

## HAMPSHIRE COUNTY COUNCIL

### Decision Report

<b>Decision Maker:</b>	Pension Fund Panel
<b>Date:</b>	16 December 2011
<b>Decision Maker:</b>	Cabinet
<b>Date:</b>	19 December 2011
<b>Title:</b>	Government consultation on increases to employee contribution rates and changes to scheme accrual rates
<b>Reference:</b>	3530
<b>Report From:</b>	County Treasurer

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#### 1. Executive Summary

- 1.1. The purpose of this paper is to provide further information on the County Council's proposed response to the Government's consultation on how short term savings of £900m nationally could be made in the cost to employers of the Local Government Pension Scheme (LGPS).
- 1.2. The Government's deadline for responses to the consultation is 6 January 2012.
- 1.3. Cabinet will consider the issue on 19 December 2011 to finalise the County Council's response.
- 1.4. The Panel agreed at its meeting on 4 November 2011 that employees should be offered a choice of how the required savings should be made, either from a worsening of the accrual rate from 1/60<sup>th</sup> to 1/70<sup>th</sup> or from an increase in employee contribution rates. Although the Panel did highlight that the aspect of choice could be achieved through the additional voluntary contribution (AVC) route.
- 1.5. The Employment in Hampshire County Council Committee considered the consultation proposals on 9 November 2011. The Committee concluded that no choice should be offered to employees, for ease of understanding and administrative simplicity, and that all the savings should be achieved by worsening the accrual rate from 1/60<sup>th</sup> to 1/70<sup>th</sup>, with no increases in the contributions paid by employees. This conclusion recognised the point made by the Pension Fund Panel regarding AVCs and determined that this was the appropriate route for employees to exercise choice.

- 1.6. The report explains the background and asks the Panel to confirm its final response to the Government.

## 2. Background

- 2.1. The Government consulted on 7 October 2011 on proposals to save £900m per annum by 2014/15 in the cost of the LGPS nationally, with the savings phased in from 2012/13. The Government's proposals included two options for splitting the savings between increases in employee contribution rates and a worsening of the rate at which benefits accrue. The two options are summarised in Table 1. The full consultation paper is available as part of the report to the Panel on 4 November 2011 at:  
[http://www3.hants.gov.uk/councilmeetings/advsearchmeetings/meetingsitemssummary.htm?pref=Y&tab=1&item\\_ID=3410&cancel=n](http://www3.hants.gov.uk/councilmeetings/advsearchmeetings/meetingsitemssummary.htm?pref=Y&tab=1&item_ID=3410&cancel=n)

**Table 1 – The Government's proposals for savings**

	<b>Option 1</b>	<b>Option 2</b>
<b>Employee contributions</b>	<p>To save <b>£450m</b> per annum                      Phased in over 2012/13, 2013/14 and 2014/15                      Eleven salary bands, eg:                      Up to £15,100:                          no change                      £22,001 to £32,400:                          Now: 6.5%                          2012/13 7.2%                          2013/14 8.0%                          2014/15 8.3%</p> <p>Contributions for the highest salary band would increase from 7.5% to 12.5%</p> <p>See Table 2 below for full details of the bands</p>	<p>To save <b>£300m</b> per annum                      Phased in over 2012/13, 2013/14 and 2014/15                      Eleven salary bands, eg:                      Up to £15,100:                          no change                      £22,001 to £32,400:                          Now: 6.5%                          2012/13 6.8%                          2013/14 7.2%                          2014/15 7.5%</p> <p>Contributions for the highest salary band would increase from 7.5% to 12.5%</p> <p>See Table 2 below for the full details of the bands</p>
<b>Accrual rates</b>	<p>To save <b>£450m</b> per annum                      Now 1/60<sup>th</sup>                      2012/13 no change                      2013/14 1/64<sup>th</sup>                      2014/15 1/65<sup>th</sup></p>	<p>To save <b>£600m</b> per annum                      Now 1/60<sup>th</sup>                      2012/13 no change                      2013/14 no change                      2014/15 1/67<sup>th</sup></p>

**Table 1 – The Government’s proposals for savings**

Savings	Option 1			Option 2		
	2012/13	2013/14	2014/15	2012/13	2013/14	2014/15
	£m	£m	£m	£m	£m	£m
<b>Contributions</b>	180	360	450	95	220	300
<b>Accrual rates</b>	-	360	450	-	-	600
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<b>Total</b>	180	720	900	95	220	900
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<b>Total savings</b>	1,800			1,215		

2.2. The following table shows the significant impact of the Government’s proposals on the mid to higher salary bands, even after meeting part of the required savings by worsening accrual rates.

