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Consultation on Proposed Increases to Employee Contribution Rates and Changes to Scheme Accrual Rates - effective from 1 April 2012 in England and Wales

I refer to the consultation document dated 7 October 2011 proposing measures to achieve short term savings of £900 million by 2014/15 within the Local Government Pension Scheme (LGPS). I submit the following response on behalf of the Wirral Borough Council in its capacity as the Administering Authority of the Merseyside Pension Fund (MPF).

MPF is receptive to the need for change in addressing the ongoing financial pressures emerging from increased longevity and the requirement to calibrate the cost of pension provision between public sector employees and taxpayers.

1/ ALTERNATIVE APPROACH

MPF submitted an interim response on 22 November proposing its alternative approach for consideration. This advocated benefit revision and extended retirement age in accordance with state pension age together with minimal increases to member contributions.

MPF produced a website at <http://lgps2015.org> along with a detailed easy-to-read bulletin covering the two consultation proposals and the Fund's alternative approach. Reference to the website and the consultation was included in the Annual Personal Benefit Statements for active members.

2/ SURVEY OF MEMBERSHIP

A short web-based survey of the membership indicated that the majority of respondents preferred the Fund's alternative approach over the two government proposals; this reinforces the previously expressed opinion that any contribution increases should be avoided if possible or at least kept to a minimum to prevent members being priced out of the LGPS. The survey results are summarised in the attached Appendix.

3/ STATUTORY CONSULTATION - RESPONSE TO QUESTIONS

The Fund's response to the five questions covered within the consultation are as follows:

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

It would appear that the proposals have been constructed to ensure the necessary savings are met. However, MPF strongly support our former alternative proposal of 22 November 2011, that a large part of the saving is generated by changes to the scheme design, rather than purely contribution increases.

It would be preferable to deliver the savings solely through benefit changes - in order to minimise optant-outs and the associated adverse impact on Scheme maturity. The funded nature of the LGPS and its current positive cash-flow allows for savings to be generated from future benefit streams. This could be achieved through accrual rate reductions and delaying access to unreduced benefits in-line with state pension age. In contrast, the unfunded pay-as-you-go schemes require the cash injections from increased member contributions to meet their current pension obligations.

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

The areas of communication, administration and change management have not been fully explored in the consultation – any change incurs a cost to administrators and employers.

The provision of timely and clear information will be a key factor in minimising optant-outs from the Scheme. Inevitably there will be potentially confusing commentary on the changes in the press and from external organisations - much of this comment will be negative from a member perspective. It is essential that administrators promote the continuing benefits of the Scheme at an early stage and reinforce the "value" of the LGPS in terms of long-term retirement planning.

We will continue to keep the website updated with details of the changes, communicate directly with members and work with employers to try and ensure the changes are clearly described and that members are able to make rational, informed decisions reflecting their individual circumstances.

Historic benefit complexities within the LGPS, together with the parameters set by HM Treasury, leads to the real need of avoiding further complexity for administrators.

Question 3 - Is there a tariff or alternative measure which consultees think would help to further minimise opt out from the scheme?

It is MPF's view, in order to minimise opt-outs, any increases in member contributions need to be kept to a minimum, and any changes in benefits kept as simple as possible; which may lead to the need to limit options and choice.

It has been suggested by the Local Government Association (LGA) that the LGPS could offer members options of different contribution rate and benefit packages. MPF strongly believe that this would be both costly to administer and communicate.

Additionally, although it might reduce optant-outs in the short-term, it would create future problems and potentially increase the number of employer-employee disputes. For example, a young member could elect for a pension package at the start of their career that ultimately proves to be the wrong decision in the long-term.

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?

The Government has previously stated that its intention is “making the lower paid no worse off”. This statement can only be achieved by collecting the savings solely through increased member contributions of middle-to-high earners; as is taking place in the unfunded schemes.

Protecting the lower paid by keeping their tariff unchanged, middle-income earners would bear the brunt of the contribution increases, therefore this cohort are more susceptible to financial pressure and will choose to opt-out of the LGPS.

