously opted out, or are a casual employee.[8]

Pension benefits are based on total membership in the scheme and pensionable pay, usually in the final year of service. If a person is part-time, their scheme membership will count as its part-time length when working our their pension and their final pay is increased to what it would have been, had they been full-time. The accrual rate from 31 March 2008 is 1/60th. Subject to certain limits, up to 25% of the capital value of pension benefits can be taken as a tax-free lump sum. £12 lump sum is received for each £1 of pension given up. For membership before 31 March 2008, a member can receive an annual pension based on 1/80th of the final year's pensionable pay and an automatic tax-free lump sum of three times their pension.[9]

LGPS will pay **survivors' benefits** to widows, widowers, civil partners and, subject to certain qualifying conditions, to a nominated cohabiting partner. Pensions are also payable for eligible children. Members can nominate who they would like any death grant paid to.[10]

Prior to the introduction of reforms in April 2008, there was a standard **employee contribution rate** of 6%, except for certain members with "lower rate rights", who contributed at 5%.[11] Contribution rates are now tiered according to the level of pensionable pay.[12] The pay bands and rates applying from 2010 are:[13]

Whole-time pay rate	Contribution rate
Up-to £12,600	5.5%
£12,601 to £14,700	5.8%
£14,701 to £18,900	5.9%
£18,901 to £31,500	6.5%
£31,501 to £42,000	6.8%
£42,001 to £78,700	7.2%
More than £78,000	7.5%

6 House of Commons Deposited Paper, DEP 2008-1080
7 Local Government Employers website, Local Government Pension Scheme guides
8 DCLG, *Where next? – Options for a new-look Local Government Pension Scheme in England and Wales,* June 2006
9 Ibid
10 Ibid
11 *Local Government Pension Scheme Regulations 1997*, regulation 12.
12 *Local Government Pension Scheme (Benefits, Membership and Contributions) Regulations 2007 (SI 2007 No, 1166)*, reg 3
13 Local Government Employers, A brief guide to the Local Government Pension Scheme in England and Wales, (Updated October 2010)

Employer contributions are varied, on the basis of triennial actuarial valuations of each fund's assets and liabilities, in order to ensure that LGPS benefits are properly funded (see also, section 5 below).[14]

3 Reforms introduced in 2008

3.1 2004 consultation - Facing the future

The process of reforming the Local Government Pension Scheme started with the publication of *Facing the Future,* published by the Labour Government in October 2004. The proposals in this document were aimed at:

> Scheme modernisation to reflect the broader employment context of local government in the 21st century;
>
> Improving the Scheme's inherent attractiveness to employees and employers;
>
> Providing a simplified regulatory framework to improve understanding, application and review;
>
> Ensuring value for money for stakeholders, including taxpayers, members and employers;
>
> Encouraging new patterns of delivery and organisation through new means of efficiency, including the use of technology, joint working and new suppliers; and
>
> Providing an affordable, secure and sustainable benefit structure.[15]

From April 2005 until September 2006, much of the discussion centred on the removal of a provision from the Scheme of the "rule of 85", which provided for some people to retire on a full pension under the age of 65. The High Court ultimately confirmed that this was discriminatory on grounds of age.[16] The *Local Government Pension Scheme (Amendment) Regulations 2006*, SI 2006/966, abolished the 85 year rule with effect from 1 October 2006, with some transitional protection.[17] The same regulations introduced changes to reflect the new pension tax regime introduced under the *Finance Act 2004*, on 6 April 2006. Principal among these were:

- Facility to count more than 40 years membership of the scheme;
- Facility to increase the amount of tax free lump sum by means of commuting part of pension;
- Removal of previous limits on contributions;
- Removal of the earnings cap, with steps taken to avoid windfall gains for some higher paid members; and

---

14 *Local Government Pension Scheme (Administration) Regulations 2008* (SI 2008, No. 239), Part IV; Local Government Pension Scheme website – About the LGPS

15 ODPM, 'Facing the future: Principles and propositions for an affordable and sustainable Local Government Pension Scheme in England and Wales', October 2004, para A 1.9

16 Explanatory Memorandum to the *Local Government Pension Scheme (Benefits, Membership and Contributions) Regulations 2007* (2007 No. 1166)

17 Ibid, para 7.2-3

- Introduction of preliminary but significant steps towards the concept of flexible retirement, which will smooth scheme members' transition from employment to retirement. [18]

Discussion on the transitional arrangements following the removal of the rule of 85 continued. This is discussed in more detail in Library Standard Note SN/BT 4002, *Local Government Pension Scheme: rule of 85.*

3.2 New Look Consultation Document, June 2006

On 30 June 2006, the Department for Communities and Local Government (DCLG) published a consultation document, *Where next? – Options for a new-look Local Government Pension Scheme in England and Wales*. This proposed four (or five) very different schemes as a replacement for the existing scheme:

> **Option A** is an updated version of the current scheme with its current accrual rate of 1/80th and an automatic tax-free lump sum on retirement of 3/80ths of pension
>
> **Option B** is a new final salary scheme, with an improved accrual rate of 1/60th, but with no automatic tax-free lump sum on retirement
>
> **Option C1** is a new career-average scheme, with an accrual rate of 1.85% and RPI re-valuation
>
> **Option C2** is a new career-average scheme, with an accrual rate of 1.65% and wage inflation revaluation
>
> **Option D** is a new hybrid scheme, in which scheme members would have a one-off choice to either receive career-average linked benefits, or to make extra contributions in order to receive final salary linked benefits.[19]

The Government was careful to state that it had no preferred option.

