Facing the future -

Principles and propositions for an affordable and sustainable Local Government Pension Scheme in Scotland

LGPS (S) Policy Branch
Scottish Public Pensions Agency
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Executive Summary

The Government is committed to introducing new pension arrangements for local government. It is proposed that, for Scotland, any new-look LGPS(S) could be introduced from 2008. The intention is to retain a defined benefit final salary arrangement which is relevant to the local government workforce provided that it remains both affordable and sustainable.

Consultation Phase
The principles and propositions set out below are not intended to be a fixed and final version of a new scheme. They are, however, intended to illustrate the core elements of a new-look LGPS(S) which could be amalgamated with the best ones of the current Scheme to form a building block for the future. As such, consultees will wish to debate and discuss them and provide a considered reaction to this key consultation phase.

New-look Local Government Pension Scheme (Scotland)
Any new arrangement will have a normal scheme retirement age of 65. Where benefits are paid before this age, except on ill-health grounds, they would be actuarially reduced to reflect the fact they are being paid early. Benefits brought into payment after this age would be actuarially increased.

Benefits could accrue at 1.6% per annum, ie after 10 years service a member would receive a pension based on 16% of their salary, after 40 years service a member would receive a pension based upon 64% of their salary.

It is not intended with such an accrual rate that the Scheme could provide an automatic lump sum, but could instead allow members to commute part of their pension at a rate of 12:1; in other words, for every pound of pension foregone, £12 of lump sum would be awarded.

Pensionable pay could be limited to basic salary. All other payments, such as bonuses, fees, overtime and allowances, would be excluded.

Provision could be made for flexible retirement to ensure that members could chose to make arrangements for a more gradual approach to retirement, adjusting their work/life balance by reducing their hours or stepping-down to a less onerous job but, at the same time, able to draw some of their pension and accruing further pension rights.

Tiered ill-health retirement benefits could be introduced, with improved enhancement for members whose employment is terminated on

grounds of being permanently incapable of performing any gainful employment by reason of ill-health. A second tier of un-enhanced ill-health retirement benefits could be available to those who are incapable of continuing in their role, but who are capable of undertaking other employment.

It is proposed that survivor benefits could be extended to unmarried partners, as well as widow(er)s, registered civil partners and children. The maximum spouse/partner's pension could be 50% of the member's post commutation pension (i.e. after any lump sum has been taken), children's pensions would be 25% of the member's pension.

Death in service benefits could be increased to three times pensionable pay.

Defined Contribution Top-up Scheme

As an integral part of this exercise, consideration could also be given to the option of providing a defined contribution pension scheme as a voluntary top-up arrangement and alternative to AVC or added years provision. Further, consultees should examine the scope for such an arrangement to be offered as an alternative to the defined benefit scheme, with an appropriate level of employer contribution, to provide further flexibility and choice to Scheme members.

Costs and financing

The propositions above, if taken together, result in a total future scheme cost of about 21% of payroll. Employee contributions could be varied, based on pay levels and therefore reflect more equitably the proportionately higher pension costs attributable to higher paid Scheme members. The average contributions from employees across all pay bands would be 7% of payroll.

Transitional arrangements

To ensure a simplified, single framework for the future, any new look Scheme could provide for every person who is a contributing LGPS(S) member on the date the Scheme commences to be automatically transferred to the new arrangement. Where these members have a period of membership in the current LGPS(S), they would be awarded a period of membership in the new scheme which is of equal value.

Deferred and pension members, at the date the new scheme commences, would be entitled to retained benefits in the current LGPS(S).

Section A

Facing the future

Background

A1.1 This consultation document sets out a range of principles and propositions from which it is hoped that the basis of specific regulatory proposals to re-focus the LGPS in Scotland will emerge.

A1.2 The aim is to conserve the best elements of the current Scheme but also to develop a modern, flexible new-look LGPS(S) which can better serve the needs of local government and its workforce, as well as being affordable and sustainable for stakeholders.

A1.3 The LGPS in Scotland has developed considerably since its inception in the late 19th century. Its rules are now defined in a series of regulations made under section 7 of the Superannuation Act 1972. It is defined also for the purposes of section 1 of the Pensions Schemes Act 1993 and section 11 of the Income and Corporation Taxes Act 1988 as a statutory, public service pension scheme.

A1.4 The Scheme is sponsored centrally by the Scottish Public Pensions Agency, which is responsible for its stewardship and maintaining its regulatory framework. However, within that framework, it is administered, managed and funded at local authority level. The Scheme's continuing efficiency and effectiveness in providing secure, final salary pensions is the product of close and effective working by all stakeholders at national, regional and local levels.

A1.5 The aim is that the LGPS(S) is safeguarded as a statutory, funded, final salary pension scheme. However, this must be balanced against the increasing cost of pension provision. Recent changes to the current Scheme have sought to achieve on-going affordability by raising the retirement age to reflect that people, on average, are living longer in their retirement. Other recent regulatory changes have provided a more transparent prudential framework to address the Scheme's sustainability.

A1.6 The UK Government also recognises that there is a need to deal with the changing ratio of the economically active population to those in retirement in the UK. The 2003 White Paper, (CM 5835) *Simplicity, security and choice; planning and saving for retirement,* seeks to meet the economic challenges of these social and demographic changes by encouraging people to work longer, to help stabilise the affordability of

pension provision and to improve the retention and transfer of knowledge and skills in the workforce.

LGPS (Scotland) Policy Context

A1.7 In defining the policy framework, as a prelude to discussing the possible architecture of a new-look Scheme, it may be helpful to state SPPA's aims. New Scheme arrangements will continue to be set out in regulations made under powers in the Superannuation Act 1972. They should be:-

- comprehensive in their overall provision;
- flexible and responsive to the needs of stakeholders;
- equitable, from the points of view of all stakeholders, in terms of the balance between provision and cost;
- efficient and cost effective in terms of delivery;
- provide fully transferable rights; and
- provide the security of a guaranteed pension promise for all Scheme members.

A1.8 Historically, LGPS(S) benefits have been based on a traditional pattern of working careers which no longer reflect reality, the needs of members, their employers nor providers. The future of the LGPS(S) lies in moving towards a position from which its members are able to build up benefits over time despite changes in employment patterns to provide an appropriate target level of income for their retirement.

A1.9 It follows, therefore, that the principles and propositions developed in this consultative document are collectively 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 use of technology, joint working and new suppliers; and
- providing an affordable, secure and sustainable benefit structure.

Principles of Scheme Modernisation

A2.1 Changes to and within the LGPS(S) framework have become inevitable. While the LGPS(S) continues to meet the pension needs of full-time, career employees in and around local government employment, there is an increasing awareness that elements of it are becoming inflexible and unattractive to certain groups of employees. Of particular concern, is the growing number of younger employees who are not joining the Scheme. In addition, it has become proportionately more expensive for employers in the public, private and voluntary sectors who have hitherto subscribed to its utility and availability. Most recently, several stakeholder interests have, from their perspective, quite reasonably, questioned its fundamental affordability and even its sustainability.

A2.2 Recent policy approaches adopted by the UK Government towards occupational pension scheme provision, plus their intentions to simplify their taxation framework within new social and economic parameters, means that major schemes in the public sector are inevitably placed in the position of having to restructure, to adapt and to re-focus in order to demonstrate to taxpayers that they represent good value for money.

