HARINGEY COUNCIL

NOTICE OF MEETING

Pensions Panel

MONDAY, 23RD JANUARY, 2006 at 19:00 HRS - .

MEMBERS: Councillors Rahman Khan (Chair), Beacham, E Prescott (Deputy Chair), Floyd, Milner, Patel and Reynolds

IN ATTENDANCE: Howard Jones and Roger Melling

AGENDA

1. **APOLOGIES FOR ABSENCE (IF ANY)**

2. **URGENT BUSINESS**

3. **DECLARATIONS OF INTEREST**

4. **MINUTES - TO CONFIRM AND SIGN THE MINUTES OF THE MEETING OF PENSIONS PANEL HELD ON 21 NOVEMBER 2005 (PAGES 1 - 6)**

5. **DEPUTATIONS/PETITIONS**

   To consider receiving deputations and/or petitions in accordance with Standing Order No. 35

6. **PRESENTATION BY NORTHERN TRUST**

   A presentation to Members by our custodian, Northern Trust

7. **ATTENDANCE BY FOUR FUND MANAGERS**

Each will give a 2 minute introduction and a 10 minute presentation, followed by 8 minutes of questions from Trustees and 5 minutes of questions from the Advisor and any other questions.

1. 7:25pm Fidelity
2. 7:50pm Capital
3. 8:15pm Bernstein
4. 8:40pm Wellington

8. FUND PERFORMANCE AND ADMINISTRATION UPDATES [REPORT OF CHIEF EXEC & DIRECTOR OF FINANCE] (PAGES 7 - 40)

9. NEW ITEMS OF URGENT BUSINESS - TO CONSIDER ANY ITEMS ADMITTED AT ITEM 2 ABOVE

Yuniea Semambo
Head of Member Services
5th Floor
River Park House
225 High Road
Wood Green
London N22 8HQ

David S Fishman
Principal Support Officer (Council)
Tel: 020 8489 2615
Fax: 020 8489 2660
Email: david.fishman@haringey.gov.uk

**MINUTES OF A MEETING OF THE PENSIONS PANEL:
21 NOVEMBER 2005**

Councillors *GMMH Rahman Khan (Chair), *E. Prescott (Deputy Chair), *Beacham, *Floyd, Milner, Patel and Reynolds.
[* Members present]

In attendance: Howard Jones* (Advisor to Trustees) and Vince McEntegart (Hymans Robertson).

1. APOLOGIES FOR ABSENCE AND INTRODUCTION:

Apologies for absence were received from Councillor Milner and from Roger Melling.

The Chair requested that a letter be sent to Cllr Milner requesting his presence at the future meeting of Pensions Panel as the Panel has been failing to receive input from the Executive Member for Finance because of his absence

2. URGENT BUSINESS:

There were no items of urgent business.

3. DECLARATIONS OF INTEREST:

No declarations of interest were received.

4. MINUTES:

RESOLVED:

That the Minutes of the meeting held on 10th October 2005 be confirmed and signed as an accurate record.

The Chair mentioned that, in relation to Item 5 of the 10th of October agenda (Reinstating the Rule of 85), he had written to the Leader saying that he is concerned about the solvency of the Fund and requesting that he impress upon Central Government, whenever there is engagement with them, the need to increase the Revenue Support Grant to take account of the extra costs in view of reinstating the 85 year rule.

5. REVIEW OF INVESTMENT STRATEGY:

Before asking the officers to present the report the Chair expressed concern as to how to comply with the legal comments in the report as to how, “act in the best interest of the beneficiaries as a whole” in the absence of any representatives at the Panel meeting from admitted bodies. It was said by the officers that the admitted bodies were present at the Annual General meeting of the Pensions Panel. The adviser to the Trustees advised to take legal opinion on the issue. The Chair drew the attention of

MINUTES OF A MEETING OF THE PENSIONS PANEL:
21 NOVEMBER 2005

officers to the subject.

A representative from Hymans Robertson (Mr Vince McEntegart independent of the scheme actuary) presented the company's report to the Panel.

Mr McEntegart said that the last time the company had been contracted to provide a review of investment strategy they had produced a 50-page report. This time they had produced a shorter document with supporting information provided. The Chair stated that the supporting documents, as mentioned in various sections of the reports were not released to members, and as such Panel Members were not aware if any fundamental information had been omitted. The Director of Finance assured the Panel that the key information were incorporated into the tabled reports, however the chair asked the officers that in future he would like to see reports from Hymans Robertson in full. In addition to the report, the representative of Hymans Robertson tabled a range of graphs, highlighting various points.

The first chart showed the forecast benefit outgoings for current members of the Pension Scheme. This was currently £20m per annum and would rise to a peak of £60m in 2030. After 2030, liabilities to current members of the scheme would start to reduce. However, of course, by that stage new members would have joined the scheme and so the total outflow of benefits would be higher as benefits would have to be paid to new members who had reached retirement age by then.

Combined forecasts for income and outflow were provided to 2023. The income for the scheme would come from 3 sources: standard employer contributions, employer deficit contributions and employee contributions. In April 2005, the actuary set the current rate for employer deficit contributions. Currently the net flow (the difference between the income and outgoing) into the Pension Scheme was positive but, in 2015, it was forecast to become negative if current contribution rates remained the same.

The Panel enquired as to what were the best safeguards the Panel could take so that admitted bodies would not default, because many of them have no tax raising powers of their own.

The Director of Finance advised the Panel that some admitted bodies had bonds to cover the risks. The Panel asked the D.O.F to let the Panel know in due course what safeguard the Panel could have in the case of admitted bodies, which had no bonds or tax-raising powers. The Chair pointed out that we must have proper safeguards to take account of the admitted bodies as a whole.

The Panel was advised that these would be: a higher contribution rate and asking those who had not already done so to take out bonds to insure themselves.

Members were informed that the distribution of assets of the Pension Fund was as follows:

- 70% - equities
- 23% - bonds

- 6% - property
- 1% - cash

Based on this, Hymans Robertson ran 5,000 different simulations as to what the future value of these assets would be. The 'funnel of doubt' increased as time moved on and so there was a larger range of possible outcomes.

The employer contribution rate needed by the Fund was modelled. The median figure obtained was 23.9%. There was a 50% chance that the employer contributions after 2007 would have to be higher than the current level.

The risk being run by the investment strategy was estimated as was the 'active risk' being run. The total risk was calculated as 12.6%. Half of this risk was due to the Fund's exposure to UK equities.

In order to reduce risk flowing from investments in UK equities, the suggestion was made that more money could be invested in overseas equities rather than UK ones; that the share of the fund made up of property could be increased from 6 to 10% and that 5% of the fund could be invested in private equities. These measures would reduce the proportion of risk accounted for by the UK stock market.

The strategy of the Fund is based on mainly investing in equities because more than 100 years of capital market data suggests that the best rewards with risks could be obtained from equities.

Demographic assumptions were made by the actuary, taking account of increasing life expectancy. These assumptions, like the assumptions relating to investment performance, are fair estimates – in that they reflect the best knowledge available at the time – but they may prove to be inaccurate.

The Chair stated that the Panel was guided in its decisions by the advice of the internal and external professionals and finally by the Director of Finance. Always the Panel sought optimum returns with reasonable risks.

The Director of Finance stated that he was satisfied with the report. No significant changes in the general balance of funds between the equities (70%) and other investments (30%) were recommended in the report. This was a recommendation the Director concurred with.

The adviser to the Trustees (Mr Howard Jones) stated that it would be desirable for Hymans Robertson to come back to the Panel at a future meeting with evidence that private equity and property would provide a good return and were worth increasing our exposure to. Also, members asked that more information be provided on emerging markets.

Decisions as to the allocation of funds between UK and overseas equities and between public and private equities would be made at a future date.