All the options would improve the scheme's death in service benefits from two to three years' pay and provide partners' pensions for cohabitees. They would also introduce two tier ill-health pension provisions. Only the top tier (likely to be 5-15% of ill health retirees) would receive an enhancement of their existing membership by 50% of their prospective service up to age 65. The top tier would cover people who are permanently unfit to perform the duties of their local government employment and whose incapacity is such that they are unlikely to secure gainful or regular employment again. The second tier (those who are judged to be capable of undertaking other regular employment) would not receive enhancement but would receive immediate and unreduced payment of accrued benefits. The consultation document included costings and a range of possible contribution rates associated with the different options. [20]

The consultation period ended on 29 September 2006. The Government said there was "clear and strong consensus amongst respondees to the *Where Next?* consultation indicating significant support for a final-salary scheme which meets the test of affordability,

---

[18] Ibid, para 7.4

[19] DCLG, LGPS "Options" Consultation Paper, Q&A, 30 June 2006

[20] DCLG, Where next? – Options for a new look Local Government Pension Scheme in England and Wales, June 2006, Annex 1

viability and fairness to members employers and taxpayers."[21] Support for Option A (an updated version of the existing scheme), however, "did not take account of the need to recycle 50% of the savings from the removal of the Rule of 85, as had been agreed by the Government and the main stakeholders."[22] Options C and D (a "career average" or hybrid scheme) did not receive across the board support from respondants for a number of reasons:

> Including their wish to see the LGPS compare with other public services and a failure to meet the challenge of providing a benefit package which would directly assist in recruiting, motivating and retaining staff. [23]

The then Minister for Local Government and Community Cohesion, Phil Woolas, made a statement to the House on 23 November 2006, explaining the Government's intentions:

> The consultation package will propose that the scheme remains as a final salary pension arrangement and be based on an accrual of 1/60th of salary for each year of membership. It will continue to have a normal pension age of 65, and will move towards providing, by 2010, for pensions to be paid no earlier than age 55, rather than the current minimum age of 50, except on grounds of ill-health. A revised and better targeted ill-health retirement package is to be proposed, and survivor benefits, which are available for spouses, civil partners, and children, will be extended to include other co-habiting partners. In order to help equality-proof the scheme, tiered employee contribution rates, linked to salary, will be introduced, as well as more flexible retirement provisions. Arrangements will be included which protect the accrued rights of all existing scheme members up to 31 March 2008. All present and future members of the scheme will build up rights in the new-look scheme from 1 April 2008. In addition, the protections already provided in the current scheme for eligible members, at no cost to taxpayers, following the final removal of the rule of 85 from the scheme, from 1 October 2006, will be retained.
>
> The Government is mindful of the need to maintain stability of costs in the new-look Scheme and a fair and equitable balance in its long-term resourcing between members, employers and taxpayers. The Government's intention throughout this reform process has been to ensure that no additional costs are imposed on taxpayers. It is intended, therefore, to establish an appropriate mechanism for sharing future cost pressures and to have the arrangements in place by March 2009. These will both inform and take account of the 2010 actuarial valuation of the Scheme. The new arrangements can be taken into account when individual fund actuaries set new employer contribution rates in the valuations which will take effect from 1 April 2011. This important timetable will be reflected in the new Scheme regulatory framework programmed to take effect from 1 April 2008.
>
> The package, as a whole, is both workable and affordable. Overall, it meets the balance of responses received to the recent consultation exercise and complies with

---

[21] Draft Local Government Pension Scheme Benefit Regulations 2007; Initial Regulatory Impact Assessment;
A more detailed summary of the responses was listed on the local government pensions website at: http://www.xoq83.dial.pipex.com/whatsnew.htm under the date headings 21 and 29 November 2006. Unfortunately, the information no longer appears to be accessible.

[22] Draft Local Government Pension Scheme Benefit Regulations 2007; Initial Regulatory Impact Assessment, para 26

[23] Ibid, para 24-5

> the Government's central policy objectives for the Scheme's reform, particularly in terms of its viability, affordability and fairness to members and taxpayers. [24]

A policy review group would be established to "assist in the on-going monitoring of the Scheme's regulatory and policy development"[25]

Comment

The GMB commented that while progress had been achieved there remained some outstanding issues. In particular, it asked for assurance that "no current member of the scheme will see their accrued benefits reduced when the new scheme is introduced."[26]

On 6 March 2007, representatives of UNISON's local government members welcomed "substantial improvements" in the Government's proposals, including: a guaranteed final salary scheme; the accrual rate of 1/60th, pensions for unmarried partners and improved death-in-service benefits.[27] They argued that negotiations should continue on a number of issues, in particular around:

> - contribution rates for part-time workers and those currently on a protected 5% rate;
>
> - provision for people retiring on ill-health grounds;
>
> - protection for those formerly covered by the 'rule of 85' which allowed some members to retire at 60 with an unreduced pension. [28]