A2.3 In seeking to recognise the priorities of all stakeholders, the intention is to safeguard the LGPS(S) as a funded, final salary pension scheme, whilst ensuring its affordability for the future.

A2.4 Accordingly, the basis of a new scheme needs to balance stakeholders' interests and the cumulative pressures these create by providing reasonable levels of benefit at an affordable cost to employers, members and taxpayers; ensuring value for money and financial sustainability; and responding positively to stakeholders' priorities as they change over time.

A2.5 Building on the best elements of the current Scheme a modernised, new-look LGPS(S), therefore, has to meet the combined needs of key stakeholders, to be diverse, inclusive, flexible and attractive, as well as affordable and sustainable. It needs at a practical

level to be useful, understandable, relevant and straightforward to amend. Its regulations and administration should be of high quality, be cost-effective and be proportionate to their policy intention. Communication standards at all levels, and between interested parties, should reflect the importance of sustaining the pension promise within a broad based and cost-effective delivery framework.

Section B

An Analysis of the Central Issues

Scheme Membership Principles

Current position

B1.1 Developing as it did from Local Acts, the LGPS(S) provides a pension scheme for local government employees, joint boards and institutions linked to local government who, by passing a statutory resolution, put themselves in the same place as local authorities.

B1.2 Recent developments, linked to contracting out and partnership working, has seen the LGPS(S) assume a positive role as public service provider where access to one of the other public service pension schemes covered by the Superannuation Act 1972 is not available.

B1.3 Nevertheless, taking a broad view of local government, the functions and services it provides, a link may be established for quite a broad range, notably under the admission body provisions. The provisions governing these bodies have been developed recently to deal with policy developments such as outsourcing and are now comprehensively drawn. Their scope has been significantly broadened so that they now allow a range of non-scheme employers to give appropriate employees access to the LGPS(S). They offer one route by which local authorities undertaking TUPE transfers can meet their statutory duty under the Local Government Act 2003 to ensure that either LGPS(S) membership or a broadly comparable pension is provided by a contractor.

B1.4 The vires afforded by the 1972 Act, and the position under Social Security legislation covering non-local government employers, limits the extent to which any change could be made to the status of LGPS(S) employer beyond what is currently available. As they stand there are no plans to change the current position, and continuation of admitted body status will play a key role in any future Scheme.

B1.5 The Local Government Pensions Committee of the Employers' Organisation for Local Government has highlighted the problem of membership take-up – in particular for the low paid and new joiners under age 30. Some of this is related to the interface between occupational pension schemes and State pensions, and propositions in the sections B2 and B3 go some way to resolve this issue. These would indicate there is little more, at this time, that can be done.

Although of course it is essential that administering authorities and employers have in place the capacity to clearly communicate the virtues and benefits of a good quality pension scheme in terms of recruitment retention and motivation of staff. It also plays a vital part in meeting the government agenda of pension provision being linked to employment provision.

B1.6 However, one area requires specific examination – the provision in the existing Scheme under which casual staff are not automatically deemed to have elected to join.

B1.7 Under the current opting arrangements, casual employees have to opt in if they wish to join the Scheme. However, the term “casual” is not defined in the Scheme regulations. Persons with whom no mutuality of obligations is established are not likely to be “employees” within the meaning of current employment law, and so are not entitled to be in the pension scheme (although developments in case law may affect this). At least some “staff” recruited on a casual basis might seem to fall into this category. Casual employees, for the purpose of the Scheme, might best be considered to be those on short-term contracts with whom a mutuality of obligations is established but for whom no long-lasting, permanent or regular employment relationship is envisaged.

B1.8 There would seem to be no obvious reason for differentiating between casual employees who fall within these terms and other employees on short-term contracts but who have not been designated as casual employees.

B1.9 It is therefore proposed that employees employed on fixed-term contracts of less than two years will not be deemed to have opted into the scheme but must make a written election if they wish to join.

B1.10 Employees of admission bodies also have to opt in. As employees of a non-scheme employer, they may consider other pension arrangements, including the employer's own scheme if provided, to be more appropriate to their circumstances.

Contributions - Employers and Employees

Background

B2.1 Currently, the scheme's regulations require members to contribute 6% of their gross pensionable pay, with a declining number of defined “manual workers” having a protected right to contribute 5%.

B2.2 Increasingly, where the rising cost of pension provision is a key factor in employers' attitude to the affordability and sustainability of the LGPS(S), the statutorily prescribed position of employees' contribution rate contrasts markedly with the perceived rate of increases in employers' contributions.

B2.3 Central to the consideration of a new scheme is the determination of what is the most equitable level of employee contribution to a final salary public service pension scheme, especially given the part played by tax payers who effectively underpin the statutory promise.

B2.4 In previous consultations, the position of a range of stakeholder groups has been to argue for an immediate increase in employee contribution rates for the current members of the current scheme. Representations both for and against an immediate increase from 1 April 2004 were carefully considered in the context of the current scheme but it was decided not to amend the Scheme in this respect. It was decided, however, to develop specific policy proposals as part of a comprehensive assessment of the scope of any propositions to adjust the employees' contribution rate.

Propositions for the future

B2.5 Determining the equitable balance between the provision of reasonable benefits and affordability inevitably involves a trade-off within the overall scheme benefit package. This section discusses the prospects for employees paying a larger proportion of the increasing cost of providing LGPS(S) pensions.

B2.6 Any historic perspective on the relationship of LGPS(S) pension provision reveals that the employers' contribution, as a proportion of the total future service cost, has increased significantly in the last decade. Employees are therefore meeting a significantly lower proportion of the cost of Scheme.

B2.7 In 1926 the structure of the Scheme implied members met 40% of the cost of provision and employers 60%, the position today is that employees meet 30% of the cost, with the prospect of this falling to 27% by 2050. It was estimated that in order to restore the balance to the 60/40 relationship of 1926, employees would need to pay some 7%to 8% of pay today, and 9% by 2050.

B2.8 The most recent data extracted from local government responses to the LFR24 exercise, as at 31 March 2003, provides some helpful

perspectives on these matters. This shows employer contributions of some £398 million and employee contributions of around £174 million.

B2.9 This then provides a ratio of employer contributions to employee contributions of 70:30. However, this ratio takes no account of the fact that part of the employers' contributions in this period relate to past service liabilities which are not covered by current assets.

B2.10 The ratio of employer contributions to employee contributions in relation to future service costs only is a more appropriate measure, as the previous ratio will vary wildly with cyclical variations in the value of pension fund assets. The last actuarial valuation in 2002 showed that the median future service rate was 11.15% of payroll. This means that the median ratio between employer and employee contributions in 2002 was in fact 65:35. A scheme average employee contribution rate of 7%, for example, at this median future service cost provides a ratio of 60:40.

B2.11 In addition, there are matters of equity and fairness within the scheme to be considered now that its membership is so diverse, with many engaged in considerable levels of part-time employment and variable contracts.

B2.12 Table 1 below shows the net contributions under the current scheme, where all employees contribute 6% of salary, for employees at certain salary levels. The table highlights several disparities and a lack of equity. For example, it suggests that higher salaried members pay proportionately less than those with lower earnings. As the LGPS(S) is a contracted out occupational pension scheme, members who earn above the lower earnings threshold also pay lower national insurance contributions.