MINUTES OF A MEETING OF THE PENSIONS PANEL: 21 NOVEMBER 2005

Both the Chair and the Director of Finance reported that in the various meetings of the panel various fund managers commented that the return from overseas equities were better than the UK equities.

RESOLVED:

1. That the report be noted and the recommendation of the Director of Finance to continue to invest approximately 70% of funds in equities and the remainder in other assets be continued.

2. That Hymans Robertson present their next report at the 2nd February 2006 meeting of Pensions Panel.

3. That Hymans Robertson's next report also include the following items discussed at meeting:

- more analysis and the effect on the risk budget of options for splitting equities between UK and overseas.
- substance for justifying investing in private equity and for considering greater investment in property.
- More information be provided regarding investing in emerging markets, investing in hedge funds and also what the best available safeguards against interest rate risk, inflation risk and other risks are.

6. NEW ITEMS OF URGENT BUSINESS

There were no new items of urgent business.

7. EXCLUSION OF THE PRESS AND PUBLIC:

RESOLVED:

That the press and public be excluded from the meeting for item 10 below as the item contained 'exempt' information as defined in Section 100A of the Local Government Act 1972, namely that they contain terms proposed or to be proposed by or to the Authority in the course of negotiations for a contract for the supply of goods or services.

8. EXEMPT MINUTES:

RESOLVED:

That the exempt minutes of the meeting held on 10th October 2005 be confirmed and signed as an accurate record.

9. NEW ITEMS OF URGENT EXEMPT BUSINESS:

MINUTES OF A MEETING OF THE PENSIONS PANEL:
21 NOVEMBER 2005

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The meeting ended at 8:30pm

Signed……………………………………………………………………….....

Date…………………………………………………………………………...

COUNCILLOR GMMH RAHMAN KHAN
CHAIR.

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Agenda Item 8

HARINGEY COUNCIL

Agenda Item

Pensions Panel **On 23 January 2006**

Report title: **FUND PERFORMANCE AND ADMINISTRATION UPDATES**

Report of: DIRECTOR OF FINANCE AND CHIEF EXECUTIVE

Ward(s) affected: All	**Report for: Information**

1. Purpose

1.1 To consider the latest investment performance data for the Pension Fund and for each of the Fund's investment managers.

1.2 To consider regulatory changes affecting the administration of the Local Government Pension Scheme together with relevant issues covered in circulars issued by the Local Government Pensions Committee (LGPC).

1.3 To report 2005/6 budget monitoring to the end of December 2005.

1.4 To consider the way forward on training for trustees.

2. Recommendations

2.1 That the Fund Performance position as at the end of September 2005 be noted.

2.2 That the administration update be noted.

2.3 That the budget monitoring position to end of December 2005 (period 9) be noted.

2.4 That trustees training requirements be determined.

Report authorised by: Andrew Travers – Director of Finance

Contact officers: : Ian Benson, Pensions Manager (tel no: 020 8489 3824)

John Hardy, Head of Finance-Budgeting, Projects & Treasury (tel no: 020 8489 3726)

3. Executive Summary

This report sets out the fund performance and administration updates to end of September 2005 and Pension Fund budget monitoring to the end of December 2005.

4. Reasons for any change in policy or for new policy development (if applicable)

No changes are proposed.

5. Local Government (Access to Information) Act 1985

The following background papers were used in the preparation of this report:

Northern Trust Performance Monitoring reports

Fund Performance Update report to Pensions Panel on 10th October 2005

Regulatory changes and circulars received regarding the LGPS

6. Background

6.1 The investment performance of the Pension fund was last reported to the Panel in October 2005. That report covered the period up to 30 June 2005,at which time the following points were noted:

- The combined Haringey fund has increased in absolute terms since inception by 17.57% and under performed against the gross target by 2.08% in annualised terms.
- Bernstein, Fidelity and ING have met their agreed benchmarks to date with ING also meeting their target. Capital's performance worsened slightly since the position reported at the last meeting.
- The performance of Wellington improved marginally but remains a concern as annualised under-performance compared to benchmark and target since inception is 1.47% and 3.47% respectively. 27 months is a relatively short period of time and therefore will continue to monitor carefully as agreed as part of the healthcheck.

6.2 The investment performance of the fund is critical as it impacts directly on the level of employers contributions that the Council is required to pay.

6.3 This report updates the investment performance information by including data for the three month period up to September 2005. Members are aware that on 13 March 2003 our new Investment Management structure was implemented following a transition of investments from the old structure. This means that a new benchmark has also been implemented. Four new Fund Managers and an existing Manager, Capital International, took over active management for their new mandates from that date.

7. Combined Fund Performance

7.1 Performance of the overall fund compared to target is shown below. The target is shown gross of Fund Managers fees and assumes that returns above benchmark are achieved evenly throughout the year.

	3 months to end of September 2005	30 months to end of September 2005 (annualised performance)
	%	%
Overall fund performance	+6.68	+18.72
Benchmark	+6.89	+19.20
Performance versus benchmark	-0.21	-0.48
Overall fund performance	+6.68	+18.72
Target	+7.30	+20.85
Performance versus target	-0.62	-2.13

7.2 This shows that in the period to September 2005:

The annualised performance of the combined Haringey fund has increased in absolute terms by 18.72% but under-performed against the benchmark by 0.48% and target by 2.13%.

7.3 Appendix 1 shows the following for the combined fund as at end of September 2005 and 2004 for comparison purposes:(1) top ten shares held, (2) fund holdings.

8. Fund Manager Performance

8.1 Appendix 2 shows for each Fund Manager investment performance to 30 September 2005 compared to agreed benchmarks and targets as supplied by our performance manager, Northern Trust.

8.2 Gross performance targets for each Fund Manager are shown below. They denote the percentage annual return above benchmark over a rolling 3 year period.

Bernstein	2.0%
Capital	1.5%
Fidelity	1.4%
ING	0.7%
Wellington	2.0%

8.3 Trustees will remember that at the January 2005 meeting of the Panel it was agreed that a full review of the Fund's strategy be commissioned. The results of the review are likely to be available around the time that our structure has been in place for three years in April 2006.

8.4 Our latest quarterly meetings took place on 17 November 2005 between each Fund Manager and the Head of Finance–Budgeting, Projects & Treasury. Howard Jones, Advisor to Trustees, also attended. A summary of the key issues discussed at those meetings is set out below.

8.4.1 **Bernstein**
- Performance to date.
- Governance and SRI.
- Unbundling Commissions

8.4.2 **Capital International**
- Performance to date.
- Governance and SRI.
- Unbundling Commissions
- Bonds presentation

8.4.3 **Fidelity**
- Performance to date.
- Governance and SRI.
- Unbundling commissions
- Enhancements to research team
- Bonds presentation

8.4.4 **ING**
- Performance to date.

8.4.5 **Wellington**
- Performance to date.
- Measures being taken to address performance shortfall.
- Governance and SRI.
- Unbundling commissions

9. Conclusions

9.1 The combined Haringey fund has increased in absolute terms since inception by 18.72% and under performed against the gross benchmark by 0.48% and gross target by 2.13% in annualised terms.

9.2 Bernstein, Fidelity and ING have met their agreed benchmarks to date with ING also meeting their target. Fidelity have therefore improved since the annual healthcheck was reported in January 2005. Capital are 0.70% below the benchmark to date.

9.3 The performance of Wellington worsened slightly over the past quarter and is still a concern as annualised under-performance compared to benchmark and target since inception is 1.64% and 3.64% respectively. We will continue to monitor carefully as agreed as part of the healthcheck.