4 Introduction of new look scheme - April 2008

4.1 Benefit regulations

Regulations to implement the scheme, the *Local Government Pension Scheme (Benefits, Membership and Contributions) Regulations 2007 (SI 2007 No. 1166)* (the Benefit Regulations) were laid before Parliament on 4 April 2007 and came into force on 1 April 2008. Existing employees, who were active members as at 31 March 2007 and who continue in the employment of a LGPS employer on 1 April 2008 would automatically join the new scheme on 1 April 2008. Those who opted out could elect to rejoin the LGPS at any time.[29] The Regulatory Impact Assessment explained that the main features proposed in the draft regulations form the basis of the benefit package in the finalised regulations:

> Normal Retirement Age (NRA) of 65 for release of unreduced benefit;
>
> Pension to be indexed in line with the Retail Prices Index and must come into payment before the member's 75th birthday;
>
> Earliest age for release of pension is 55 by 2010 for current members, except on grounds of ill-health;

---

24 HC Deb, 23 November 2006, c69-70; See also, Minister's statement and letter to chief executives, 23 November 2006 [viewed January 2011]

25 Ibid

26 GMB response, *Draft Regulations: The Local Government Pension Scheme (Benefits, Membership and Contributions)*

27 UNISON press release, 6 March 2007, *Local Government members back pension talks* [viewed January 2011]

28 Ibid

29 CLG, *The LGPS (Benefits, Membership and Contributions) Regulations 2007. Q and A Briefing. 15 May 2007*

Early release on objective justification basis;

Early release from age 55 on grounds of redundancy or business efficiency;

Augmentation of membership/benefits on an objectively justified basis;

Final Salary Pension based on 1/60th of salary for each year of pensionable service, with the flexible option to commute pension at the rate of £1 of annual pension for £12 of lump sum up to a maximum tax-free lump sum of 25% of capital value of accrued benefit rights at date of retirement;

The best actual in the last three years or an averaging of 3 years (financial) within the last ten;

Survivor benefits for life, payable to spouses, civil partners and "nominated" dependant partners (opposite and same sex) at a 1/160th accrual rate;

Survivor benefits payable to children at maximum accrual of 1/160th;

Revised ill-health retirement package with no review system – two levels with a higher enhancement of benefits for total incapacity; 25% (with degree of protection) enhancement with prospect of return to gainful employment;

A death in service tax-free lump sum of 3 times salary;

Post-retirement lump sum death benefit up to a maximum of 10 years before age 75;

Phased retirement arrangements that would enable LGPS members under specified circumstances to draw down some or all of their accrued pension rights from the scheme while still continuing to work;

Actuarial enhancement for those who continue in work beyond NRA of 65 without accessing their pension benefits;

Tiered employee contribution rates with 5.5% payable on first £12,000 of full time equivalent pensionable pay, and 7.5% paid on the excess over £12,000 each year[30];

A facility to purchase up to £5,000 of added annual pension; and

Facility to contribute to AVC arrangement in conjunction with external provider.

It was further announced that it would be a requirement of the Scheme Regulations to establish, by no later than 31 March 2009, guidance for the Secretary of State to issue in order to manage equitably potential increases in the future service costs of the LGPS.[31]

Some changes had been made to the proposals as a result of the consultation:

These alterations include, specifically, adjustments to provisions now covered by Regulation 19 (Early leavers: inefficiency and redundancy) and Regulation 20 (Early leavers: ill-health) as well as in Regulation 4 which deals with employee contributions and regulations 28, 34 and 37 dealing with orphaned children.

---

30 The accompanying Regulatory Impact Assessment notes that the tiered contribution rate "produces a greater yield overall, without imposing too great a burden on lower paid, predominantly female, part-timers." para 38

31 CLG, *Final Regulatory Impact Assessment, Local Government Pension Scheme (Benefits, Membership and Contributions) Regulations 2007*

> Consultees requested that consideration be given also to the revision of contribution rates to an older protected group of "manual workers" still paying an employee contribution rate of 5%. A solution has been agreed with the local authority employers and trades unions and this will be reflected in the new Scheme package by means of other, transitional provisions.[32]

The Government Actuary's Department has also produced a summary of key features of the scheme pre and post 1 April 2008.[33]

4.2 Administration regulations

In his statement on 23 November 2006, the Minister explained that the draft regulations dealing with the administrative aspects of the new Scheme would be issued for consultation.[34] Draft regulations were issued for consultation in January 2007.[35] A covering letter explained that other work was ongoing to carry over all the extant provisions of the *Local Government Pension Scheme Regulations 1997*, however:

> work on the latter is taking longer than expected and the decision has therefore been taken to come forward with a separate SI, as an amendment to the 1997 regulations, on the three measures described in paragraph 2 above. Work will continue on the extant provisions of the 1997 Regulations and will be the subject of a further statutory consultation exercise very shortly.[36]

Professional Pensions commended that:

> West Midland Pension Fund chief pensions officer Mike Woodall told PP that most of the detail needed for implementing the new-look scheme would be in the delayed regulations. "I was expecting a much more detailed set of regulations setting out the actual mechanics under which the scheme will operate." He added: "People will be seeking clarification from the DCLG as to when we will receive this detail."[37]

Two sets of regulations, the *Local Government Pension Scheme (Transitional Provisions) Regulations 2008* (SI 2008, No 238) and the *Local Government Pension Scheme (Administration) Regulations 2008* (SI 2008, No. 239) were made on 6 February 2008.[38]

4.3 Impact of the reforms

The Final Regulatory Impact Assessment (RIA) summarised the impact of the reforms as follows:

> 38. It is recognised that a final salary scheme is both attractive to potential employees and is a useful tool in recruiting and retaining LGPS members. An improved accrual rate of 1/60th is seen as particularly advantageous in comparison with the current 1/80th rate, which also provides an automatic lump sum with a 3/80th accrual. As part of the reforms, provision of a tiered contribution rate produces a greater yield overall, without imposing too great a burden on lower paid, predominantly female, part timers.