Current Scheme Contributions by Salary Table 1

Salary	Total Employee Contribution	Tax Relief	Actual (Net) Employee Contribution	Actual (Net) Employee Contribution (%)	Gross Employee Contribution Rate (%)
3000	180	0	180	6	6
6000	360	36	324	5.4	6
12000	720	158	562	4.7	6
24000	1440	317	1123	4.7	6
30000	1800	396	1404	4.7	6
36000	2160	864	1296	3.6	6
72000	4320	1728	2592	3.6	6

Principles for a new arrangement

B2.13 The underlying proposition on which to take forward this debate within a new-look LGPS(S) rests on employees contributing at variable rates, linked to their basic salary. The average employee contribution rate across the scheme would be 7%, but variable bands would apply to reflect the member's ability to pay, the benefits accruing and the tax relief that members receive in relation to their income tax banding.

B2.14 Such an approach deals with two issues. It recognises the need for a degree of equity across the Scheme, where the median for a whole time or whole time equivalent is about £23k, whilst the mean salary is around £14k. It also deals directly with some of the issues relating to low pay and the interface with the provision of state benefits, particularly in providing access to the benefit of the "insurance" elements of the Scheme, death in service, ill-health and redundancy provisions, at an equitable cost to the member. It is not the role of a pension scheme to address differences in level of earnings throughout a working life. But the Scheme should provide opportunity and fairness to all members as many stakeholders have argued for in their recent representations on recent draft amendment regulations.

Details of a possible new approach

B2.15 The following provides an illustration of how employee contributions could be varied in bands, with the relevant contribution rate levied on the members' total pensionable pay.

< £5k	Contribution rate of	2.5%
> £5 but < £7k	Contribution rate of	5.5%
> £7k but < £38k	Contribution rate of	7%
> £38k but < £80k	Contribution rate of	9%
> £80k	Contribution rate of	10%

B2.16 Under the variable employee contribution provisions, therefore, Table 2 below shows indicative employee contributions to a new-look Scheme.

Illustrative Banded Employee Contributions Table 2

Salary	Total Employee Contribution	Tax Relief	Actual (Net) Employee Contribution	Actual Employee Contribution (%)	Gross Employee Contribution Rate (%)
3000	60	0	60	2.5	2.5
6000	330	33	297	4.95	5.5
12000	840	185	655	5.46	7
24000	1680	370	1310	5.46	7
30000	2100	462	1638	5.46	7
36000	3240	1296	1944	5.4	9
72000	6480	2594	3886	5.39	9
144000	14400	5760	8640	6	10

B2.17 Table 2 provides a typical cost split of circa 2:1; on average, employers would be responsible for 14% and employees would contribute 7%, gross of tax relief. Employers' costs will be mitigated by investment income, but they also bear the entire risk of provision.

B2.18 Alternatively, consideration could be given to having a tiered arrangement of contributions so that members would pay a proportion of the earnings up to each limit and then higher contributions on earnings above each limit. However, if this option were preferred, to achieve an average rate of 7% the contributions would obviously need to be higher than those illustrated above.

B2.19 Overall, the additional income produced for the Scheme by implementing variable levels of employee contributions at current pay levels would help to redress the balance between employer and employee cost. In return, employers would be providing a secure, modernised and attractive final salary related pension scheme at a greater level of affordability given the new levels of income produced by the flexible contribution banding. Clearly, existing membership and take-up rates would not only need to be maintained, but enhanced in those groups of eligible employees who presently opt-out of membership.

Scheme benefits in a new-look LGPS

B3.1 This section describes the overall shape of a possible benefit package for a new-look LGPS(S). It is not a detailed proposed future scheme in any sense, but an illustrative framework for discussion and debate. It includes conserved elements of the current scheme, as well

as several new elements on which this consultative exercise is seeking views and opinions from all stakeholders.

B3.2 In drawing up the outline of a possible new package, the opportunity has been taken, within the current national pension policy framework and in consideration of responses to consultations connected with the development of the Scheme and the Stocktake exercise, to come forward with constructive, innovative and attractive propositions.

B3.3 As well as according with the intention to progress changes on the basis of affordable retention, due weight has been given to the increasing significance of the needs of employers who wish to recruit and retain the best available talent from the workforce.

B3.4 The Society of Chief Personnel Officers has developed its own principles from which it believes a modern pension scheme for local government should be based. Its approach has been helpful in drawing up the basis of new elements for any future scheme changes. So too has the positive advice received from the Employers' Organisation for Local Government on the most effective way to proceed, along with its advice on the underlying necessity of balancing affordability with the desire to retain a final salary scheme. Suggestions on the potential for revising the extant scheme's benefit package have also been received from trades union interests and these too have been carefully considered in developing the elements now outlined below.

Basis

B3.5 In developing the basis of a new benefit structure for the LGPS(S) due regard must be given to balancing the pressures generated by the desirability of:-

- providing adequate levels of benefit in retirement to enhance social cohesion;

- the need to ensure the financial sustainability of pension systems; and

- the need to respond to the changing needs of all stakeholders.

B3.6 Thus some of the issues proposed need a corresponding cultural shift in employment practices. Employers must recognise the challenges faced by an ageing workforce in an ageing society. Employees must be given the opportunity to continue to be economically active for longer. It is also necessary to continue to provide a pension scheme which is non-discriminatory, continuing the

principle recognised by the LGPS(S) through changes made to both the 1987 and 1998 Regulations.

B3.7 The opportunity will be taken to make the overall benefit package simpler to understand. Any future benefit package should be easier to administer, but administrative simplification alone has not been the driver of this part of the exercise. Administration has to be proportionate to the needs of those with an interest but the needs of those have been the main determinate in setting out the Scheme design.

B3.8 It will be noted at this stage that requests for the introduction of totally open multi-choice options, the cafeteria approach, have been resisted. Whilst individuals should have flexibility available to them, they have to be aware of the impact of making such a choice. The options available have to be clear and understandable, not just to pensions professionals but to individuals making long term financial planning decisions. There is also a risk that total freedom to pick and choose can undermine the basic strengths of a pension arrangement designed to encourage inter-generational solidarity. For example, providing capacity to ask individuals to pay more for survivor benefits may lead to a risk of single members seeking refunds. There are also issues of complexity of administration and the expectancy of a pension income stream not being matched in reality.

B3.9 The proposed elements of a new-look LGPS(S) build on the flexibilities already introduced into the LGPS(S) in 1998.

Elements

- In common with the other public service pension schemes, in any new-look LGPS(S) there would be a Scheme Retirement Age (SRA) of 65. Benefits taken as of choice before SRA would be subject to an actuarial reduction. Benefits drawn post SRA would be subject to an actuarial increase. The actuarial reductions/increases would be cost neutral to the Scheme and reflect the costs/savings of paying pensions before or after SRA. In both instances, members could be in receipt of pension benefits and continue to accrue further membership whilst they remain in a relevant employment.

- Benefits could be linked to final basic salary, and could accrue on the basis of 1.6% per year, for example 10 years of membership would equate to a pension of 16% of basic salary. Basic salary does not include overtime, fees or bonuses.

- The salary used in calculating the contribution rate could be that at the start of the financial year or, if employment commences or changes during the period, the salary on commencement of the job.