10. Budget monitoring for 2005/06 to end of December 2005

10.1 The Budget monitoring analysis to period 9 (end of December 2005) is attached in Appendix 3.

10.2 Significant variances to date are:

- transfer values paid and received where volumes will vary by year and timing within years,
- employee and employer contributions that are partly dependent upon transfers in and out of the scheme.
- investment management expenses which are influenced by timing of receipt of invoices from Fund Managers and market values.
- investment income which is dependent upon investments made.

10.3 As requested by trustees, greater analysis has been provided for management expenses. This now shows the amount of expenditure relating to administrative functions performed by the fund managers and the amount relating to their Investment activities. Trading costs, duties and commissions are excluded from this figure as they are deducted at source (from cash holdings) by the managers. Each fund manager provides an estimate of trading costs for the period in their quarterly performance grids.

10.4 In overall terms spend to date is within the budget. The current surplus is being monitored carefully so that any net gain is invested by the end of March 2006.

11. Training

11.1 It is an appropriate time to reconsider training needs of Trustees.

11.2 This issue was last considered at Pensions Panel on 24 March 2005. Following that meeting some trustees attended a Local Authority trustee workshop organised by Capital International or a broader based Pension Fund Trustee course run by the NAPF.

11.3 The council's investment advisers Hymans Robertson are now offering a training course targeted at local authority trustees.

11.4 The course has been designed with the objectives of the elected members acquiring a level of understanding of:

- their responsibilities as an administering authority of a local government pension fund.
- the fundamental requirements relating to pension fund investments.
- the operation and administration of the pension fund.
- controlling and monitoring the funding level.
- taking effective decisions on management of the Council's Pension Fund.

11.5 The course can be provided in a range of formats including a two day intensive course or spread over several sessions as required.

11.6 Further details on course content, format and the costs of the course to the fund are shown in appendix 4.

11.7 Our Fund Managers could be approached to provide training on various investment matters e.g. bonds as this is a relatively complex area. This could be done as part of a wider half day or evening of training.

11.8 Trustees views are sought as to the way forward.

12. Unlisted Investments

12.1 At the October 2005 Panel meeting trustees required clarification on the term unlisted investments. Unlisted investments are those holdings which are not listed on a stock exchange. Consequently, unlisted investments generally carry more liquidity risk as they are more difficult to trade. Most of the pension fund's investments are listed however certain property holdings are unlisted as are Fidelity's holdings in Institutional Open ended Investment Company (OEICs). The liquidity risk associated with the OEIC holdings are relatively minimal as the assets underling these investment vehicles are predominantly listed shares. Property holdings comprise less than 6% of the Fund and are held for the long term so liquidity risk is again relatively low.

13. Pensions Administration

13.1 **LGPC Circular 177 October 2005**

LGPC Circular 177 notified authorities of the Employer Organisation's response to the ODPM following a series of meetings of the Tripartite Committee.

The proposals put forward were previously supported by the Council as part of the consultation process on the Stocktake exercise on the Local Government Pension Scheme.

13.2 LGPC Circular 178 December 2008

Survivor Benefits for Civil Partners

The Civil Partnership Act 2004 allows same sex partners to register a civil partnership.

The earliest date for registration was 21st December 2005.

The LGPC has been amended by the LGPS (Civil Partnership) (Amendment) (England and Wales) Regulations 2005 to provide the payment of survivor pensions to civil partners and to eligible children. Calculation of survivor benefits is limited to membership from 5th April 1988.

A bulletin is planned for publication in February which will inform scheme members about this change to the scheme.

14. **Governance Policy**

14.0 The LGPS (Amendment) (No 2) Regulations 2005 require the publication and maintenance of a governance policy statement to be in place by 1st April 2006.

14.1 Guidance on the content of the Governance statement will be issued to authorities by CIPFA. On receipt of the CIPFA guidance, consultation will take place with relevant stakeholders with a view to bringing a policy statement to the March meeting of the Pensions Panel for approval.

14.2 Communication Policy

The above regulations also require the publication and maintenance of a communications policy statement. This policy statement is currently place, having been approved by Pensions Panel on 24th March 2005.

15 **Draft Amendment Regulation proposed for 6th April 2006.**

15.1 ODPM have published Draft Amendment (No3) Regulations for consultation.

15.2 These regulations result from the ongoing discussions of the Tripartite Committee and the consultation process under the Stocktake exercise to which the Council has already responded.

15.3 A summary of the main proposals is outlined below and this has been passed to the Corporate Industrial Relations Group for their information.

15.3.1 85 Year Rule to cease for service accrued after 30th September 2006. Transitional arrangements for older workers have yet to be agreed.

15.3.2 Members who wish retire from age 60, will be able to nominate a retirement date, and pay contributions to offset any reduction in benefits.

15.3.3 Membership of the scheme can be extended to age 75 (Limited to 65 at present)

15.3.4 15% limit on contributions will be removed allowing members more flexibility in building up pension rights.

15.4 The current Inland revenue restrictions will be replaced by a Lifetime Allowance of £1.5m and an annual accrual allowance of £215,000. Tax charges will only apply if pension benefits from all sources exceed the capital value of the Lifetime Allowance or if the value of benefit increase in any one year exceed the annual allowance.

15.5 Members will be allowed to convert up to 25% of the capital value of their pension to a single tax free lump sum payment.

15.6 Purchase of Strike Absence will be changed from a flat rate 16% of Pay to the employee rate plus current employer contribution rate.

15.7 Benefits deferred at 65 will be actuarially increased when the member elects for payment. Age for early release of benefits to remain at 50 but must increase to 55 by 2010.

15.8 Flexible retirement options to be available from age 60. The Head of Personnel will bring forward proposals for a flexible retirement policy.

15.9 A number of technical matters remain to be resolved and the LGPC will respond to the ODPM on these issues. A Bulletin will be issued to all scheme members informing them of the changes.

16 **Part-timer pension claims – the Beswick Case**

16.1 This matter relates to the long standing claims being pursued through industrial tribunals. The claims stem from a European Court of Justice ruling which recognised the right of some scheme members to but back a period of part time service.

16.2 The LGPC Circular sets out the Employer's Organisation view that claimants with pre 1st April 1988 part-time service should not now be allowed to resurrect a claim for earlier service when they had the opportunity to act at the time that Part time Buy Back provisions was first introduced.

17. Written statement to Parliament from the Minister for Local Government

17.1 Phil Woolas the Minister for Local Government made a written statement to Parliament on the consultation that had taken place around the 85 Year Rule.

17.2 The statement also refers to a paper to be issued for consultation in the summer of 2006 leading to regulations being in place by April 2007 and coming into effect in April 2008.

The statement is attached as Appendix 5

18. Cost of delay in implementing 85 Year Rule

18.1 Following advice from the Government Actuary and further consultation with the employers, the ODPM have advised that the provision to allow members to convert up to 25% of the capital value of their pension into an immediate lump sum payment will offset the cost of the delayed revocation of the 85 Year Rule. This proposal is included in the amendments scheduled to commence on 6th April 2006.

18.2 The Governments Regulatory Impact Assessment setting out a cost benefit analysis for this proposal is attached as Appendix 6

19. Early Retirements; Quarterly Report to 31st December 2005

During the period from 1st April 2005 to 31st December 2005 the following early retirements from Haringey Council were approved.