---

32 Ibid
33 Government Actuary's Department, *Local Government Pension Scheme in England and Wales – Key features pre/post 1 April 2008 (Summary as at 29/04/2008)*
34 HC Deb, 23 November 2006, WS c69-70
35 CLG, Draft *Local Government Pension Scheme (Amendment) (No.2) Regulations 2007*
36 CLG, Covering letter issued with Draft LGPS (Amendment)(No 2) Regulations 2007
37 'New LGPS administration regulations delayed', Professional Pensions, 1 February 2007
38 CLG, Covering letter, 14 February 2008

> This meets a twin aim of helping to sustain the Scheme and providing for some improving proposals to be developed further. It aims to assist lower paid members within the Scheme and is intended to encourage a higher take-up of membership from all parts of the workforce.
>
> 39. Allied to this is the need to achieve a proper balance of risk sharing between Scheme employers and active members to maintain the Scheme's sustainability. This will be done through regulatory mechanisms, to be in place by no later than March 2009, which ensure costs are contained and that equitable principles of sharing costs are adopted. [39]

The RIA explained that reforms were needed so that 50% of the savings from removing the "rule of 85" could be recycled into the LGPS:

> Following ministerial assurance earlier in the year that 50% of the saving to be made from the removal of the Rule of 85 would be recycled into the Scheme, a failure to reform would contradict this agreement which was also supported by LGPS interested parties.[40]

On 27 October 2008, the then Minister for Local Government, John Healey, provided an estimate of the annual savings from the reforms:

> Reforms to the Local Government Pension Scheme in England and Wales took effect from 1 April 2008 based on benchmark costs provided by the Government Actuary's Department and agreed with key stakeholders, within a total cost envelope of 19.5 per cent. of total pensionable payroll. The net assumed annual savings arising from the reforms in respect of future accrual of pension rights is estimated at some 1.3 per cent. of pensionable payroll, which was estimated to be some £30 billion for the year 2007-08.[41]

The Pensions Policy Institute published an assessment of the Government's reforms to public sector pensions in October 2008. It found that:

> The reforms to the Local Government pension scheme are estimated to reduce employer contributions by £340 million a year, or by 7% of the pre-reform employer cost. Since this scheme is funded, these savings mean a direct reduction in the annual cost of the scheme to taxpayers.[42]

An article in *Pensions Week* in April 2008 suggested that the true costs of the reformed scheme would not be known for some time:

> The journey toward April 1 2008 and the introduction of the new LGPS, has been a long one. For employers, the true cost of the scheme will only become evident once administration procedures have been in place for some time and the outstanding issue

---

39 CLG, *Final Regulatory Impact Assessment, Local Government Pension Scheme (Benefits, Membership and Contributions) Regulations 2007,* para 38

40 Ibid, para 36

41 HC Deb, 27 October 2008, c723W

42 Pensions Policy Institute, *An assessment of the Government's reforms to public sector pensions,* October 2008, p28

surrounding the third tier ill-health benefit is finalised. Only time will tell, but there is a real possibility that this may not be the end of the changes for this sizeable scheme.[43]

4.4 Establishing a cost-sharing mechanism

One of the objectives of the recent public sector pension reforms has been to ensure "long-term sustainability of the schemes". For this reason, negotiations on reforms of the teachers, NHS and civil service schemes have included agreements on "cost sharing" and "cost capping". These are to:

> …ensure that any future increases in costs will be fairly shared between employers and employees. In addition, the cost capping mechanism will ensure that there will be an upper limit on the costs to the tax payer should costs increase [44]

The Government's intention throughout the process of reviewing the LGPS has been to ensure that "no additional costs are imposed on taxpayers". It has therefore announced its intention to establish "an appropriate mechanism for sharing future cost pressures":

> The Government are mindful of the need to maintain stability of costs in the new-look scheme and a fair and equitable balance in its long-term resourcing between members, employers and taxpayers. The Government's intention throughout this reform has been to ensure that no additional cost are imposed on taxpayers. It is intended, therefore, to establish an appropriate mechanism for sharing future cost pressures and to have the arrangements in place by March 2009. These will both inform and take account of the 2010 actuarial valuation of the scheme. The new arrangements can be taken into account when individual fund actuaries set new employer contribution rates in the valuations which will take effect from 1 April 2011..[45]

An informal consultation paper, *Sustaining the Local Government Pension Scheme in England and Wales* was published in February 2008. This explained the need to develop a cost-sharing approach that would be appropriate to the LGPS, given its nature as a funded and multi-employer scheme. It was proposed to establish a model national fund which would be used to calculate the proportion of costs (or savings) falling to members. This amount could be recognised through a change on contribution rates or in benefits. This change would then be fed back into the local valuation process to determine the local employer contribution rate:

> 26. Given the nature of the LGPS, it is essential to provide a cost-share arrangement which is relevant to it. In particular, its funded and varied multi-employer status renders the approach taken by the unfunded, centrally-managed public service Schemes as not being appropriate. The distortions this would create would indeed undermine the status of the Scheme as a single national arrangement, raising questions as to its continued status as a single scheme. It would be technically difficult also, and too complex to establish a cost-share for every local single LGPS employer. Instead, therefore, a bespoke LGPS approach, but still encompassing the essence of the Government's requirements for public service schemes is required specifically to meet the needs of the Scheme, and its shared holders.