- It is not intended that there would be an automatic lump sum in any new arrangement. Individuals could instead be able to commute up to the maximum permissible under Inland Revenue rules, i.e. 25% of the capital value of the benefits accrued at the point they are paid, up to ten years before or after SRA. The commutation rate could be 12:1; for every £1 of pension surrendered, £12 of lump sum would be awarded, up to the Inland Revenue 25% limit.

- Apart from the new Inland Revenue allowances, from 2006, there could be no Scheme limit on the period of membership which could accrue in relation to employment.

- There would be no facility to buy additional membership of the Scheme but consideration could be given to providing a defined contribution LGPS(S) top-up arrangement.

- There would be no requirement for employers to offer an AVC arrangement. However, members would be able to use an external AVC arrangement or take advantage of the Inland Revenue changes which will allow concurrent membership of registered pension schemes.

- Death in service benefit could be 3 times final basic salary, paid as under the current arrangements, in consideration of the member's expression of wish as to who they nominate to receive the payment.

- There would be no short-term survivor benefit provisions. Adult survivor benefits could be 50% of the pension after any commutation. Individual child survivor benefits could be 25% of the pension after any commutation and limited to a maximum of 50% where multiple dependants exist. Payment of childrens' pensions could cease at age 18.

- Enhanced Ill health benefits could be payable only where a member is permanently incapable of any employment, with enhancement up to the scheme retirement age. Consideration could be given to similar enhancement in relation to survivor benefits which are paid following death in service.

- The Scheme could continue to offer unreduced benefits to early leavers whose departure is outside their control, and where

termination of employment occurs on or after the members 55th birthday.

- Any provision for the payment of pension benefits on redundancy grounds would not extend to statutory redundancies that would not attract any statutory redundancy payment. In a changing employment environment, and as part of the Government's policy of increasing the number of those who are still economically active after 50, it is believed that redundancy and efficiency retirements will reduce from the levels seen in the previous two decades.

- The total illustrative future service cost, to be met by employer and employee contributions, of this package has been calculated as being in the region of 21% of pay, but would clearly vary depending on the profile of each employer's members and the final detail of any ultimate new-look arrangement.

B3.10 Consultees will wish to consider the propositions above in depth during the consultation period. Their pros and cons will require careful assessment and discussion. Ministers in due course will wish to go forward with a clear choice as a basis for any new, longer-term benefit package.

Benefit Illustrations

B4.1 The following tables set out an illustration of the benefits which could be provided under a new-look arrangement.

B4.2 Table 3 below shows the annual pension payable, based upon an accrual rate of 1.6%, a salary of £20,000 and with varying periods of membership. The final 2 columns show the maximum lump sum that could be allowed under Inland Revenue tax regime and the pension that would be payable if the scheme allowed, and the member chose, the maximum lump sum to be taken.

Illustration of Post Commutation Pension Benefits (25%) Table 3

Total Scheme Membership	Pension as Percentage of Final Salary	Final Basic Pay	Maximum Pension	Inland Revenue Capital Value	Maximum Lump Sum	Pension if Maximum Lump Sum Taken
5	8%	20000	1600	32000	8000	933
10	16%		3200	64000	16000	1867
25	40%		8000	160000	40000	4667
40	64%		12800	256000	64000	7467
45	72%		14400	288000	72000	8400

B4.3 Table 4 below, on the same basis as the one above, shows the pension that would be payable if the member chose to take a lump sum equivalent to the 3/80ths provided under the current Scheme.

Illustration of Post Commutation Pension Benefits (3/80ths)Table 4

Total Scheme Membership	Pension as Percentage of Final Salary	Final Basic Pay	Maximum Pension	Lump Sum Under Current Scheme	Pension if Equivalent Lump Sum Taken	Pension that would have been paid under current scheme
5	8%	20000	1600	3750	1288	1250
10	16%		3200	7500	2575	2500
25	40%		8000	18750	6438	6250
40	64%		12800	30000	10300	10000
45	72%		14400	33750	11588	11250

B4.4 The scheme benefits and contributions set out in this and the preceding sections are intended to stimulate discussion and debate in an important area for all stakeholders, no matter how central or peripheral they may be to the LGPS(S).

Defined Contribution Top-up Scheme

B5.1 To provide further choice and scope within the Scheme for members and potential members who want to maximise their benefit, the Scheme could also provide a defined contribution money purchase arrangement.

B5.2 An arrangement could be provided for members who wish to contribute in respect of any elements of their pay which do not constitute basic salary and are not, therefore, included in the core, final salary based benefit package. For members with overtime or fees which may vary during their employment, this would provide a facility to make additional contributions based upon fluctuating payments over a career.

B5.3 Members of the defined benefit final salary arrangement could also be allowed to contribute concurrently to the DC in relation to pensionable earnings. Such an arrangement would provide an opportunity for members to provide additional pension provision for themselves and could be used to provide additional benefits in order to facilitate earlier retirement or to finance a phased retirement. Such opportunities chime with the aim of more choice in the Scheme and more structured opportunities to build up greater pension benefits to enhance income in retirement.

B5.4 The provision of a DC scheme alongside with the main new-look Scheme could help to overcome the specific shortcomings of a defined benefit scheme in relation to contributions made at any point in a working life where they would not count for final salary benefit calculation purposes. For instance, where overtime is worked disproportionately during early years of employment but declines later on. It also overcomes the inequality seen where members receive an artificially higher final salary due to exceptional or unusual payments being made during the last few years of their employment.

B5.5 A DC arrangement would only run in parallel to the defined benefit arrangements in the new-look Scheme and would thus have some of its investment costs and risks more easily managed by the providing authority.

B5.6 Consultees views on such a proposition are invited. If consultees consider that there are other options worth exploring as part of the exercise, which would help to improve choice and provide members with opportunities to make additional voluntary provision, it would be helpful to receive them.

Questions relating to Scheme Development

B6.1 The previous sections throw up a number of questions and residual issues. In order to add to the debate and discussions during the consultation consultees are invited in their responses to explicitly comment where appropriate on the following questions which arise from sections above. NB: For your convenience, the questions listed below together with other questions arising throughout the document have been collated into a separate questionnaire. The SPPA would appreciate you taking the time to complete this and return it to us by the deadline.

B6.2 Decisions will have to be made on how to manage internal transfers (and IFAs) in the future. Should inter fund adjustments automatically provide year for year service or is there a case for extending the principle introduced for handling the cessation of concurrent employments?

B6.3 Should day to day transfers apply to members who move jobs between contribution bands, or should the membership period be adjusted to reflect the contribution band in the new post?

B6.4 How should the Scheme deal with non-Club transfers, should they buy membership or go to the top up arrangement?

B6.5 How should multiple-employments be dealt with under the new Scheme? For example, should total basic pay be considered when establishing the appropriate employee contribution rate in view of the higher tax relief received by the member?

B6.6 Is there any need to deal with the issue of multiple employments below the threshold(s)?

B6.7 What scope should there be for dependants benefits to be ½ (or ¼ for children) of actual pension in payment or what would come into payment? Should the Scheme offer flexibility over how death benefit and commutation can be applied in such circumstances?

B6.8 What scope should there be for considering reduction in survivor benefits where there is significant age differential?

B6.9 Should consideration also be given to providing a facility for members who elect not to join the defined benefit Scheme to contribute instead to the defined contribution arrangement, with an appropriate level of employer contribution?