Haringey Council	**Early Retirements 1 April 2005 to 31 Dec 2005**			
Approved by D o F	**Cases**	**Cost of Added Years**	**Basic Capital Cost**	**Total Cost**
	***Redundancy*:**			
	4	£ 0	£101,000	£101,000
	Efficiency			
		£ 0	£0	£ 0
	The 85 year rule			
	0	£ 0	£0	£ 0
	Sub-Total			
	4	**£ 0**	**£101,000**	**£101,000**
Approved by Members	**Cases**	**Cost of Added Years**	**Basic Capital Cost**	**Total Cost**
	Efficiency			
	1	£407,000	£163,000	£570,000
	Redundancy			
	2	£63,000	£166,000	£229,000
	85 Year Rule			
	0			
	Sub Total			
	3	**£470,000**	**£329,000**	**£799,000**
Employing Bodies				
	Redundancy	**Cost of Added Years**	**Basic Capital Cost**	**Total Cost**
	0	£0	£0	£0
	Efficiency			
	0	£0	£0	£0
	The 85 Year Rule			
	0	£0	£0	£0
	Sub-Total			
	0	£0	£0	£0
Total For Haringey Council and Employing Bodies				
	7	**£470,000**	**£430,000**	**£900,000**

19.1 The early retirements for Haringey Council reported above, were approved under the terms of the scheme regulations and the Council's Policy on the use of its discretionary powers.

20. Appeals Process; Quarterly Report to 31st December 2005

Appeals Process Quarterly Report	Number Received	Upheld	Not Upheld
Stage 1 Appeal	1	0	0
Stage 2 Appeal	1	0	1
Pensions Ombudsman	0	0	0
Total	**1**	**0**	**1**

Appendix 5

The Minister for Local Government (Phil Woolas): My Statement to the House on 13 July made it clear that, taking account of costed assessments of the effect on the Local Government Pension Scheme (the LGPS) of reinstating the rule of 85 with effect from 1 April 2005, the Deputy Prime Minister would come forward with new regulations in the autumn to address the consequences for the Scheme in time for the provisions to be in place from April 2006.

Careful consideration has been given to the representations and specialist actuarial advice received from interested parties involved with the Scheme, and to the helpful discussions involving the key stakeholders within the framework of the LGPS Tripartite Committee. The estimates provided by LGPS administering authorities of the anticipated cost pressures arising from the decision to reinstate the rule of 85 in the Scheme with effect from 1 April 2005, have also been taken into account. Draft amending regulations will shortly be circulated for consultation to all LGPS interests in England and Wales and will be laid before Parliament in the New Year once they are finalised.

The combined scope of the consultation package and the subsequent regulations will secure the on-going solvency of the Scheme without any additional calls on central or local government budgets. This meets the Government's intention to secure the continued affordability and long term viability of the Scheme, and its acceptability to taxpayers.

Amending regulations, on which the necessary statutory consultation begins shortly, will directly contribute towards mitigating and managing the costs pressures arising from the decision to reinstate the rule of 85 in respect of pension liabilities accruing on the Scheme for the period 1 April 2005 until 30 September 2006. Other amendments, based on the responses received from a previous consultation exercise carried out over the summer, will further extend the existing flexibilities in the LGPS linked to the new tax regime for occupational pension Schemes already established by the Finance Act 2004.

Further Scheme amendments are also necessary to implement the terms of the European Employment Directive 2000/78/EC which establishes a general framework for equal treatment in employment and occupation. To give effect to the Directive and compliance with the timetable for associated Government legislation on age discrimination and employment law being introduced by DTI, the effective date for the removal of the rule of 85 from the LGPS will be 1 October 2006. Subject to the outcome of the proposed consultation exercise, it will be necessary to put in place appropriate safeguards, which can be objectively justified, for those LGPS members closest to retirement to take effect from the same date. The statutory consultation will provide a framework for discussion between the local authority employers and the trades unions in particular about the precise terms of these safeguards, and to explore how these may be associated both with the current proposed Scheme changes, and others which may be developed in the wider discussion about the future of the Scheme.

Balancing the scope of such safeguards with the opportunity to develop the longer term reform of equality proofed Scheme will form an integral part of the discussions and negotiations which the Tripartite Committee stakeholders have already agreed to undertake over the next six months. These will involve local authority employers, trades unions and other Scheme interests in a programme of discussion and analysis to modernise and reform the Scheme. These discussions will take account of wider pension policy developments, to ensure the LGPS can meet the challenges of a changing and flexible workforce, in and around local government, and deal effectively with the high incidence of part-time employees many of whom are female on lower incomes.

It is intended to consult widely on a policy discussion paper, about the proposed way forward for the LGPS in the Summer of 2006 for analysis and comment. This will allow a subsequent statutory consultation to begin later in the autumn of 2006, leading to new Scheme provisions for April 2007 with the ultimate objective of having a new-look LGPS in place for April 2008.

The continued affordability and viability of the Scheme, as well as its acceptability to taxpayers, remains a central theme of the Government's intentions for the LGPS. So too is our commitment towards ensuring the Scheme offers an equality proofed pension framework for all its increasingly diverse and part-time workforce. Delivering an effective and affordable balance between the cost of its provision to employers and tax payers on the one hand, and fairness to Scheme members on the other, remains a priority, within the overall resource framework of local government and of other employers within the Scheme. A flexible and attractive pension scheme for local government and employers associated with it is now required.

This Statement is in effect, the beginning of a series of detailed consultations with all LGPS interests about the future of the Scheme. Initially, the affordability of the existing LGPS must be established but, in doing that, it is essential to begin to move forward and begin to discuss and analyse the possible form and content of a new-look LGPS for 2008. All LGPS interests are committed to that intent and objective.

Appendix 6

OFFICE OF THE DEPUTY PRIME MINISTER

PARTIAL REGULATORY IMPACT ASSESSMENT (RIA)

LOCAL GOVERNMENT PENSION SCHEME (AMENDMENT) (NO.3) REGULATIONS 2005

Local Government and Firefighters' Pensions Schemes Division
ODPM
December 2005

PARTIAL REGULATORY IMPACT ASSESSMENT (RIA)

Title of Proposal

1. To consider measures for ensuring the ongoing solvency of the Local Government Pension Scheme (LGPS) following the revocation of the Local Government Pension Scheme (Amendment) (No.2) Regulations 2004 and the reinstatement of the 85 year rule in the LGPS.

Purpose and Intended Effect of Measure

<u>Objective</u>

2. Following the revocation of the Local Government Pension Scheme (Amendment) (No.2) Regulations 2004 the Deputy Prime Minister (DPM) invited representatives of the local government employers' and trades unions, in July 2005, to develop realistic and costed measures by the autumn, to <u>fully</u> meet the identified costs arising from the decision to revoke. The purpose of this Regulatory Impact Assessment is to consider the options for meeting the cost pressures.

<u>Background</u>

3. The Local Government Pension Scheme (Amendment) (No.2) Regulations were introduced in December 2004 and came into effect on 1 April 2005. They made two changes to the Scheme. The first ensured that the earliest age at which a pension could be paid, other than on grounds of ill-health, was increased from 50-55. The second phased out from the Scheme the rights of eligible members, who joined the Scheme before age 35-40, to receive an unreduced pension if they choose to retire before age 65. The LGPS already has a normal retirement age of 65. Transitional protection applied to Scheme members who were already 50 by 31 March 2005, and also to those who would reach their 60th birthday by 31 March 2013, with at least 25 years membership.

4. The Secretary of State, by means of the Local Government Pension Scheme Regulations 1997, requires local authority pension funds to carry out actuarial valuations every three years. The Amendment No.2

Regulations 2004 were introduced to ensure the Scheme complied with the Government's policy for a normal retirement age of 65 in public sector schemes and to positively influence the outcomes for employers of the expected increases in their contributions to arise from the 2004 valuation.

5. However, following the laying of the Amendment No.2 Regulations in December 2004, significant concerns were expressed by Members of Parliament, trades unions and scheme members. The DPM issued a statement on 18 March 2005 that he was minded to revoke the Local Government Pension Scheme (Amendment) (No.2) Regulations 2004, subject to statutory consultation, and with retrospective effect to 1 April 2005. The statement also announced that the DPM was establishing a Tripartite Committee, with key stakeholders, to consider what measures should be put in place to ensure the Scheme's affordability and sustainability for the longer term

6. Statutory consultation began on 1 April on draft proposed amending regulations which would have the effect of revoking the Amendment No.2 Regulations 2004, which themselves came into force that day. It was made clear, as part of the consultation material, that no new money from government or local authorities would be made available and that any savings foregone if revocation occurred would need to be found by other means.