**Table 2 – the Government’s proposals for employee contribution bands**

Tariff band	Current	Option 1			Option 2		
	2012/13	2013/14	2014/15	2012/13	2013/14	2014/15	
	%	%	%	%	%	%	
£0 – 12,900	5.5%	5.5%	5.5%	5.5%	5.5%	5.5%	
£12,901 – 15,100	5.8%	5.8%	5.8%	5.8%	5.8%	5.8%	
£15,101 – 19,400	5.9%	5.9%	6.0%	6.0%	5.9%	6.0%	
£19,401 – 21,000	6.5%	6.7%	7.2%	7.7%	6.5%	6.8%	
£21,001 – 32,400	6.5%	7.2%	8.0%	8.3%	6.8%	7.2%	
£32,401 – 43,300	6.8%	7.5%	8.3%	8.7%	7.1%	7.8%	
£43,301 – 60,000	7.2%	8.2%	8.7%	9.0%	7.8%	8.4%	
£60,001 – 81,100	7.2%	8.7%	9.2%	10.0%	8.7%	8.8%	
£81,101 – 100,000	7.5%	9.0%	9.8%	11.0%	9.0%	9.8%	
£100,001 – 150,000	7.5%	9.5%	11.0%	12.0%	9.3%	10.8%	
£150,001+	7.5%	10.0%	12.0%	12.5%	9.5%	11.8%	

2.3. The Government has accepted in these proposals that the funded status of the LGPS allows it more flexibility than the unfunded public sector pension schemes in determining how the savings can be achieved. The savings do not have to be met wholly from increased employee contributions and parts of the benefits package can be considered, such as accrual rates.

2.4. Following the discussion of the proposals on 4 November 2011, the Panel concluded from the point of view of the administering authority of the Hampshire Pension Fund that employees should be offered the choice of:

- (1) worsening the accrual rate from 1/60<sup>th</sup> to 1/70<sup>th</sup> with no increase in employee contribution rates, or

(2) retaining the current accrual rate of 1/60<sup>th</sup> but with higher employee contribution rates.

- 2.5. The Employment in Hampshire County Council Committee on 9 November 2011 preferred the first option of simply worsening the accrual rate from 1/60<sup>th</sup> to 1/70<sup>th</sup> without giving employees the choice of higher contribution rates instead. This recognised the point made by the Pension Fund Panel regarding AVCs and determined that this was the appropriate route for employees to exercise choice. The Committee felt that this would have the following benefits:
- employees' pay would be unaffected
  - the level of opt-outs by employees from the LGPS should be reduced, protecting the future financial viability of the scheme
  - the risk of further industrial action might be reduced
  - the proposal is easier to understand and simpler to administer than options that involve choice.
- 2.6. The Government had asked respondents to provide costed information for alternative proposals for the savings by 25 November 2011, in advance of the final deadline for responses of 6 January 2012. The County Treasurer provided information to the Government based on the recommendation of the Employment in Hampshire County Council for a worsening of the accrual rate from 1/60<sup>th</sup> to 1/70<sup>th</sup>. If this was introduced in 2013/14, the savings of £900m per annum could be phased to match the impact of either of the Government's two options in Table 1. The County Treasurer's response to the Government is attached as Appendix 1.

### **3. Comments from other employers**

- 3.1. The Government's consultation paper has been forwarded by the County Treasurer to the Pension Fund's other employers to enable them to respond to the Government if they wish. The employers were advised that the County Council was considering a proposal to ask the Government to achieve all savings from a worsening of the accrual rate. They were asked to send any comments on that proposal, and the consultation paper generally, to the County Treasurer by 30 November 2011.
- 3.2. Comments have been received from two district councils. One supports worsening the accrual rate in preference to an increase in employee contribution rates. The other district council took the view that staff would prefer to have the choice.
- 3.3. Responses have been received from 22 other employers, including parish and town councils, colleges and academy and other schools. Although, it is clear from these responses that many of them are the personal views of the individual responding on behalf of the employer and therefore not necessarily a representative response from the employer perspective. Of the 21 employers that expressed a preference, all supported the option of an increase in employee contribution rates instead of worsening accrual rates

Although in many instances reference was made to needing to know more regarding the proposed increase levels which would lead one to question whether all respondents had read the Government's full consultation document.