B6.10 On what basis should members' contributions to any defined contribution arrangement be invested or protected? For instance, would it be appropriate to consider offering a provision where any capital invested is protected, alongside an investment return based upon a proportion of any real return realised by the fund, or against a national index?

B6.11 Alternatively, instead of having added year provisions to purchase additional scheme benefits, should actuarial colleagues be asked to set a charge for purchasing £100 of annual pension?

Flexible Retirement

B7.1 At present, the tax treatment of occupational pension schemes does not allow people to work and draw a pension from the same employer. In 2001, a Treasury-led Review of Ill-Health Retirements in the Public Sector recognised that the lack of such a facility created a "cliff-edge" between work and retirement where a stark choice between one or the other had to be made. The subsequent action plan

recommended that the LGPS(S) should incorporate flexible retirement provisions when the necessary tax legislation permitted.

B7.2 The Government has since introduced the concept of flexible retirement as part of its agenda for simplifying the tax treatment of occupational pension schemes. This will be achieved mainly by removing the concept of normal retirement age from the tax rules. Under the new tax regime, to take effect in 2006, members could draw a part of their pension whilst still working for the same employer as an alternative to retirement. Flexible retirement, as it has become known, is therefore intended to encourage those who wish to work longer, to do so.

B7.3 In taking this concept forward, pension schemes have been asked to help wherever possible to ensure that their scheme rules do not discourage flexible retirement. In particular,

- members are offered a fair return for deferring their pension while they work beyond normal retirement age;
- those who work beyond normal retirement age are able to continue to build up their pension entitlement, and
- members in final salary schemes who opt for part time employment or who step down in responsibility near the end of the careers should be treated fairly.

B7.4 A twin-track approach for the LGPS(S) in the future seems appropriate. Firstly, age discrimination legislation will be introduced by 2006 to prevent discrimination on age grounds. Further flexibility will be allowed by relaxing current tax law to allow employees to continue in work whilst drawing on their occupational pension scheme.

B7.5 Currently, Regulation 19(4A) of the LGPS(S) regulations provides that when a member's LGPS(S) benefits become payable where he has remained in employment after his 65th birthday, those benefits are actuarially increased for each day payment was deferred by. At present, where a member attains age 65 he can no longer continue to count additional membership (exceptions are currently made for specific persons). Going forward, it seems appropriate to allow members to continue to contribute to the Scheme at any age.

B7.6 It is envisaged that the introduction of flexible retirement provisions in the LGPS(S) would provide for employer discretions to assist in the on-going management of staff. Advantages are seen in the introduction of provisions for LGPS(S) employers to allow members aged 55 or over to draw some or all of their accrued pension benefits

whilst remaining in full or part time employment. Such an amendment would allow members to take a gradual approach to retirement where this supports the business needs of the relevant employer, rather than all interests having to cope with the current 'cliff edge' experience.

B7.7 The regulations could provide that such payments may only be made where there is a reduction in the hours and/or pay or, alternatively, such matters could be left for each employer to determine locally in a policy statement specifically related to such events. Under the new tax regime for registered pensions members could be able to rejoin the LGPS(S) in their new employment and, therefore, accrue further pension benefits. A helpful approach might be to provide that scheme employers be required to formulate a policy as to how they will exercise flexible retirement provisions and, subject to that, members would be able to make a request to their employer.

B7.8 Consultees are invited to comment on the following potential options:-

B7.8.1 Members who have attained age 65 and remain in relevant employment could be allowed to continue to accrue LGPS(S) membership regardless of the extent of their total membership; or

B7.8.2 Members' LGPS(S) benefits may be put into payment at age 65 and if they remain in relevant employment they may rejoin the Scheme and accrue further LGPS(S) pension rights.

B7.8.3 Members who have attained age 55 and meet any qualifying requirements (e.g. reduction in pay or hours / local policy statement criteria) may elect for payment of accrued LGPS(S) benefits. Where benefits are brought into payment early under such provisions they would be actuarially reduced to reflect this fact; and

B7.8.4 Members would be allowed to continue in relevant employment with the Scheme Employer whilst drawing their accrued LGPS(S) benefits and may also be allowed to rejoin the Scheme and accrue further membership.

B7.9 Any new scheme benefit package will need to ultimately ensure that local government, through the LGPS(S), overriding tax legislation and human resource policies, is able to operate successful flexible retirement policies. It is important that the LGPS(S) contains no impediments or barriers to such policies, given the complementary

provision they provide to allow members to take an appropriate and measured approach to retirement, set against the scheme's retirement age and employers' needs.

Survivors' Benefits

Married and civil partners

B8.1 Currently the LGPS(S) provides pension benefits to the surviving spouse of a deceased scheme member. No such provision is available for unmarried partners of either the opposite or the same sex as the member.

B8.2 If the Government's Civil Partnership Bill becomes law, the LGPS(S) will be required to provide survivor pensions for same sex registered civil partners, calculated on the member's service accrued after the Bill's enactment. For existing members, the LGPS(S) is also likely to have discretion to introduce arrangements to take previous service into account at member cost. This could be achieved on transition to the new scheme by treating all accrued service as membership of the new scheme and making appropriate service adjustments. (Married members will be treated similarly to remove any remaining differences in survivor benefits which may apply for historic or gender reasons to members with long service.)

B8.3 Therefore, there are existing or planned mechanisms available (marriage through either a civil or a religious ceremony, and registration of a civil partnership) under which both opposite and same sex partners would automatically have an entitlement to survivor benefits. In the new scheme this would be on a common total membership basis for both new and existing members.

Cohabiting partners

B8.4 There are no proposals which would require pension schemes to provide survivor pensions to partners who are neither married nor registered as civil partners. Government policy, however, is that public service schemes such as the LGPS(S) may provide these benefits (referred to here as cohabiting partners' pensions) if the general membership wants them and pays any extra costs. The employers' representatives and trade unions jointly put forward proposals in 2001 for introducing cohabiting partners' pensions. However, the additional costs would have been funded not by members but by employers

forgoing potential future savings; this was out of line with Government policy.

B8.5 Earlier discussions papers pointed to the need to address the issue of cohabiting partners' pensions. In response, the Employers' Organisation proposed a 7% employee contribution rate for including cohabiting partners' pensions based on future membership in the benefit package (optional for existing members, and with past service buy-back terms). The TUC pressed for cohabiting partners' pensions to be provided with no increase in employee contributions; however, this again did not accord with UK government policy.

B8.6 However, the development of a new benefit package allows cohabiting partners' pensions to be introduced within the framework of a new-look scheme.

B8.7 Certain considerations arise from the difference between cohabiting partners and married couples or civil partners. For married and civil partners, entitlement is easy to prove objectively and provisions should be simple to administer. For cohabiting partners, clear evidence would be necessary to show that they were living together as if they were husband and wife or civil partners. For the LGPS(S), as for other public service schemes, evidence of the following would be needed:

- co-habitation;

- an exclusive, long-term relationship established for a minimum of 2 years;

- financial dependence or interdependence; and

- valid nomination of a partner with whom there would be no legal bar to marriage or civil registration.

B8.8 Administering authorities would need to satisfy themselves that the evidence demonstrates that the member and cohabiting partner were living together in a relationship akin to marriage or civil partnership.