7. The consultation closed on 31 May and the responses received were then considered. On 13 July a statement was made to the Houses of Parliament that the Amendment No.2 Regulations 2004 would be revoked with retrospective effect to 1 April. The Local Government Pension Scheme (Amendment) Regulations 2005 to achieve revocation were laid the same day and came into effect on 3 August 2005.

8. To fulfil his commitment that the costs of revocation would not fall on the taxpayer, representatives of the local government employers and trades unions were invited to develop realistic and costed measures by the autumn, to fully meet the identified costs arising from the decision to revoke. The framework provided by the LGPS Tripartite Committee would ensure effective and co-ordinated progress of the development of the Scheme.

9. To assist in that process and as a measure to ensure the continued stability of the Scheme, an amendment was also made by the Local Government Pension Scheme (Amendment) Regulations 2005 to provide each LGPS administering authority with the vires to request an interim valuation of their pension fund, as at 31 March 2005, so as to properly identify cost pressures resulting from the revocation.

10. Local Authorities are required, by the Local Government Pension Scheme Regulations 1997, to publish and maintain a Funding Strategy Statement. In light of the decision to reinstate the 85 year rule in the Scheme. Appropriate changes could be made to the pension funds' deficit recovery periods which could subsequently be taken into account by actuaries in the relevant actuarial cycle.

Meeting costs and the 85 year rule

11. The 85 year rule is a special provision within the LGPS which allows Scheme members to retire on a full pension, before the normal scheme retirement age of 65. Scheme members, aged 60 or over, can choose to retire on an unreduced pension where their age plus years of service equals 85 years. Scheme members aged 50 to 60, who also satisfy the rule, can retire with their employers consent.

12. The Council Directive 2000/78/EC establishes a general framework for equal treatment in employment and occupation. To comply with the Directive, the Department of Trade and Industry consulted on draft Employment Equality (Age) Regulations 2006. The consultation finished on 17 October and the regulations will come into force from 1 October 2006.

13. The Government has concluded that under this legislation the 85 year rule would be considered age discriminatory and therefore must be removed from the Scheme no later than 1 October 2006. This is because the 85 year rule takes the sum of the member's age and pensionable service to determine eligibility to pension benefit. If a member does not have sufficient age and pensionable service, they are not eligible for the benefit.

14. The following example may help: The members must be in comparable situations but for their age; one is 61 and the other 63; they both have 22 years service and wish to retire; the 63 year old would have no actuarial reduction in their pension as they satisfied the 85 year rule, whereas the 61 year old would have an actuarial reduction. The reason for the different pension entitlement is on the basis of age; therefore the rule is age discriminatory.

15. It may be possible to objectively justify the retention of the rule for Scheme members who are close to retirement, as it would not be easily possible for them to make alternative arrangements so close to their retirement.

16. Confirmation that the 85 year rule must be removed from the Scheme, by no later than 1 October 2006 will assist the Stakeholders in determining what the cost pressures are arising from the revocation, and how they should be met.

Transitional Protections

17. Consideration will need to be given to the cost of providing transitional protections for existing Scheme members close to retirement.

18. Transitional protections were originally provided in the Amendment No.2 Regulations 2004, for all Scheme members who would be aged 60, with 25 years service by 31 March 2013.

19. Had these protections not been provided then there would have been an additional saving of just over 0.5% of pensionable payroll, or £125 million, per year, for the 8 years - 2005 to 2013.[1]

20. So long as the cost of any transitional protections are no more expensive than those under the Amendment No2 Regulations 2004, then there should be no additional cost needing to be taken into account

Rationale for government intervention

21. The Secretary of State is responsible for the policy development and overall regulatory stewardship of the Scheme in England and Wales and, using the powers under the Superannuation Act 1972, sets the statutory framework within secondary legislation for the management, investment and administration of the Scheme.

22. It is generally understood, it being the Government's stated policy since July 2003 in respect of the LGPS, that one of the reasons the Scheme was initially amended on 1 April 2005 (by the LGPS (Amendment) (No.2) Regulations 2004) was to assist in reducing employers' cost pressures and to mitigate the anticipated rate of employers' contribution increases as a result of the 2004 valuations. At that time, the "savings" were estimated between £200-400 million per annum.

23. Following an updated assessment of the LGPS 2004 valuation reports the Government Actuary's Department (GAD) concluded that the costs across all LGPS employers was about £400 million in 2005/06. For local authorities, i.e. those employers with precepting/revenue raising powers, a broad estimate suggests that their costs for 2005/06 fall in the range of £300-350 million.

24. Revocation of the Amendment No.2 Regulations 2004 means that the cost pressures the changes were intended to relieve remain to be faced. For there to be no additional costs from the revocation falling on government, local authorities or taxpayers, the government must introduce further regulations dealing with these cost pressures to ensure the ongoing solvency of the Scheme and to provide certainty for local authorities' finances generally.

25. Ministers are committed to providing stable and attractive benefits to current and future Scheme members. It is imperative, therefore, for the Scheme's affordability and sustainability that the effects of revocation are managed prudently, and so help to ensure its ongoing solvency.

26. Representatives of the local authority employers and trades unions were invited to come forward with proposals to fully meet the cost pressures arising from the decision to revoke, to allow all parties to give further consideration to the issues facing the LGPS.

27. However, it was made clear that if the employers and the unions were unable to agree a fully costed proposal for the way forward, then a

decision would still be required on what amendments were necessary to ensure the Scheme's viability and effect on taxpayers.

Consultation

Within government

Government Actuary's Department

Scottish Public Pensions Agency

HM Treasury

Public consultation

Local Government Association (LGA)

Employers' Organisation and through it other Scheme employers

Local Authorities in England and Wales

Association of Consulting Actuaries (ACA)

UNISON

GMB

Amicus

Transport and General Workers Union (TGWU)

Union of Construction, Allied Trades and Technicians (UCATT)

National Association of Probation Officers (NAPO)

Community and Youth Workers Union (CYWU)

Information to assist in the development of proposals

30. There were four discrete, but linked events, programmed to assist in meeting the objective of providing properly costed proposals:

a) LGPS funds to provide funding updates by 30 September 2005;

b) data gathering exercise organised by the Employers' Organisation to consider the relationship between the retirement age of members in the Scheme and satisfying the rule of 85

c) commissioning by ODPM of an actuarial longevity study of the LGPS in England and Wales;

and

d) administering authorities agreeing to provide copies of the 2004 valuation reports to trades unions and their actuarial advisor.

Powers to allow an interim actuarial valuation of funds

31. The issues surrounding the estimates of the cost of revocation are complex and depend upon a range of assumptions being applied to cover a wide variety of individual Scheme member's circumstances, including their retirement decisions, socio-economic factors, and even their health.

32. The interim actuarial valuation of funds in England and Wales identified the one year cost of revoking the 85 year rule as £435 million for 2005/06.

33. After making an allowance for the possible beneficial effect of late retirees, the Government Actuary's Department (GAD) and the actuaries advising the LGA and its constituent employers, suggested a reasonable range for the likely total cost of revocation would be between 80-90% of the total £435 million cost. In monetary terms this is around £340-390 million[2], of which £280-315 is estimated to relate only to local authorities in the Scheme in England and Wales.

34. If the 85 year rule is not removed until 1 October 2006, then the cost of revocation, for the 18 month period 1 April 2005 to 1 October 2006, based on the same assumptions as above, is in the range of £520-590 million.

