Avon Pension Fund
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Date: ?? December 2011

Dear Sir / Madam

Avon Pension Fund submission on the consultation on the proposed increases to employee contribution rates and changes to scheme accrual rates, effective from 1 April 2012

The Avon Pension Fund [APF] is part of the Local Government Pension Scheme [LGPS] and is committed to participating in all discussions and consultations regarding its future. This response considers the proposals impact on the future sustainability of the fund and in particular membership implications. The administrative impacts are similarly considered. All employers within the APF have been informed of the consultation and have been encouraged to put forward their own comments.

The Avon Pension Fund recognises the underlying aims of providing a scheme that is affordable, sustainable and fair to both members and taxpayer and supports the need for change in order to achieve this across the public sector.

The key issues for the Fund arising from these proposals are;

- Increases in contributions and wider scheme proposals are inextricably linked and every effort should be made to ensure that a single coherent package of measures is proposed and the LGPS only changes once.

- Minimising opt out rates is crucial to the sustainability of the fund and given both the balance of membership of the LGPS (low paid, part time) and current economic conditions, contribution rate increases should be minimized. (Approach 2 would be more preferable than Approach 1)

- Scheme changes should be simple and easily understood to reduce the administrative burden of complex system changes and unnecessary communications.

- The proposals for contribution rate increases fail to recognise that the LGPS has already done this in 2008 as well as a myriad of other changes. The universal application of the 3.2% contribution savings fails to recognise the strides already taken by the LGPS in addressing its financial sustainability.

- Savings arising from the proposed increase in employee contributions cannot be passed back to employers without regulation and if so would only be temporary. This underlines the point that the LGPS is structurally different to all other public sector pension schemes.

Before answering the specific questions posed in the consultation, I would like to expand on the above points.

Communications
It was unfortunate that consultation in respect of the 2012 changes was issued within weeks of the Treasury's document on 2015 changes – "Public Service Pensions: good pensions that last". Whilst the two may be regarded as separate they are invariably linked and employers and members want to understand the implications of both.

The numerous press releases from both Government and Unions contain confused and misleading information which administrators are finding difficult to understand and communicate, leaving little hope for the fund member.

For example; The Treasury document on the 2015 changes contained numerous implications for the changes proposed from 2012 (e.g. protection from April 2012 if with 10 years of retirement age / 60th accrual rate as opposed to reduced accrual rates for earlier years). Of course there is still the proviso that the 2015 proposals may be withdrawn!
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It is therefore difficult to respond to a consultation that is clearly fluid and which underlines how difficult it is to separate the two sets of proposals. **The fundamental conclusion is that DCLG and Treasury need to agree a single package of reforms with one implementation date, supported by a structured communication strategy.**

The LGPS differential
Although the Treasury have acknowledged that the LGPS is different from the other public sector schemes because of its funded nature it still fails to recognise the structural differences that exist between it and other schemes.

Many of the Hutton recommendations have already been addressed within previous LGPS changes. The DCLG has already addressed the issue of retirements at age 60 with unreduced benefits, when the rule of 85 was abolished in 2006 and, unlike other public sector schemes who retained age 60 retirements for existing members, LGPS only gave full and limited protections to members nearing retirement. Indeed any benefits accruing on service from April 2020 are only payable unreduced from age 65. Compare this to the Teacher's Scheme where a 25 year old in the scheme at 31 December 2006 has retained the right to receive their pension unreduced at age 60 on all service.

This is further highlighted by the fact that the Government Actuary does not regard the LGPS as a broadly comparable scheme for TUPE transfer with other public sector schemes. The LGPS has recently been amended to cater for Learning Skills Council Staff transferring into Councils in order to protect their superior benefits. However in any information given out by the Government, all public sector schemes are deemed as one.

On the basis that the public sector pension schemes have to generate a 3.2% contribution saving or cost reduction, It is a great pity that the efforts already taken by DCLG to ensure that the LGPS is more sustainable have not been recognised and accepted. **The cumulative impact of the 2012 and 2015 proposals will undoubtedly give rise to deterioration in membership levels due purely to affordability**.