Back-dating

B8.10 In line with normal government policy, cohabiting partners' pensions would be based on membership accrued after the date the provision is introduced. There is a question for existing members whether past membership should be taken into account, though this

could only be at member cost. If so, the question then arises whether this should be automatic and compulsory, which would simplify administration and put cohabiting partners on the same footing as married and civil partners, or introduced as a member option. If the compulsory option were adopted, transitional service adjustments as for civil partners might appear to be the best mechanism. If an optional approach is adopted, either membership adjustment or additional payments (one-off lump sum, or instalments) might be considered.

B8.11 Consultees' views are sought on the following questions:

B8.11.1 whether the proposal that existing members' past membership should be taken into account for civil partners' benefits in the new scheme through appropriate transitional membership adjustments;

B8.11.2 the introduction of cohabiting partners' pensions;

B8.11.3 the proposal that administering authorities should determine eligibility for cohabiting partners' pensions, and whether the criteria for so doing are met;

B8.11.4 whether to provide buy-back terms for past service of cohabiting partners;

B8.11.5whether any such buy-back should be optional or compulsory; and

B8.11.6 how buy-back might work - eg by membership adjustment on moving to any new-look scheme or by an additional payment by lump sum or instalments.

Ill-Health Retirement and Income Protection

B9.1 Under the existing provisions of the LGPS(S), local authority employers, in conjunction with their medical advisers and on the basis of a certificate from an independent medical practitioner (IMP), are required to assess the permanency of an incapacitating condition at the time employment ceased. This arrangement places a significant burden on the medical profession in terms of making a reliable and robust prognosis in each case and takes no account of post-retirement improvement or deterioration in a person's medical condition or earnings potential.

B9.2 Neither do the current regulations differentiate between those scheme members whose incapacity prevents them from undertaking any gainful employment in the future and those who have an incapacity in relation to their existing duties but who remain capable of performing a wide range of employment, either in local government or elsewhere.

B9.3 To overcome these problems, the Principal Civil Service Pension Scheme, for example, has already moved to a two-tier ill-health retirement arrangement and other major public service pension schemes are currently developing similar proposals. It is proposed that the LGPS(S) should follow suit at the earliest opportunity on a broadly similar basis.

B9.4 The proposition has been put forward in the Scheme Benefits Section (B3) that ill-health retirement provision would only be payable from the Scheme where, in the IMP's opinion, the member was permanently incapable of ANY further employment up to SRA. In such case enhancement up to the SRA would apply. This is a significant improvement – in line with PCSPS and good private sector provision – providing much greater security for families and individuals most in need of support following such a substantial change in circumstances.

B9.5 This proposal, in line with considerations underway in other public service pension schemes, provides a top tier of benefit from the Scheme. There is some concern that advances in medical science could vary at a later date the totally valid opinion provided at the relevant time by the IMP. Thus, the PCSPS has included in its top tier a review mechanism. This consultation paper provides the opportunity for consultees to comment on whether such an approach should form part of any new-look LGPS(S).

B9.6 The approach of providing an improved benefit package for a smaller proportion of the membership leaves a separate issue to be resolved. To what extent should a second tier of benefit cover members who are unable to perform the duties of their existing employment. It is highly likely for such cases that an IMP would express the opinion that such members are likely to be capable of undertaking alternative employment. Perhaps even with the same earnings capacity. It is therefore proposed that members in this second tier should be entitled to the payment of their accrued pension rights with no enhancement. Such payment would be subject to a review process, with the benefit ceasing or being reduced where a member took up subsequent employment.

B9.7 It has to be recognised that this is, in reality, an employment, and management of that employment, issue rather than a pension issue.

But the pension scheme could be used by way of assisting the management of such cases.

B9.8 A more radical alternative approach perhaps would be to consider the potential scope for removing such income protection cases from the pension scheme. This would mean that, other than flexible draw down provisions, a pension is only paid from the Scheme when a member will not, or is not able to, work again. Benefit, calculated on the same accrual basis as a pension, would operate alongside the top tier set out above and in the benefit Section. Such an arrangement to provide income protection could also sweep up all the current injury allowance discretions.

B9.9 There is a wide choice of commercial products in the insurance sector that offers the sort of income protection that could be adopted as a viable alternative to the majority of ill-health retirement cases where the capacity to perform gainful employment of some kind is not at issue. Another option, therefore, would be for the new scheme to set out the general framework for income protection arrangements but leaving individual local authority employers to make their own local arrangements, using external contractors where appropriate.

B9.10 There are several key matters for discussion and debate raised here on which consultees' views are invited. It seems likely that specialist stakeholders will need to take forward these in greater depth within the consultation period in order to provide a firm basis for future policy decisions.

Compensation

B10.1 There is also now a statutory necessity to review the compensation provisions arising from the Department for Trade and Industry proposals on age discrimination legislation, which will have to take effect from October 2006. As a consequence, the current provisions, which are in part based on age, used to determine the amount of the one-off compensation payment or whether an employee can be considered for an award of a credited period (commonly referred to as compensatory added years) must be replaced.

B10.2 It has also been suggested by stakeholder interests, including the Society of Chief Personnel Officers, that the current provisions do not provide sufficient flexibility, nor do they meet the day-to-day business needs of individual local authority employers. The opportunity has therefore been taken to review the overall discretionary package that currently applies to local authority employers in Scotland.

B10.3 One possible way forward would be to revoke the current provisions and to replace them with a facility to make a discretionary one-off lump sum payment based on a specified period of service multiplied by pay. The current regulatory maximum is 66 weeks pay.

B10.4 An alternative, which has been discussed in principle with HR practitioners, might be to set a legal maximum level of payment and within that limit to require employers to make specific decisions in respect of an individual's level of service and pay, on the basis of a agreed policy and business plan which is workable, affordable and reasonable, having regard to foreseeable costs. The policy would also need to take account of age discrimination issues, as well as any other employment or discriminatory legislation. To ensure this approach worked on value for money grounds and was fully transparent, employers would clearly need to be able to demonstrate their business case for the level of the award they determine to be appropriate which would itself be subject to usual levels of audit scrutiny.

B10.5 To ensure that the new provisions meet the needs of stakeholders, it would be helpful to have views on the following questions. These are not comprehensive and comments on other relevant issues are welcome, particularly on the form and content of the associated business plan and policy document, the requirement for which would need to be built into any reformed regulations.

B10.6 Consultees are invited to comment on the following questions and to add to the debate as they feel appropriate:-

B10.6.1 Should such awards be limited to cases where the employee is made redundant?

B10.6.2 Is there a case for including employees where cessation of employment is under a compromise agreement or for another reason i.e. where seeking volunteers to mitigate compulsory redundancies?

B10.6.3 What sort of matters should be set out in the business plan and policy document?

B10.6.4 What might be an appropriate maximum level of award?

B10.6.5 Is there a case for allowing LGPS(S) members the option to exchange cash payments for LGPS(S) pension benefits of equivalent value?

INLAND REVENUE CHANGES

Finance Act 2004

B11.1 The Finance Act 2004 received Royal Assent in August 2004 and establishes a new tax regime for all registered pension schemes, which comes into effect on 6 April 2006.

B11.2 The current LGPS(S) regulatory framework will need to be amended to take account of the changes to the tax regime, from 2006. The new tax regime will allow additional flexibility, which may be incorporated into the Scheme from this time, but could more appropriately be introduced in any new-look arrangement.