35. A further option is if the 85 year rule is removed for new members from April 2006 and for existing Scheme members as at 31 March 2006, from 1 October 2006. Advice from GAD is that this would reduce liabilities in 2006/07 by £5-10 million. However, savings would be very dependent on turnover and the number/profile of new joiners.

36. The trades unions believe the total Scheme cost of revocation, for local authorities, falls between £225-275 million.

37. In light of the government's commitment that the cost of revocation should not fall on central government or the council tax payer, and that regulations to meet the cost pressures would be forthcoming, many local authorities decided not to commission a revised rates and adjustments certificate at this time, and to maintain their existing levels of employer contribution rates.

Data gathering exercise organised by the Employers' Organisation (EO)

38. The EO gathered information from local authorities on:

a) the average age of retirement of all LGPS pensioners broken down by employer type and gender (male/female)

b) the average retirement age of all LGPS pensioners retiring in the year to 31st March 2005 broken down by employer type and gender (male/female)

c) the average pension for all LGPS pensioners broken down by employer type, by gender (male/female), and by type of pension

d) the average pension, and the average service and average pay on which the pensions were calculated, for all pensioners retiring in the year to 31st March 2005 broken down by employer type, by gender (male/female), and by type of pension.

39. Detailed scheme data was passed from the EO to the unions on 23 September. An updated version was then sent on 29 September.

40. It was not possible for data to be gathered on the amount of time employees worked past their Earliest Retirement Age[3] as this date was not calculated and stored by the computer programme software used.

Commissioning of the demographic study of the LGPS in England and Wales

41. The actuarial firm Hymans Robertson LLP was commissioned to produce an actuarial longevity study of the LGPS in England and Wales. Their report, Local Government Pension Scheme in England and Wales: Review of Demographic Patterns, September 2005, was based on terms of reference and key questions agreed between ODPM, the Employers' Organisation and the trades unions at the second Tripartite Committee on 30 June 2005.

42. The principal purpose of the report was to provide all the Tripartite Committee Stakeholders with statistical information on the demographics of the scheme membership. This covered three broad areas:

a) the profile of employee members and pensions in payment,

b) the retirement behaviour of employees, and

c) the mortality experience of pensions in payment.

43. In summary the main findings of the report were as follows:

w That the membership of the LGPS had changed significantly both since the Scheme was originally implemented in 1922, and when the existing benefit structure was introduced in the early 1970's. This had become particularly apparent since all part-timers were allowed to join in 1993.

w 72% of the current employee membership is female, with 57% of female workers working part-time. Almost half the employee members work part-time.

w 75% of pensions in payment are less than £5,000 a year. Women tend to be in receipt of lower pensions than men, primarily due to shorter service and lower pay.

w For members retiring in the LGPS between 2001 and 2004, almost 90% of men and two-thirds of women would have been able to retire on an unreduced pension at age 60, under the 85 year rule - their Earliest Retirement Age (ERA).

w Women's ERAs are generally later than men's, due to their joining later than average.

w Around 15% of all retirements are Scheme members who have worked past their ERA. These are known as 'late' retirements. Of these late retirements, men are more likely to continue in employment beyond their ERA than women. The average period of working late was around three years for both men and women.

w Individuals with larger pensions tend to retire sooner than those with smaller pensions, often on redundancy grounds or in the interests of efficiency.

w Life expectancy at birth is increasing, but is not directly relevant in the context of pension scheme funding, where the expectation of life from retirement age is most important.

w Statistics confirmed that the UK population generally, and the LGPS population specifically, are showing reductions in mortality rates, implying material increases in the average period that pensions are in payment, compared to when the scheme rules were devised..

w For men retiring at 65, based simply on population mortality, the average period that a pension is expected to be in payment has risen from 12.2 years to 16.0 years since the early 1970's, an increase of some 31%. For women, the rise is from 16.1 years to 19.0 years, a rise of some 18%.

w Pensioners who retire from the LGPS in normal health would be expected, on average, to live around 2 to 4 years longer than pensioners in the population as a whole.

44. In conclusion Hymans summarised that there appeared to be a strong case for the benefit structure evolving, just as the population that it is designed to cater for is evolving. Increased longevity and a substantially increasing pensioner population (compared to working population) means retaining older workers in employment would become increasingly important.

45. Hymans report also provided further justification for the removal of the 85 year rule on discrimination grounds, as it showed that the rule is indirectly discriminatory towards women. This is because although they make up the majority of the workforce, on average, they have less service in local government than men, as a result of joining later if life, and therefore are less likely to be in a position to benefit from the rule.

Administering authorities provide copies of 2004 actuarial valuation reports

46. A first batch of these reports was passed to the trades unions, by the EO, in July 2005. A further batch, making a complete set, was handed over by the EO in September for analysis.

47. In addition to this the trades unions requested information direct from Local Authorities under the Freedom of Information Act 2000.

Options

48. Three options have been identified:

A) Do nothing

B) Increase tax-free lump sum

C) Increase employee contributions

Option A - Do nothing

49. It was made clear, as part of the consultation material on regulations to revoke the Amendment No.2 Regulations 2004, that any savings foregone through revocation would need to be found by other means. No new money from government or local authorities would be made available.

50. As the Amendment Regulations 2005 allowed for the taking place of interim valuations, it could be the case that the revised certificate will show that due to investments performing better than expected, the suspected cost of revocation has been mitigated.

51. However, relying on the increased performance of investments would not be prudent, as investments can go down as well as up and any improvements in investments could easily be offset by a reduction in bond yields, or vice versa.

52. Furthermore, the Government made a clear commitment to Parliament that further regulations will be introduced to ensure the cost pressures arising from the revocation are met. Relying on increased performance of investments would not ensure the costs have been met in the long term, and therefore would not meet the Government's commitment to Parliament.

Option B - Increase tax-free lump sum

53. Scheme members currently receive 3 times the amount of their final pension as a tax-free lump sum when they retire.

54. From 6 April 2006, HM Revenue and Customs (HMRC) tax simplification will permit Scheme members to take up to 25% of the capital value of the pension as a tax-free lump sum, when they retire.[4]

55. Where Scheme members chose to take more, any increase, above the three times amount currently provided for, would be paid for by the Scheme member commuting part of their final pension, e.g. swapping pension for tax-free cash at a commutation rate of 12:1. This means for every £1 of pension foregone they would receive £12 tax-free cash.

56. This could be popular with members and at the same time reduce employers' liabilities. The attached spouse's pension would be unaffected as only part of the member's pension would be surrendered.

Option C - Increase employee contributions

57. Scheme members, post 1998, currently pay a 6% contribution towards their pension fund. A small number of manual workers who were members of the Scheme prior to 1988 pay 5%.

58. One option for meeting the cost pressures arising from the Scheme is to increase all Scheme member contributions by 1%.

59. This could have a knock-on effect of increased pay demands from local government workers, possibly discourage Scheme membership take-up (particularly the part-time) and possibly lead to existing members opting out.

<u>Alternative options considered</u>

Binding pay deals

60. This would prevent high pay increases which place pressure on the pension fund. A variation of this would be the option to control or reduce the amount of pay which is pensionable. Pay rises could also be negotiated separately from pensionable pay rises, so that, for example, pensionable pay might rise each year by 1% less than actual pay.

61. The impact of introducing binding pay restraints, or a variation thereof, would depend on when this was introduced and for how long. It is almost inevitable that there would be catch-up in the future and so any saving would be unlikely to be realised in the long term, although future catch-up could not be backdated.