Contrast this with the proposed cost ceiling for the schemes beyond 2015 where the civil service scheme has the highest cost ceiling percentage level but the lowest average employee contribution rate. It would seem that differences between schemes are sometimes relevant!

There is also a lack of evidence that the proposals for 2012 will actually generate savings of £900m and with the protection for lower paid members it does throw this into doubt. Moreover it is unclear what effect this will have on the Hutton recommendations if the required savings are not achieved. **This again points to the need for a single package of reforms and to further ensure that there will be no need for further revisits in the near future.**

Employer Savings

There is an expectation that employers will benefit by a reduction in contributions as a result of these proposals **but** at the 2010 valuation the APF extended recovery periods as far as is deemed prudent in order stabilise employers contributions. The current economic circumstances do not auger well for asset returns and a valuation in 2013 will leave it no choice but to increase employer rates in 2014. The Fund's actuary has already advised that any windfall savings should be used to reduce this recovery period and definitely **not reduce employer's contributions**.

This points to two clear issues; that the 2012 proposals will not generate any savings for the employer unless Government legislates for this and that even if it does the savings will be short lived as contribution rates will increase in 2014; Further savings from any new scheme proposal will need to be agreed early in order to affect the 2013 valuation. Given the economic conditions it would seem sensible to merge proposals into a coherent scheme and contemplate postponement of the 2013 valuation. Given market performance over the past decade I would go further and extend the valuation period to 5 years – 3 years being too short to reflect on the volatility of financial markets and assess underlying asset growth.

Protecting the Low paid (minimising opt out)

A disproportionate number of APF (LGPS) members are part time and low paid and the contribution basis (gross pay) for calculating contribution rates unduly puts financial pressure of the low paid and is a real deterrent to membership. With the changes taking place within Councils workforces, the number of part time members will continue to grow. The present proposals for increasing contribution rates (which are confusing) also put a disproportionate cost on a smaller percentage of the higher paid workforce – which is not the case in other public sector schemes. Hence the argument to keep member contribution rises to a minimum

Each employer within the LGPS will have a different make up of pay profiles and an employer with a high level of members with pay under £19,400 will not achieve the expected savings or if they do, it will be because the other scheme members are compensating. One of our employing bodies has 60% of its scheme members with pay under £19,400, therefore the other 40% would be expected to make up the savings.

The table below for this employer shows that both options fail to produce the required % contribution increase by 2015

	2012/13	2013/14	2014/15
	% of payroll	**% of payroll**	**% of payroll**
CURRENT	**6.45**	**6.45**	**6.45**
Approach 1	**6.94**	**7.47**	**7.75**
Difference from current	**0.50**	**1.02**	**1.30**
Approach 2	**6.71**	**7.08**	**7.31**
Difference from current	**0.26**	**0.64**	**0.86**

There is therefore a fine balance here between avoiding opt outs within low paid members on pure affordability grounds and preventing opt outs from mid to high earners who feel that their value for money is being compromised by the increases required on their contribution rates which are higher because of the guaranteed protections for low paid.

There is a very serious risk that increases in employee contributions, economic conditions and potential adverse decisions from the Fair Deal consultation could cause a spiralling effect on funds where membership decreases significantly bringing funds closer to maturity. This then impacts on employers costs which would be passed on to the members if it exceeds the scheme's cost ceiling and therefore creating a cycle of decline, thus making the scheme untenable.

Administrative complexity
The proposition of changes to administration and payroll systems not once but twice in short succession (2012, 2015), gives rise to serious concerns around the funds ability to maintain accurate records, collect the correct contributions and pay the right benefits. The administrative changes are

- Increasing in the number of pay-bands from 7 to 11
- Two options on the level of increases [including sharp increases on specific bands between the two options]
- More complexity for Employer payrolls in paying members correctly and providing administering authorities with the necessary information. This is a key area as timescales to produce these are reducing with the increase in HMRC requirements and career average calculations.
- Increasing employers recruitment problems where promotion could lead to very little or no net pay increase; thus removing incentive for employees.
- No consideration for members to decide their own requirements. Pay more to get higher accrual rate or in the case of low paid pay less to get less: as set out in the LGA proposals
- Either one or two changes in accrual rate before any changes for 2015 when they could change again or does this mean LGPS will be different from the other schemes and not have 60th accrual rate as set out in the Treasury proposals?