However, by adjusting future accrual rates and normal retirement age as currently being considered as part of this consultation, in reality the lower paid are having their future benefits reduced.

A remedy could be to reduce the tariffs for the protected members in order to maintain the Government’s original statement. The tariff reduction could be calculated to offset the benefit changes and also make the Scheme more attractive.

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.

MPF supports the introduction of an alignment of normal retirement age with state pension age as a necessary element of Scheme reform to manage the ongoing cost of longevity and a fair redistribution of costs between the taxpayer and the member.

The abolition of the default retirement age from October 2011 strengthens this position as people can now work longer and are able to continue to contribute to a pension arrangement.

The option for people to choose to retire from age 60 should be retained with fair adjustments to the pension for those retiring earlier or later than the State Pension Age. The demographics of the LGPS mean that 50% of the membership receive low pay and may not be in a position to retire from employment before State Pension Age.

The consultation raises the prospect of employers benefiting from the effect of the changes through reductions in contributions in advance of the next actuarial valuation and the feasibility of regulatory amendments to permit such changes. Given that funding levels have fallen by around 10% since the 2010 valuation, it would be difficult to support a reduction in contribution rates without careful consideration of the potential impact on rates emerging from the 2013 valuation.

In short, as the cost envelope cap has already been established it is imperative that Scheme reform produces a clear transparent benefit design which maintains confidence in the value of the LGPS. This should be achieved by benefit structure revisions as opposed to increases in member contributions to minimise optant-outs and protect the ongoing viability and optimistic funding parameters within the LGPS; ensuring affordability for both employers and members.

4/ ACCELERATED REFORM

As there is evidently the need for a long lasting solution, MPF fully supports the recent “Heads of Agreement” between the LGA and the Trade Unions; specifically to roll contribution increases and the broader long term scheme design into a “one event” change in 2014.

Again, MPF has previously expressed an opinion that frequent change is likely to undermine confidence in the Scheme – creating fear and uncertainty amongst the membership.

An essential objective should be a solution that is capable of offering certainty in the long term. Ideally this may be achieved by implementing both the short term and long term reforms as suggested contemporaneously a year in advance of the previously discussed implementation date of April 2015.

A long standing objective of the Government has been to encourage good secure pension provision. This requires the pension provision to be valued by both the employee and employer and affordable to both. It is imperative that the revisions to the basic framework do not prove too costly and convoluted for individual members as this will rapidly increase the number of members who will choose to opt out of the Scheme, as it will be reasoned as “unaffordable and not worthwhile.”

The eventual metamorphosis of benefit design will be critical to the long term viability of the Scheme. A sustainable LGPS brings benefits to many parties, not least society as a whole, by encouraging pension saving and reducing demand on the taxpayer to support an ageing population through means tested benefits.

Yours sincerely



Ian Coleman

Deputy Chief Executive
& Director of Finance

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Statistical Summary of Web Survey

APPENDIX – Statistical Summary of Web Survey

Preference expressed:

Government Approach 1	16%
Government Approach 2	22%
MPF Alternative Approach	50%
No Answer	12%

Age of Respondents:

Under 30	6%
30-39	18%
40-49	35%
50-59	37%
60 and over	4%

Annual Salary:

£0 - £12,900	3%
£12,901 - £15,200	1%
£15,101 - £19,400	10%
£19,401 - £21,000	7%
£21,001 - £32,400	47%
£32,401 - £43,300	25%
£43,301 - £60,000	7%

Years Membership in LGPS:

0 - 5 years	31%
6 - 10 years	42%
11 - 20 years	27%

Please indicate how the adoption of certain approaches would affect your future membership of the LGPS (opt-out):

	Approach 1	Approach 2	MPF Alternative
I would continue my membership	61%	67%	71%
I would be likely to leave the LGPS	12%	9%	9%
I'm not sure at this moment...	27%	24%	20%