43 Delderfield G, 'The insider: Personal view – This could well be the first of many makeovers for the new-look LGPS", Pensions Week, 14 April 2008

44 HL Deb, 27 October 2008, c1397W

45 HC Deb, 23 November 2006, c 70-72WS

> 27. To simplify the process, therefore, one proposed approach is to establish a model, national fund and for it to be maintained centrally by CLG, with the assistance of the Government Actuary's Department with the co-operation of key stakeholders. The model scheme would represent the position of all LGPS funds, but would be adjusted accordingly, to only take into account those items included within the cost-share model. Maintaining a centrally-managed model scheme would also enable the efficient running of "what if" scenarios which would otherwise need to be complied as the aggregate of numerous local calculations.
>
> 28. The model, national fund would be used to calculate the proportion of costs (or savings) which fall to the member. This amount could be recognized by an increase (decrease) in the members' contribution rate, or a change in the benefits provided by the scheme. The output of the model scheme (e.g. a change to the member contribution rate) would then be fed back into the local valuation processes to determine the local employer rate necessary to locally finance scheme benefits. [46]

It was proposed that stability of contribution rates could be improved by having regard to fluctuations over the longer term and by adopting a long period over which any surplus or deficit was spread. An average of 20 years is "not untypical in LGPS funds":

> 32. An important aim is to ensure stability throughout all elements of this mechanism. The stability of the contribution rates could be improved by having regard to long term rather than short term fluctuations in experience and by adopting a long period over which any surplus or deficit is spread. Typically, private sector pension schemes adopt an amortisation period of around 10 years as this is the longest period normally permitted by the Pensions Regulator. However, the LGPS is exempt from this requirement and amortization periods on average of some 20 years are not un-typical in LGPS funds. The current 2007 actuarial valuation average amortization period could, at the outset, be adopted in the notional fund. Views are sought on how this could be managed.

It was proposed that costs emerging from the model scheme should be shared between employers and members on a "50:50 basis" and that employer contributions should be subject to a cap.[47]

Draft regulations were published for consultation on 27 November 2008.[48] *The Local Government Pension Scheme (Amendment) Regulations 2009* (SI 2009 No. 1025) came into force on 15 May 2009. These require administering authorities to provide fund data to the Secretary of State which will be used to produce guidance for the national model fund. The outputs of this will enable the Secretary of State to determine national benchmark and overall costs of the Scheme in terms of future accrual of liabilities and any impacts of unforeseen future experience on past service liabilities. Where this guidance leads to changes to benefits payable or employee contribution rates, the regulations will enable actuaries to amend employer contribution rates where appropriate in individual pension funds from the second year following the 2010 valuation – i.e. with effect from 1st April 2012:

> 7.4 The Scheme, as it applies to England and Wales, comprises 89 separate and individually managed pension funds, each of which is the responsibility of a designated local administering authority. The purpose of these Regulations is

---

46 DCLG, *Sustaining the Local Government Pension Scheme in England and Wales,* February 2008

47 Ibid, para 42-44

48 DCLG letter 27 November 2008

therefore to enable the collection all of the individual fund data and for that data to be actuarially assessed on the basis of a single national model fund .This is achieved by virtue of regulation 3(a) of these Regulations which introduces a new regulation 36A to the Administration Regulations.

7.5 Regulation 36A(2) requires administering authorities to provide all their fund data to the Secretary of State by 31st August 2010, and triennially thereafter. Regulation 36A(3) requires the Government Actuary to provide by 31st October 2010, and triennially thereafter, an actuarial valuation based on the data received from the administering authorities in order to provide the Secretary of State with a valuation report and an overall cost certificate. Regulations 36A(4) and (5) specify what information the valuation report and costs certificate must contain.

7.6 Following receipt of the specified information, the Secretary of State will be in a position to produce guidance on the actuarial assumptions and methodology adopted in the model fund (regulation 36A(1)).

7.7 The timescales specified in this instrument (in new regulation 36A(2), (3) and (5)) will allow individual fund authorities and Scheme employers to prepare for the setting of new cost sharing arrangements when individual fund actuaries set new employer contribution rates at the next actuarial valuation as at 31 March 2010. The regulatory timetable imposes a transparent framework and discipline within which the specified parties must operate. It also recognises the statutory responsibilities of the Secretary of State for the Scheme.

7.8 The outputs of this national model fund will enable the Secretary of State to determine national benchmark and overall costs of the Scheme in terms of future accrual of liabilities and any impacts of unforeseen future experience on past service liabilities. The national costs will vary from those established at local level as the model will assume the model fund is fully funded, and statistical smoothing will occur when data is aggregated across all funds and all members. Administering authorities and employers will need to understand the relationship between these costs presented in guidance and their own local pension fund employer costs, planning for future variations as necessary.