It is recognised that any new scheme will create additional complexity, if only to reflect the inherent protections inbuilt. However the vast growth in employers due to creation of academies and outsourcing are already causing administrative pressures and in order not to add to the burden, **Funds will need more powers** to compel employers to provide accurate and timely information. The act of enabling the construction of **administration strategies** and penalty regimes did not go far enough and needs cementing with clear penalty structures for failing employers and compulsion to make necessary system changes to meet the needs of Funds. Without this the cost of bureaucracy will increase.

The questions raised in the consultation

Question 1 – Do the proposals meet the policy and objectives to deliver the necessary level of savings in the LGPS?

It is unclear whether the proposals will deliver the necessary level of savings as the cost of protections has not been calculated. It is expected though that the savings will be in the right region. Unfortunately the savings objective has been universally applied and does not recognise the starting position of the LGPS and is not aligned to future Hutton proposals as the proposal is isolated at present from the main scheme reforms.

Question 2 – Are there any consequences or aspects of the proposals that have not been fully addressed?

The effect of increased contributions at a time when the country is at best in a period of low growth if not further recession is already impacting on membership numbers. The proposals need to be put in context of other measures already impacting on membership numbers, such as pay freezes, VAT increases, future increases of NI contributions due to the proposed abolition of contracting out, all of which make the LGPS more unaffordable.

Question 3 – Is there a tariff or alternative measures which consultees think would help to further minimise any opt outs from the scheme?

Trying to cater for all categories of employee within a single package of measures is extremely difficult. However catering for the low paid in particular needs to be given separate and detailed consideration. Options to consider would be

- a reduced pension based on lower contributions and lower accrual rate
- an increase retirement age in line with state level to remove the increase in costs
- an incentive to give low paid possible reasons to stay in or join. (e g Allow early partial lump sum release.)

Question 4 - Are there equality issues that could result in any individual groups being disproportionately affected by the proposals? If so, what are considered to be the nature and scale of that disproportionate effect? What remedies would you suggest?

There is the existing anomaly for part-timers who get assessed on their whole time pay equivalent and so if a member is earning only £15,000 but working half time they would pay considerably more contributions than a full time employee on £15,000.

The contribution rate differential between pay bands will discourage individuals from seeking promotion and equally the ability to attract high quality professionals and leaders into local government will reduce.

Consideration should be given to having contribution bands similar to income tax, by having contributions paid on each level as each band is reached. Fewer bands would then be needed and it would assist employers in recruitment in that employees being promoted would only have pension contribution increases on the amounts over the next limit rather than the whole salary being affected.

An example of how this could work

	Pay	13000	33000	97000
		Employee Contributions		
5%	Up to 15000	650	750	750
10%	15001 – 30000	0	1500	1500
12%	30001 - 75000	0	360	5400
14%	75000 +	0	0	3080
		650	2700	10730

Question 5 - Within the consultation period, consultee's views are invited on the prospects of introducing into the LGPS a link with state pension age as recommended to the Government in Lord Hutton's report.

Fully support the current move to bring this forward earlier to prevent having the proposed scheme changes in the 2012-15 period and then again from 2015 onwards. If this also leads to a lower contribution increase and therefore less opt outs then it should be given serious consideration. The Chancellors further proposals for bringing state retirement age forward in 2026 to 67 will no doubt also have a beneficial impact on costs, if adopted across the public sector schemes.

Conclusions

- We urge that serious efforts are made to ensure that only **one single set of clear scheme changes** is introduced. **We would support bringing forward the implementation date for the Hutton recommendation changes to April 2014 to achieve this.**

- Emphasis must be placed on creating a sustainable LGPS for the long term. This must be achieved sensibly and not driven by unhelpful time constraints due to economic circumstances rather than pension scheme sustainability.

- The impact of increased contributions of any magnitude to LGPS members could result in significant scheme opt-outs due to the high numbers of part time and low paid staff and this defeats the object of the exercise. This is therefore the opportunity to make sure we cater for all the membership's needs over the long term.

- DCLG should endorse the philosophy advocated by Lord Hutton that it is not "a race to the bottom" with pension schemes.

Yours faithfully

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