B11.3 To take forward the changes that need to be implemented by 6 April 2006, the SPPA will issue draft amendment regulations to interested parties in Scotland in mid 2005. In the interim period views are sought on the questions at the end of this Section.

Overview of the new tax regime for registered pension schemes

Lifetime allowance

B11.4 The new tax regime provides a lifetime allowance on the amount an individual may accrue in pension rights before those benefits are subject to a tax charge in addition to the normal income tax levy on pension benefits. Where a person's total pension benefits exceed the lifetime allowance a charge will be applied to the excess benefits at the point that they are paid. Where the excess is paid as a pension, a charge of 25% will be applied in addition to the 40% income tax rate. If the excess is paid as a lump sum, a charge of 55% will be applied.

B11.5 The lifetime allowance is £1.5m in the 2005/06 tax year and will rise in annual steps until 2010, as set out below. From 2010 the lifetime allowance will be indexed.

B11.6 Lifetime Allowance for the tax years 2006/07 to 2010/11

2006/2007 £1,500,000
2007/2008 £1,600,000
2008/2009 £1,650,000
2009/2010 £1,750,000
2010/2011 £1,800,000

B11.7 It should also be noted that new regime will allow individuals to be active members of the LGPS(S) whilst concurrently contributing to alternative pension arrangements. The lifetime and annual allowances apply to an individual's total pension rights, including any AVCs, added years contracts, defined contribution pension rights and concurrent personal pension rights.

Annual allowance

B11.8 In addition to the lifetime allowance there is an annual allowance on an individual's pension benefits. Where a member's pension benefits increase beyond the annual allowance in any year, the excess will be subject to a 40% tax charge, thus effectively removing the preferential tax treatment for any excess benefits. The annual allowance is initially set at £215,000 for the tax year 2005/06 and will also increase in predetermined annual steps until 2010, as set out below. From 2010 the annual allowance will be indexed.

B11.9 The annual allowance will not be assessed against the contributions paid in respect of a member, but against the increase in value of their pension benefits during the relevant tax year, using a factor of 10.

B11.10 For example, in the current LGPS(S), a member's scheme benefits will be assessed as having increased in value at:

- 10 times 1/80th of their pensionable pay plus 3/80ths of their pensionable pay, plus
- 10 times any increase in pensionable pay multiplied by the total period of LGPS(S) membership to which the increase applies.

B11.11 For example, the increase in a member's LGPS(S) benefits during a year, where pensionable pay rose from £20,000 to £24,000, the members total membership increased to 6 years and they were awarded 2 years additional membership, would be assessed as follows:-

10 x the LGPS(S) benefit arising from the period of membership in the tax year
(10 x (24000 x 1/80)) + (24000 x 3/80) = £3,900
+
10 x the increase in LGPS(S) benefits arising from the £4,000 increase in pensionable pay
(10 x (4,000 x 5/80)) + (4000 x 3/80) = £2,650
+
any additional service awarded to the member.
(10 x (24000 x 2/80)) + (24000 x 3/80) = £6,900
=
Increase in LGPS(S) benefits during the year = £13,450

B11.12 Where a member's benefits increase above the annual allowance, a tax charge of 40% of the excess will arise.

B11.13 Maximum Annual Allowances for the tax years 2006/07 to 2010/11
2006/2007 £215,000
2007/2008 £225,000
2008/2009 £235,000
2009/2010 £245,000
2010/2011 £255,000

Tax Free Lump Sum

B11.14 The new tax regime allows Schemes to offer a tax free lump sum of up to 25% of the assessed value of a member's pension benefits. This would mean that an LGPS(S) member with 20 years membership of the current Scheme and a final salary of £20,000, could be offered a tax-free lump sum of £28,750.

B11.15 The current LGPS(S) provides an automatic lump sum benefit of 3/80ths, in the example given - £15,000. As discussed in Section 2, it is not proposed that any new-look LGPS(S) would provide an automatic lump sum. Rather consideration could be given to allowing members to choose to commute part of the pension to provide a tax free lump sum up to the permissible maximum on retirement, up to the 25% allowed under the new tax regime, as discussed in Section B.

B11.16 It is believed that such an approach would provide members with the flexibility to take their own decisions about the pension benefits that are appropriate to their own needs. As members would be allowed to contribute concurrently to any other pension arrangement, they could, for instance, make voluntary contributions to a defined contribution

pension scheme to provide a tax-free lump sum at retirement and therefore chose not to commute any part of their new-look LGPS(S) benefits.

Flexible Retirement

B11.17 As discussed in Section 2 "Flexible retirement", the new tax regime allows members to take a phased approach to retirement, rather than the current cliff edge – allowing those people in occupational pension schemes, where scheme rules allow it, to continue working whilst drawing retirement benefits.

B11.18 In designing any new-look Scheme, consideration will be given to the most appropriate way for the Scheme to embrace this flexibility and provide employers with the powers to develop retirement policies which meet both their needs and those of their employees.

Total Membership

B11.19 Currently the LGPS(S) includes a number of restrictions on the period of total membership a person may count under the Scheme. Under the new tax regime there would be no requirement to retain such limits in the Scheme. The removal of the current restrictions would ensure that members continue to accrue membership for any period they remain in employment and continue to contribute to the Scheme, and would remove the current disincentive for longer serving members to continue in service after attaining 40 years membership.

Members Contributions

B11.20 The LGPS(S) currently prohibits members from contributing more than 15% of their pensionable pay in any tax year. This restriction applies to total contributions, ie the total contribution made to the Scheme and to any added years contract or AVC vehicle. The new tax regime will remove such restrictions on the amount of contributions a member may make to registered pension schemes.

B11.21 As proposed earlier in this Section, there would be no requirement for the Scheme to allow members to purchase added years in the future, nor will there be a requirement for Scheme employers to offer access to any additional voluntary contribution vehicle. If, under any new-look arrangement, there would be no facility for members to purchase additional membership of the LGPS(S), it appears that it would no longer be necessary for the Scheme to restrict the level of contributions which a member may make.

High Earners

B11.22 The transitional arrangements for the protection of rights accruing before the new regime comes into force may be relevant to some senior members of the Scheme. Individual members should seek their own professional advice on the effects of the new tax regime.

B11.23 Consultees are invited to comment on the following propositions in relation to both the current Scheme and any development of a future LGPS(S):-

B11.23.1 Should the LGPS(S) introduce a scheme specific maximum pensionable salary equivalent to the current Inland Revenue earnings cap for post 1989 joiners?

B11.23.2 If the LGPS does not introduce a Scheme specific salary cap, should the Scheme include specific provisions to prevent any member who is current subject to the earning cap from making a windfall gain? For example if the Scheme did not introduce a salary cap, a member who is currently subject to the £102,000 employment cap, but earns £150,000, would suddenly have a higher pensionable pay figure, despite never having paid contributions in respect of the £48,000 excess above the cap. This would result in considerable cost implications for the employing authority.

B11.23.3 If a salary cap is introduced in the Scheme, what measures should be taken to protect the uncapped position of certain pre-1989 members?

B11.23.4 Should the LGPS(S) remove the maximum 40/45 year total membership restrictions and, if so, should consideration be given to removing them from the current Scheme from 2006 or only in relation to any new-look Scheme from 2008?