7.9 Where this guidance leads to changes to the benefit package available, or the contribution rates applying under the Benefits Regulations to employees, the new regulation 38A, introduced by regulation 3(b) of these Regulations, will enable actuaries to amend employer contribution rates where appropriate in individual pension funds from the second year following the valuation – ie with effect from 1st April 2012.[49]

4.5 Development of a three tier ill-health retirement provision

Prior to April 2008, an LGPS member could retire early on an enhanced pension if they were considered permanently unable to do their job, or any comparable job with their employer. A 2003 leaflet for LGPS scheme members explained:

What happens if I have to retire early due to ill health?

If you have at least two years total membership or have brought a transfer value into the LGPS and an administering authority approved independent registered medical

[49] Explanatory Memorandum to *The Local Government Pension Scheme (Amendment) Regulations 2009* (SI 2009 No. 1025)

practitioner certifies that you have become permanently unable to do your job, or any comparable job with your employer, efficiently because of ill health or infirmity of mind or body, you will receive your pension and lump sum immediately. The medical practitioner must be qualified in occupational health medicine and must not have previously been involved in your case.

How is an ill health pension and lump sum calculated?

Ill health pensions and lump sums are calculated in the same way as detailed in the section on Retirement Benefits, except that the total membership used in the calculation will be increased if your total membership, excluding any additional membership granted by your employer, is five or more. This is to reflect the fact that you are having to retire early. The amount by which it will be increased is shown in the table below.

Total membership	**Total membership after increase awarded**
Less than 5 years	Actual **total membership** only
Between 5 and 10 years	**Total membership** doubled
Between 10 and 13 1/3 years	**Total membership** increased to 20 years
Between 13 1/3 and 33 1/3 years	**Total membership** increased by 6 2/3 years
Between 33 1/3 and 40 years	**Total membership** increased to 40 years
Over 40 years	Actual **total membership** only

Your increased membership, however, must not exceed the **total membership** you would have accrued had you continued until age 65.[50]

In October 2000, HM Treasury published a *Review of Ill-Health Retirement in the Public Sector action plan, which* included the requirement to introduce a two tier ill-health retirement pension arrangement.[51] A working group was set up to look at how this should be taken forward.

A Communities and Local Government (CLG) consultation paper published in June 2006, proposed the introduction of a two tier arrangement in the LGPS:

The top tier

8.6 The top tier provision would cover those scheme members who are permanently unfit to perform the duties of their local government employment and whose incapacity is such that they are unlikely to secure gainful or regularemployment again.

8.7 Consultees views are invited on what criteria should be used to define "regular employment". These criteria would need to take account of the diverse nature of the

---

[50] LGPS, *A Guide to the Local Government Pension Scheme,* May 2003

[51] HM Treasury press release,' Action needs to be taken to reduce ill health retirement: conclusions of Treasury review published', 11 July 2000

LGPS workforce. One example is the Firefighters' schemes, in which "regular employment" is defined as being "not less than 30 hours per week on average over a twelve month period".

8.8 Those ill-health retirees satisfying the top tier criteria would receive benefits based on an enhancement of their existing membership by 50% of their prospective service up to the scheme's normal retirement age of 65. Consideration could be given as to whether local authority employers should have the facility to award more than the 50% enhancement in individual cases where more generous awards can be justified on compassionate grounds.

The second tier

8.9 The second tier provision would cover those members who cease employment with a Scheme employer on the grounds of incapacity, but who are judged to capable of undertaking other regular employment.

8.10 Those ill-health retirees satisfying the second tier criteria would not receive enhancement of their existing membership, but would receive immediate and unreduced payment of their accrued benefits.

Review arrangements

8.11 A key element of the two tier arrangement will be whether ill-health retirement cases are to be kept under review, with the entitlement to benefits being adjusted according to changes in circumstances. Such a review would need to be done by scheme employers in conjunction with their medical advisers and/or independent registered medical practitioners. [52]

The working group considered that a third tier was necessary to cover those able to undertake gainful employment within a reasonable period of time:

7. Although the HM Treasury review focussed its attention on a two tier ill-health pension arrangement, the working group set up by the then DETR to take forward implementation of the action plan considered that the range of incapacities covered by the second tier from those just short of meeting the top tier criteria and those who would be capable of obtaining gainful employment almost immediately after ceasing their local government employment on permanent ill-health grounds, was such that an additional, third, tier was necessary for those scheme members who satisfied the permanency test in terms of their local government employment, but whose incapacity was such that they could undertake gainful employment within a reasonable period of leaving their local government employment.[53]

Following consultation, Ministers decided to come forward in April with proposals for a two tier arrangement – with a higher enhancement of benefits for total incapacity and a 25% enhancement for those with the prospect of return to gainful employment.[54] The proposal for a third tier was not taken forward at that point because "both sides of local government agreed to explore the scope for coming forward with a form of income replacement

[52] Department for Communities and Local Government, *Where next? – Options for a new-look Local Government Pension Scheme in England and Wales,* June 2006, chapter 8

[53] '*Informal guidance on ill-health retirement benefits in the new look scheme',* 4 March 2008, para 7

[54] *Local Government and Pension Scheme (Benefits, Membership and Contributions) Regulations* 2007 (SI 2007/1166), regulation 20

allowance, outwith the pension scheme to be paid by local authority employers from their revenue."[55]