62. This option was rejected as the potential long term benefits could not be guaranteed.

Move to Career Average Re-valued Earnings (CARE) Scheme

63. A CARE scheme could help control future cost volatility and can be designed to deliver broadly the same expected employer cost as a final salary scheme, but with a lower member contribution rate. The saving arises from the difference in the expected rate or revaluation of each year's benefits. This could be more attractive than final salary designs to those with modest pay growth expectations.

64. One possible variation on this option is that CARE could be offered as the default options for certain groups of staff e.g. part-timers or those

whose earnings were below a certain level. All members could be allowed to opt into the other design (i.e. from CARE to final salary and vice versa) at the start of their career and possibly at points in the future (for subsequent benefit accrual).

65. A CARE scheme would reduce the risk of future cost volatility due to pay settlements and is potentially cheaper to administer in the long term. It could provide better pension for low paid/part-time workers and more accurately reflect the needs of the local government workforce (as identified in the Review of Demographic Patterns report, by Hymans Robertson). It is not known what accrual and revaluation rates would be acceptable to trades unions. It could also exacerbate work place tensions as it would require a cultural shift from the perceived "gold standard" of the final salary pension Scheme.

66. This option was rejected as it would require a major change to the Scheme which would not be possible by the autumn. It is likely to be considered further in discussions on the long term reform of the Scheme.

Change to ill-health/early retirement packages

67. Current practice permits local authorities to enhance a Scheme member's pension, up to a maximum 40 years, where they retire early or under ill-health grounds. Savings could be achieved by amending the amount local authorities can enhance by, or criteria by which they set their standard. This could result in better pension provision for those permanently retired on ill-health grounds

68. For ill-health retirements, a two tier system could be introduced for Scheme members who are able to work again but not necessarily in their previous local government post. This could reduce instances of Scheme members retiring on ill-health grounds and then returning to work in another area (not local government) whilst still receiving a full occupational pension from local government. It would also reduce the long term liabilities facing the Scheme by reducing the number of fully enhanced ill-health/early retirement cases.

69. This option was rejected as it would require a major change to the Scheme which would not be possible by the autumn. It is likely to be considered further in discussions on the long term reform of the Scheme.

Incentives to remain in employment

70. The later members delay their retirement beyond the earliest age from which they can take their benefits unreduced (and as of right), the greater the cost saving to the Scheme. Care would be needed in designing the benefits being offered to members to delay their retirement, so they do not fall under the preservation requirements or fall foul of age discrimination.

71. The wider picture also needs to be taken into account. Encouraging scheme members to remain in employment will become increasingly important as the ratio of working age population to pensioner population

decreases in the coming years (as identified in the Review of Demographic Patterns report, by Hymans Robertson).

72. This option was rejected as it would require a major change to the Scheme which would not be possible by the autumn. It is likely to be considered further in discussions on the long term reform of the Scheme.

Costs and Benefits

Sectors and groups affected

73. There are currently 1.5 million active Scheme members who could be affected by any amendments to the LGPS benefit structure.

Race equality assessment

74. There are no race equality issues concerning our proposals

Health impact assessment

75. The Normal Retirement Age for the LGPS is 65. However, the 85 year rule enables Scheme members satisfying the rule to retire on an unreduced pension from age 60, or from age 50 with employer's consent. The trades unions and some actuaries have expressed concern that there may be more instances of ill-health retirement if the 85 year rule is removed from the Scheme and local employees have to work longer. No evidence has been supplied, at this stage, to support this opinion. If the 85 year rule is removed from the Scheme any increase in ill-health retirements will become apparent at the tri-annual actuarial valuations of the funds.

76. It is intended that flexible retirement provisions, as introduced by Finance Act 2004, which will be permissible from 6 April 2006 may mitigate this risk. Flexible retirement, will allow Scheme members to continue working at reduced hours/grade, and accruing pension benefit whilst starting to draw part of their pension. This will remove the current cliff edge where a Scheme member retires from work overnight.

Rural considerations

77. In their report, Review of Demographic Patterns (as referred to in paragraphs 41 to 45), Hymans Robertson looked at longevity figures in the LGPS and analysed the mortality experience for their England and Wales LGPS client funds over the three years from 2001-2004. A subset of the pensioner data they considered, for officers retiring other than through ill-health, related to regional variation.

78. The results of this analysis showed that the North-South[5] gap in mortality figures was slightly less pronounced than Urban-Rural[6] differences. The gap between London and the rest of the South was the most significant. Overall these figures showed that those in Rural areas were living, on average, 1.5 years longer than those in Urban areas. This means that increased longevity will have a greater impact on cost pressures facing the LGPS Rural funds than it will for Urban funds.

Breakdown of costs and benefits

79. For all stakeholders it was imperative there was an evidential base for the costs and benefits of the proposals. Various initiatives to determine the evidential base were undertaken by the stakeholders (as referred to in paragraphs 30 to 47). The following costings have been agreed by GAD.

Option A - Do nothing

Economic

80. Benefits - None

81. Costs - As referred to in paragraphs 33 and 34 the one year cost (2005/06) of reinstating the rule of 85 is in the range of £340-390 million. The 18 month cost (1 April 2005 to 1 October 2006) is in the range of 520-590 million. In the longer term the retention of such a rule would cost the scheme some 2% -2.5% of pay per year.

Environmental

82. There are no environmental benefits or costs to this proposal.

Social

83. Benefits - The trades unions and many Scheme members may welcome maintaining the status quo and not making changes to the Scheme for current members.

84. Costs - Not taking any action to mitigate the current cost pressures facing the Scheme is likely to be criticised by local authorities and taxpayers generally. Furthermore, not taking the cost pressures facing the Scheme into account now could jeopardise the long term future of the Scheme. The Government has a statutory obligation to ensure the Scheme's affordability, viability and acceptability, and to have regard to issues of fairness in the balance between taxpayers and members benefits.

Option B - Increase tax-free lump sum

Economic

85. Benefits - Certain assumptions have to be made in relation to this proposal. For example take-up rate and commutation rate all have to be assumed by the actuaries, when establishing whether this would be a cost or a benefit to the Scheme. GAD have advised that based on a 50% take up rate[7] and a commutation rate of 12:1[8] a saving to the Scheme of around 0.3% of payroll, or £75 million, could be assumed.[9]

86. Costs - Potential loss of revenue for the exchequer as the lump sum is tax-free. Increasing the amount of lump-sum taken, above the 3 times pension automatically provided, also reduces the overall pension in payment liability to tax. It may also mean that some scheme members,

who take an increased lump sum, would find they are now entitled to pension credit, due to the reduction in overall pension.

Environmental Benefits/Costs

87. There are no environmental benefits or costs to this proposal.

Social

88. Benefits - Allow scheme members more access to ready cash which is likely to be welcomed by the Scheme member.

89. Costs - As scheme members would have to commute any amount above the current 3/80ths permitted, if they wished to draw more of their pension as tax-free lump sum, then Scheme members will need to obtain professional advice on the best course of action for them, based on their own personal circumstances, before reaching a decision.

Option C - Increase employee contributions

Economic

90. Benefits - A 1% increase in employee contributions over the two years 2006/07 and 2007/08 might provide an extra £250 million per year.[10] If the cost pressures arising from the reinstatement of the 85 year rule are spread in line with the current recovery periods as set out in LGPS Funding Strategy Statements then this would cover the cost for 2005/06.[11]

91. Costs - An increase in the employee contribution rate could call for increased pay demands, which could ultimately mean the cost pressures falling on local authority employers. Furthermore the increase in the contribution rate only recoups the cost if the 85 year rule is removed from April 2006. It would not cover the extra cost incurred between April and October 2006, if the rule is not removed until 1 October 2006.

Environmental

92. There are no environmental benefits or costs to this proposal

Social Benefits

93. Benefits - None

94. Costs - The increase may be seen as poorly targeted as it would affect all Scheme members, not just those entitled to retire under the 85 year rule. Therefore some Scheme members would be paying for a benefit that they would not be able to receive. The increase could also result in a lower take-up of the Scheme at a time when measures to increase member take-up are being considered.