B11.23.5 Should members be permitted to accrue further LGPS(S) membership even if they have reached or exceeded the new Inland Revenue lifetime limit? Note: This is not simply a pension issue but relates to terms and conditions of employment, pressures on pay negotiations and consequential pay drift.

B11.23.6 Should any new-look LGPS(S) restrict scheme benefits to a specified level, for instance the lifetime allowance?

B11.23.7 Should consideration be given to allowing commutation lump sum payments up to 25% of the assessed value of a

member's pension benefits, or should any new-look Scheme offer a lower maximum lump sum?

B11.23.8 Should consideration be given to allowing employers to meet the tax charge arising from the award of an additional period of membership which results in a member's benefits increasing above the annual allowance?

B11.23.9 Should the current 15% limit on member contributions be removed from the current LGPS(S) from 2006 or only in relation to any new-look Scheme from 2008?

B11.23.10 Views are sought on the introduction of flexible retirement provisions, as set out on page 26, either in relation to a new-look scheme or from 2006.

Section C

Governance - Simplification

C1.1 In the context of developing a new regulatory framework for 2008 and beyond there is a firm prospect of a greater use of codes of practice, in close association with, a simplified, yet authoritative, regulatory framework. It is essential, therefore, to ensure, from the outset, that the regulatory framework to provide it is fit for purpose and that stakeholders subscribe to the approach being followed.

C1.2 The existing regulatory provisions will not be amended to provide the new scheme; the opportunity, therefore, exists for any totally new LGPS(S) regulatory framework to reflect innovative principles of regulation, current best practice and a minimising of prescription, balanced by a more concerted use of codes of guidance where this is appropriate and legally feasible.

C1.3 As currently set out in regulations made under powers in the Superannuation Act 1972, it is not the intention to change the statutory basis of the Scheme; however, this opportunity, to consider an innovative and fresh approach to the form and content of the regulations governing a new-look LGPS(S), should not be wasted.

C1.4 It follows, therefore, that in this consultative document, the basic principles of any new regulatory framework are associated and views sought from stakeholders on them.

C1.5 The regulations to define the new-look LGPS(S) will need to prescribe the core policy intention being sought, but there then remains considerable scope for either development of appropriately focussed codes of guidance and practice, in association with these core policy prescribing regulations, or, where the new regulations may prescribe the need for a policy statement, then codes of voluntary best practice could be developed alongside their preparation.

C1.6 In the preparation of new, policy-focussed provisions, the principles established by the Better Regulation Task Force (see paragraph C1.8 below) will be applied to SPPA's approach, together with a strong emphasis on the specific pension focus on simplification given by the report "A Simpler Way to Better Pensions" produced in 2002 by Alan Pickering. The report included recommendations about the need to explicitly identify the policy aim in legislation, from the outset, and that secondary legislation should be proportionate to that aim and avoid unnecessary complexity. Finally, requirements in statute

should focus on the objective to be achieved by the legislation, rather than the process to achieve it.

C1.7 These basic principles appear to be eminently transferable to the development of a new LGPS(S) framework, underpinned as they are by the principles of the Better Regulations Task Force, which are set out below.

Principles of Good Regulation

C1.8 The Better Regulations Task Force issued guidance in 2003 (see link below in para C1.9) about improving the quality of regulation and its enforcement. It's message was "that regulations are necessary, fair, effective, affordable and enjoy a broad degree of public confidence". It drew attention to earlier (1997) guidance which established five principles of good regulation:-

Proportionality -	regulations are produced only where necessary and appropriate to minimise the risks and costs;
Accountability -	regulations should be justifiable and subject to public scrutiny;
Consistency -	regulations should be joined up and implemented fairly;
Transparency -	regulations should be open, user-friendly, simple;
Targeting -	regulations should be focussed on the problem, be reviewed and modified if necessary.

Prescriptive legislation

C1.9 In developing an approach for a new-look LGPS(S) which could involve a greater use of codes of practice it should be acknowledged that they can, when used as a substitute for detailed and often over prescriptive regulations, be more effective, more responsive and provide better value for money. Having a statutory linkage, or even statutory backing through a compliance requirement provides added credibility and produces an effect on users which is often described as co-regulation (see for example Section 8 of the Better Regulation Task Force: Imaginative Thinking for Better Regulation Report 17 September 2003). Within the existing LGPS(S) this approach has been developed positively in recent years, initially, at least, in the investment regulatory framework.

C1.10 It is this sort of evolutionary step that provides a possible way forward for any new-look LGPS(S) and its associated new regulatory framework. As long as the Scheme retains its status as a public service pension scheme, then it must be set out in secondary legislation. However, if this new framework established a new balance between essential, proportionate regulation as against authoritative codes of practice prepared by recognised agencies - as already so ably demonstrated by CIPFA's Pensions Panel - then considerable simplification improvements might well be gained within any new statutory framework.

C1.11 Consultees will undoubtedly have a range of views on these matters. It is intended that in the course of developing a new framework, if and when this is forthcoming, that specific, early work on the aspect will be given priority with joint development working with key stakeholders within the consultation period.

Section D

Next Steps

D1.1 This consultative exercise is intended to be a significant step forward in SPPA's on-going stewardship of the LGPS(S). It is seen as essential that there is a strong and comprehensive engagement from the outset with, and between, all stakeholders about the propositions which have been set out in this document. It is essential that all opinions are expressed and discussed both during and beyond the consultation period.

Development Group

D1.2 SPPA will be involved in a development group of which is being established to provide an authoritative forum within which to discuss the proposals and any relevant alternatives, to examine their relative merits, to consider the practicalities surrounding the proposals and generally to assist SPPA during the consultation period on emerging issues linked to the development of a new-look LGPS(S).

D1.3 It would not, however, be the purpose of the Group to re-appraise established Government policy and its impact on the LGPS(S) but rather to move the agenda forward and to devise practical solutions to areas of complexity and change so as to ensure that the Government's policies for the Scheme's future affordability and sustainability are fully achieved within the timescale set. The group will include representatives from the following bodies

The Office of the Deputy Prime Minister
Local Government Association
Employers' Organisation/LGPC
Trades Union Congress
Society of Chief Personnel Officers
Association of Consulting Actuaries

Timing

D1.5 SPPA wish to provide an extended period of public consultation and consultees are therefore invited to respond by 20th May 2005.

D1.6 Going forward, it is envisaged that the outcome of the exercise will be reported to Ministers in the Summer of 2005, with a view to the

publication, later in 2005, of a specific set of proposals which will in due course form the basis of a new-look LGPS(S). It is envisaged that draft amending regulations would be circulated for consultation in 2006 with the intention of having the new scheme provisions coming into force in April, 2008.

Consultation Responses and SPPA Contacts

D2.1 The deadline for the receipt of responses is Friday 20th May 2005.

D2.2 Completed questionnaires and responses to the propositions set out in this document should be sent to Jean Steel, Policy Officer LGPS(S), Scottish Public Pensions Agency, 7 Tweedside Park, Tweedbank, Galashiels, TD1 3TE

D2.3 Completed questionnaires and responses may be sent by email to locgovpensionsreform@scotland.gsi.gov.uk.

D2.4 Any queries concerning the consultation, or requests for meetings to discuss the consultation package, should be directed to David Lauder, Policy Manager, by telephone on 01896 893227 or by 'e'mail to david.lauder@scotland.gsi.gov.uk