In November 2007, CLG set out proposals for a third tier to cover those permanently incapable of their local authority employment but capable of obtaining gainful employment within a reasonable period. The benefit would be subject to review if circumstances changed:

> 3. The proposed measures would provide local authority employers with powers to award benefits for those scheme members who are permanently incapable of their local authority employment but are judged by an occupational health practitioner to be capable of gainful employment quite soon after leaving that employment.
>
> 4. It remains the Government's policy that any proposal remains affordable and fair within the cost envelope of 19.5% of payroll for the revised new look LGPS which comes into effect in April 2008, and that the third tier of ill health provision equates to some 0.1% of payroll.
>
> 5. The benefit improvement being proposed involves providing a pension based on the annual equivalent of the member's accrued pension benefits at the point of leaving employment. Payments would continue provided that other gainful employment was not found but would cease when it was. It will be necessary to monitor the third tier's practical application because the recipient is expected to be able to obtain alternative employment within a reasonable period. We are proposing that the recipient should notify the relevant administering authority, giving details, if they obtain employment. The administering authority would have powers to then suspend the payment of the benefit if gainful employment had been obtained.
>
> 6. The administering authority will have powers to ask the recipient, after the benefit has been in payment for a period (for example, a year) if their circumstances have changed. If it is found that gainful employment has been obtained, the administering authority will have powers to suspend the benefit. Comments are welcomed on how long the period should be before a review is undertaken.
>
> 7. When benefits are stopped, the recipient would become a pensioner member with suspended benefits.
>
> 8. When benefits are suspended, and should a 3rd tier member subsequently become an active member of the LGPS, the earlier period of membership which resulted in ill health benefits will not be aggregated with the later active membership. Two pension payments would, ultimately, be payable in these circumstances.[56]
>
> 8. In December 2007, interested parties were consulted on a three tier arrangement with those members judged to be permanently incapable of both their local government employment and any gainful employment before reaching their normal retirement age ("NRA") receiving the immediate payment of their benefits enhanced by 50% of their prospective service up to their NRA. For those members also leaving on the grounds of permanent ill-health but who were judged to be capable of obtaining gainful employment after a reasonable period, but before their NRA, the immediate payment of benefits would be enhanced by 25% of prospective service. This left those members, again leaving on the grounds of permanent ill-health, but who could

[55] CLG consultation letter, 21 November 2007, 'Third tier ill-health provision', para 9
[56] CLG consultation letter, 21 November 2007, 'Third tier ill-health provision'

undertake gainful employment within a reasonable period after cessation. Members falling within this third tier would receive the immediate payment of benefits, but with no enhancement. It was further proposed that for administrative simplicity, there would be no review arrangement or mobility between tiers.

After consideration of the views expressed by interested parties, Ministers decided to come forward in April 2007 with a two tier arrangement Members who are totally incapacitated from their local government employment and any other gainful employment will receive their accrued pension entitlements plus a service enhancement of all their prospective membership to NRA, and those with a lower level of incapacity will receive 25% of their prospective membership along with their accrued pension entitlements.

The "third tier" referred to in paragraph 8 above was not taken forward because both sides of local government agreed to explore the scope for coming forward with a form of income replacement allowance, outwith the pension scheme and to be paid by local authority employers from their revenue.

A summary of responses to the consultation was issued on 14 May 2008.[57] This shows that responses were varied. For example, Local Government Employers were concerned about the increased burden or work represented by the third tier:

The LGE expressed their continuing support for a two tier ill health system, believing that a third tier would increase the burden of work, both for administrators who would need to monitor the individuals concerned and for medical practitioners, and also increase the number of appeals. The LGE's first fallback position was to have a third tier of benefits outside the LGPS in the form of a one off termination payment. If the third tier were to remain in the Scheme, the definition of a "reasonable period of time" for determining which tier should be used should be set in the region of three years. This would give time for relevant treatments to run their course.

The trade union, UNISON welcomed:

… the original proposal for the third tier to be paid through the LGPS instead of by employers. However, they argued that it is essential that anyone retiring through permanent ill health should have the right to an immediate lifetime pension. UNISON expressed concerns that the proposals would particularly affect the low paid who would be unable to take gainful employment without losing their pension, even if the pay in the new job was much less. Such individuals would benefit from the introduction of an income replacement scheme. UNISON argued that their preference was that reviews should only occur if the member is able to get a comparable job, but that in any case reviews should provide for the possibility of transferring to the upper two tiers.[58]

Legislation to introduce the third tier was included in the *Local Government Pension Scheme (Amendment) Regulations 2008* (SI 2008 No. 1083), which amended regulation 20 of the *Local Government Pension Scheme (Benefits, Membership and Contributions) regulations 2007* (SI 2007, No. 1166). The DCLG issued informal guidance on 4 March 2008.[59]

---

57 DCLG, Third tier ill-health retirement – summary of consultation responses, 14 May 2008
58 Ibid
59 http://www.lge.gov.uk/lge/aio/125635 (retrieved 31 March 2009)

Lord Campbell-Savours laid a motion praying against the regulations in the House of Lords. In debate he referred to concerns raised by UNISON about the new ill health benefits. There were particular concerns about the third tier of ill-health benefits:

> The level 3 pension is intended for those who are judged permanently incapable of doing their job, but capable of gainful employment within a reasonable time after leaving. The regulations define a reasonable period as three years. They state that, in all cases, benefit will cease after three years without a requirement for the employer to review at this point whether the member is still unfit to obtain regular gainful employment. I am concerned that there has been flawed consultation on this three-year definition. There seems to have been no consultation on the provision to stop the pension after three years…

He asked a number of specific questions, including what would happen to a member after three years and what definition of paid employment would be used. He asked whether the change was necessary:

> …the numbers of ill health retirements in the local government pension scheme have dramatically declined over the past years, and indications are that the trend will continue. I am not altogether sure that it is necessary to treat those capable of some kind of employment in such a penal way. In addition, there are no data to indicate how many future ill health retirements will fall into which of the three levels. Government costings appear to be based purely on estimates.[60]

In response, the then Parliamentary Under Secretary of State, Lord Bassam said the issue was "central to the reforms recently concluded for the LGPS."[61] He explained the first two tiers of ill-health benefits as follows:

> The top tier provides 100 per cent enhancement to members' accrued retirement benefits where the employee leaves employment because they are permanently incapable of their local authority employment and are independently medically assessed as not likely to work in any other employment before 65, their normal retirement age.
>
> A second tier provides a 25 per cent enhancement for those assessed as permanently incapable of their current jobs but who are likely to become capable of gainful employment at some stage before 65.[62]

The third tier would apply:

> …to a local government employee who leaves his current job because he is permanently incapable of doing that job but who is judged medically capable of obtaining other employment within three years. It provides a mandatory pension until the pensioner member obtains gainful employment and it is not intended that the payments should continue for ever. Third tier payments, therefore, will be reviewed after 18 months to assess the member's employment status. Payments cease where gainful employment has been found. But if it is shown that work has not been obtained following the review, the employer must seek a further medical opinion.

---

[60] HL Deb, 22 May 2008, c1651-2
[61] Ibid, c1656
[62] Ibid, c1657

> The regulations provide for two outcomes when a second medical opinion is received. First, there is the opportunity to uplift the member to the enhanced second tier. Alternatively, payments will stop if the member remains medically assessed as being capable of employment within the three years of leaving their job. When payments cease, the member becomes a pensioner member with deferred benefits. The member's final scheme retirement pension will not be reduced because of third tier payments.[63]

He explained UNISON had been involved in consultation on the regulations and that a high-level ill health monitoring group had been set up, including key stakeholders from the employer and trade union sides.[64] As regards the specific questions that had been raised regarding the third tier:

- The only circumstances under which a member who left their local government employment on the grounds of permanent ill health would not become entitled to the award of an ill health pension scheme would be where they were judged by an independent registered medical practitioner to be immediately capable of undertaking gainful employment.

- He did not consider that the new test would be misconstrued:

  > "If the medical condition rendering the member permanently incapable of their current employment also means that they cannot obtain gainful employment within three years, not within three years, or at any time before normal retirement age, ill health benefits are payable. This test does not require consideration of the range of alternative employment, and is not open to misinterpretation."

- Third tier payments could not simply be stopped:

  > "It is a requirement in the regulations that the employer reviews the employment status of a third-tier member if payments are still being made after 18 months. Payments cannot be stopped unless the member has notified that they have found work or that, following the review, medical opinion supports the earlier opinion that the member is capable of gainful employment within three years of leaving their employment. The review payments can cease after three years, where the medical assessment confirms that."

- It was the intention that a third-tier member would be capable of gainful employment before the end of the three year period. If not, the employer could make a further determination to award a second-tier pension at any time.

- In the context of the definition of gainful employment in regulation 20 (14), it was "clear that paid employment means any remunerative employment."[65]

DCLG issued statutory ill-health guidance in November 2008.[66] The provisions are also explained in a leaflet for scheme members produced by Local Government Employers, *Your LGPS benefits*, January 2010.

---

[63] Ibid, c1659
[64] Ibid, c1660
[65] Ibid, c1661-3
[66] See also, covering letter from DCLG dated 24 November 2008

5 Further information

Information on the LGPS can be found on the Local Government Pensions section of the DCLG website. More detailed information can be found on the DCLG workforce pay and pensions division website (though no new content has been added this site since February 2009). DCLG produced Local Government Pension Scheme: Commentary Guidance on the new scheme in April 2008.

The Local Government Employers website (which represents employers' interests on local government pensions policy) has a section on LGPS. It includes copies of LGPS guides and leaflets.

The Government Actuary's Department (GAD) has also produced a summary of key features of the scheme pre and post 1 April 2008.[67] GAD also issued three sets of guidance on 28 April 2008, covering 'Late Retirement',[68] 'Individual Income and Outgoing Transfers'[69] and 'Interfund transfers'.[70]

[67] Government Actuary's Department, *Local Government Pension Scheme in England and Wales – Key features pre/post 1 April 2008 (Summary as at 29/04/2008)*
[68] GAD, 'Local Government Pension Scheme (England and Wales) – Late Retirement' (28 April 2008)
[69] GAD, 'Local Government Pension Scheme (England and Wales) Individual Incoming and Outgoing Transfers' (28 April 2008)
[70] GAD, 'Local Government Pension Scheme (England and Wales) Interfund Transfers' (2 May 2008)