Small Firms' Impact Test (SFIT)

95. As the proposals relate to and affect only the public sector, there is no need to consult business because there can be no impact.

Competition Assessment

96. This is not required for these proposals.

Enforcement, Sanctions and Monitoring
Enforcement

97. This is not required for these proposals.

Sanctions

98. This is not required for these proposals.

Monitoring and review

99. All LGPS funds undergo an actuarial valuation every three years. The last valuation took place in March 2004 and therefore the next will take place in March 2007. LGPS administering authorities' pension funds and their actuarial context are both separately monitored regularly by investment consultants and actuaries. In addition, Funding Strategy Statements are required to be regularly reviews and to provide a statutory framework for the relevant actuarial valuation exercise.

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[1] This is based on an estimated pensionable payroll figure of £25 billion for 2004/05, which was based on pay trends for the previous 3 years.

[2] This is based on an estimated pensionable payroll figure of £25 billion for 2004/05, which was based on pay trends for the previous 3 years.

[3] Earliest Retirement Age (ERA) - This is the earliest age at which an employee can retire based on their 85 year rule entitlement. For example, a Scheme member has worked in local government and contributed to the LGPS for 22 years by their 63rd birthday has an ERA of the date of their 63rd birthday, rather than the normal retirement age for the LGPS which is 65.

[4] The current 3 times final pension permitted in the LGPS equates to roughly 15% of the capital value, using the HMRC stipulated conversion factor of multiplying annual pension by 20.

[5] Broadly speaking anything south of the M4 was considered south, with anything above being considered north. South excluded London, which was considered separately.

[6] County Councils were labelled "rural" and Metropolitan Funds were labelled "Urban"

[7] Take up rate - GAD have assumed that 50% of Scheme members will take an increased lump sum up to a maximum 25% and 50% of Scheme members will take only the 3 times final pension salary.

[8] 12:1 Commutation rate means for every £1 of pension foregone the Scheme member will receive £12 of tax-free lump sum.

[9] This is based on an estimated pensionable payroll figure of £25 billion for 2004/05, which was based on pay trends for the previous 3 years. The 0.3% saving relates to new entrants' future service.

[10]This is based on an estimated pensionable payroll figure of £25 billion for 2004/05, which was based on pay trends for the previous 3 years.

[11] In the knowledge that the average spread period for managing deficits is some 20 years, this means that £35 million per year has to be managed by each fund, which is equivalent to 0.1% of payroll. This is based on an estimated pensionable payroll figure of £25 billion for 2004/05, which was based on pay trends for the previous 3 years.

APPENDIX 1

TOP TEN SHARES HELD

	As at 30 September 2005			As at 30 September 2004		
Shares	**Rank**	**Percentage of Fund**	**Market Value**	**Rank**	**Percentage of Fund**	**Market Value**
		%	**£'000**		**%**	**£'000**
1. Vodafone	1	4.1	15,113	1	4.2	12,490
2. Royal Bank of Scotland	2	2.8	10,471	2	2.6	7,745
3. Shell	3	2.8	10,233	6	2.3	6,921
4. HBOS	4	2.6	9,633	4	2.4	7,183
5. BP	5	2.6	9,424	5	2.3	6,924
6. Astrazeneca	6	2.5	9,204	3	2.5	7,512
7. Barclays	7	1.5	5,652	10	1.4	4,163
8. HSBC	8	1.4	5,298	7	1.8	5,332
9. Lloyds TSB	9	1.2	4,553	9	1.5	4,346
10. Glaxosmithkline	10	1.2	4,474	8	1.6	4,778

FUND HOLDINGS

	As at 30 September 2005		As at 30 September 2004	
Fund Holdings	**Percentage of Fund**	**Market Value**	**Percentage of Fund**	**Market Value**
	%	**£'000**	**%**	**£'000**
UK equities	43.5	221,461	43.8	181,914
Overseas equities	29.5	150,257	28.1	116,851
UK fixed interest bonds	12.5	63,721	13.0	54,044
Overseas fixed interest bonds	3.3	16,604	4.2	17,435
Cash	1.3	6,448	1.9	7,528
Index-linked securities	4.6	23,296	4.3	17,905
Property	5.3	26,938	4.7	19,473
Totals	**100.0**	**508,725**	**100.0**	**415,150**

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APPENDIX 2

FUND PERFORMANCE TO 30 SEPTEMBER 2005

GROSS OF FEES

	Market valuations 31.03.03	Market valuations 31.03.05	Market valuations 30.09.05	Weighted % Fund change 1 July to 30 September	% benchmark change 1 July to 30 September	% target 1 July to 30 September	**Under (-)/over (+) performance versus target 1 July to 30 September**	Annualised weighted % Fund change 1 April 2003 to 30 September 2005	Annualised % benchmark change 1 April 2003 to 30 September 2005	Annualised % target 1 April 2003 to 30 June 2005	**Annualised under (-)/over (+) performance versus target 1 April 2003 to 30 September 2005**
	£'000	£'000	£'000	%	%	%	**%**	%	%	%	**%**
Bernstein	57,182	93,217	105,067	8.19	8.16	8.66	**(0.47)**	24.49	24.21	26.21	**(1.72)**
Capital	92,282	127,900	140,145	5.08	6.08	6.45	**(1.37)**	16.77	17.47	18.97	**(2.20)**
Fidelity	93,294	119,536	133,643	5.56	5.01	5.38	**0.18**	15.22	14.96	16.36	**(1.14)**
ING	5,432	26,534	28,823	4.51	4.60	4.78	**(0.27)**	17.08	16.33	17.03	**0.05**
Wellington	61,019	85,777	100,884	9.63	10.27	10.57	**(0.94)**	22.28	23.92	25.92	**(3.64)**
Not allocated	15,455	1,338	162								
Totals	**324,664**	**454,302**	**508,724**	**6.68**	**6.89**	**7.30**	**(0.62)**	**18.72**	**19.20**	**20.85**	**(2.13)**

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APPENDIX 3

PENSIONS FUND

BUDGET MONITORING - PERIOD 9 (END OF DECEMBER) 2005/06

	2005/06 Budget £'000	Plan to period 9 £'000	Actual to period 9 £'000	Over/under (-) £'000	Explanations of variations
Income					
Contributions and benefits:					
Employee Contributions	(7,400)	(5,550)	(5,799)	(249)	
Employer Contributions	(22,000)	(16,500)	(18,986)	(2,486)	Increase in Employer contribution rates and membership of fund
Transfer Values Received	(6,000)	(4,500)	(4,026)	474	Volume and timing varies
Total income	**(35,400)**	**(26,550)**	**(28,811)**	**(2,261)**	
Expenditure:					
Pensions and other benefits	20,100	15,075	15,444	369	
Lump sums	2,500	1,875	1,639	(236)	Difficult to estimate
Transfer values paid	6,000	4,500	3,201	(1,299)	Volume and timing varies
Refunds on contributions	100	75	95	20	
Administrative expenses	700	525	493	(32)	
Total expenditure	**29,400**	**22,050**	**20,872**	**(1,178)**	
Net addition from dealings with members	**(6,000)**	**(4,500)**	**(7,939)**	**(3,439)**	
Returns on Investment:					
Investment income	(13,000)	(9,750)	(11,039)	(1,289)	Difficult to estimate
Investment management expenses	1,400	1,050	541	(509)	Timing of receipt of Fund Managers invoices
Investment administration expenses	600	450	276	(174)	Timing of receipt of Fund Managers invoices
Net return on investments	**(11,000)**	**(8,250)**	**(10,222)**	**(1,972)**	

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