#### 4. Government's proposals for longer term changes to the Pension Scheme

- 4.1. These proposals for short term savings in 2012/13, 2013/14 and 2014/15 in the cost of the LGPS are separate from the Government's plans for the future of public sector pension schemes from 2015 onwards.
- 4.2. The Government issued a statement on 2 November 2011 on those proposals as part of its ongoing negotiations with the unions. The details are summarised in Table 3 below. The Government will need to begin a formal consultation process once it has finalised its plans.

**Table 3 – The Government's proposals for the LGPS from 2015**

<b>Scheme element</b>	<b>Government position</b>
Type of scheme	CARE (ie, Career Average Revalued Earnings)
Accrual rate	1/60 <sup>th</sup> , after the Government's concession from 1/65 <sup>th</sup> on 2 November 2011
Employee contribution rate	Current rate plus an average 3.2%
Accrued rights	Fully protected including the link to final salaries for past service
Staff within 10 years of the Normal Retirement Age on 1 April 2012	Full protection from the proposed changes, including their future service
Revaluation for active members	Earnings
Revaluation for deferred members	Prices (CPI)
Indexation of pensions in payment	Prices (CPI)
Normal pension age	Linked to the State Pension Age
Lump sums	Optional commutation at 12:1, up to the maximum permitted by HMRC

**Table 3 – The Government’s proposals for the LGPS from 2015**

<b>Scheme element</b>	<b>Government position</b>
Ancillary benefits	Same as in the current scheme
Rejoiners	Rejoiners within 5 years may link their service
Early and late retirement	Permitted on a cost neutral basis
Start date	1 April 2015

- 4.3. The Government has allowed some scope for flexibility in implementing the details of these proposals. The Government Actuaries Department has developed a ‘Reference Scheme’ and this will be used to make sure that any further variations to the proposals are cost neutral.

## **5. Conclusion**

- 5.1. Cabinet will finalise the County Council’s response to the Government’s consultation on the short term savings on 19 December 2011.
- 5.2. The Panel may wish to consider whether it wishes to retain its proposal for offering employees a choice between meeting the required savings from worsening the accrual rate or by increasing employee contribution rates. Although, the Pension Fund Panel recognised that AVCs could be considered the appropriate route for employees to exercise choice.
- 5.3. As a major part of the Employment in Hampshire County Council Committee’s concern about offering choice related to administration costs and much of those costs would fall on the administering authority, the Panel may wish to accept the Committee’s view and agree that choice is achieved through the AVC route.

## **6. Recommendation**

- 6.1. That the Panel agree to recommend to Cabinet a response to the Government’s consultation on short term savings which either:
- (1) offers employees a choice of worsening accrual rates from 1/60<sup>th</sup> to 1/70<sup>th</sup> or an increase in employee contribution rates, or
  - (2) confirms that employees can exercise choice through the purchase of AVCs and therefore propose that all the savings should be met from worsening the accrual rate from 1/60<sup>th</sup> to 1/70.

**CORPORATE OR LEGAL INFORMATION:****Links to the Corporate Strategy**

<b>Hampshire safer and more secure for all:</b>	yes/no
Corporate Business plan link number (if appropriate):	
<b>Maximising well-being:</b>	yes/no
Corporate Business plan link number (if appropriate):	
<b>Enhancing our quality of place:</b>	yes/no
Corporate Business plan link number (if appropriate):	
<b>OR</b>	
<b>This proposal does not link to the Corporate Strategy but, nevertheless, requires a decision because a response needs to be made to the Government's consultation on short term savings.</b>	

**Other Significant Links**

<b>Links to previous Member decisions:</b>		
<u>Title</u>	<u>Reference</u>	<u>Date</u>
<b>Direct links to specific legislation or Government Directives</b>		
<u>Title</u>	<u>Date</u>	

**Section 100 D - Local Government Act 1972 - background documents**

The following documents discuss facts or matters on which this report, or an important part of it, is based and have been relied upon to a material extent in the preparation of this report. (NB: the list excludes published works and any documents which disclose exempt or confidential information as defined in the Act.)

DocumentLocation

None

## **IMPACT ASSESSMENTS:**

### **1. Equalities Impact Assessment:**

- 1.1. Equality objectives are not considered to be adversely affected by the proposals in this report.

### **2. Impact on Crime and Disorder:**

- 2.1. The proposals in this report are not considered to have any direct impact on the prevention of crime.

### **3. Climate Change:**

- a) How does what is being proposed impact on our carbon footprint / energy consumption?

No specific impact.

- b) How does what is being proposed consider the need to adapt to climate change, and be resilient to its longer term impacts?

No specific impact.

**County Treasurer's response to the Government's interim request for specific costed options for achieving the short-term savings of £900m nationally in the cost of the Local Government Pension Fund**

**Email to Richard McDonagh, LGPS Pension Team, Department for Communities and Local Government, 25 November 2011**

**Response based on the recommendation by the Employment in Hampshire County Council Committee that the savings should be met by a worsening in the accrual rate**

Dear Richard

In accordance with the timetable set out in Terry Crossley's letter of 7 October 2011, I can confirm that Hampshire County Council will propose in its final response to the Consultation that all the Government's target for short term savings of £900m from the Local Government Pension Scheme (LGPS) should be met by worsening the accrual rate from 1/60th to 1/70th, with no increases in employee contribution rates.

The funded nature of the LGPS provides this opportunity to vary accrual rates which is not available for the unfunded public sector pension schemes. The Government has already recognised that the funded nature of the LGPS is different to the other public service schemes and has agreed that the savings can be achieved by a mixture of reductions in benefits and lower increases in the member contributions, provided the combined savings total £900m p.a. by 2014/15. The worsening of the accrual rate alone from 1/60th to 1/70th will achieve the required £900m p.a. savings by 2014/15 leaving no requirement to increase member contributions.

It is appreciated that this proposal will therefore result in differentials between the public sector pension schemes and indeed employee conditions of service, but we would strongly contend that significant differences already exist in any case. Indeed only recently the Government agreed to paying all teachers earning £21,000 or less a pay award of £250 for 2011/12, Local Government have not made such a pay award to their employees in 2011/12. Therefore this proposal simply continues a current position of significant differentials between public sector pension schemes and public sector employment conditions.

In terms of the specific costings requested, Annex A to the Government's consultation paper shows that a change in accrual rate from the existing level of 1/60th to 1/65th would result in annual savings of £450m (paragraph 9). By extrapolation, a change from 1/60th to 1/70th should provide annual savings of £900m.

This change to an accrual rate of 1/70th could be introduced in 2013/14. Fund actuaries could be enabled by the technical adjustment to the Regulations referred to in paragraph 4.11 of the Consultation paper to take into account the

savings in 2013/14 and 2014/15 in setting employers' contribution rates from 2012/13 onwards to phase in the impact of the savings.

This phasing could provide savings of £180m in 2012/13, £720m in 2013/14 and £900m in 2014/15, as set out in paragraph 9 of Annex A to the Consultation paper.

This proposal will be submitted by Hampshire County Council from two perspectives, as an employer perspective as well as from the Hampshire Pension Fund administrator perspective. The final submission will expand fully upon the rationale behind this submission but in summary, it is strongly contended that this will achieve the Government's aim in a manner which is likely to be acceptable to employees whilst avoiding a significant negative impact upon the financial viability of the Pension Fund.

This proposal is easy for employees to understand and in particular makes only one change, it will be straightforward to administer, it avoids a negative impact upon employees' net pay in the current economic climate and will therefore avoid significant numbers of employees opting out of the pension fund. Should the current Government proposal continue there is a high likelihood of significant employee opt-out rates which will negatively impact upon the Pension Fund, requiring employer contributions to be increased in order to close the pension deficit, therefore resulting in the opposite effect the Government is aiming to achieve.