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pay, pensions and
employment solutions

The Local Government Pensions Committee
Secretary: Terry Edwards

CIRCULAR

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No. 199 – MAY 2007

AMENDMENTS TO THE CURRENT LOCAL GOVERNMENT PENSION SCHEME IN ENGLAND AND WALES

Purpose of this Circular

1. This Circular has been issued to bring to the attention of authorities in England and Wales recent changes that have been made to the Local Government Pension Scheme.

Background

2. The Local Government Pension Scheme (Amendment) (No. 2) Regulations 2007 [SI 2007/1488] were issued under cover of a Communities and Local Government (CLG) letter dated 25th May 2007 and make various amendments to the Local Government Pension Scheme in England and Wales.
3. Most of the amendments made by the above regulations have previously been the subject of draft regulations which CLG issued for consultation on 3rd November 2006 and 1st January 2007. The majority, but not all, of the Scheme amendments arise from changes in the tax regime governing pension schemes (as introduced by the Finance Act 2004).
4. The Amendment Regulations come into force on 21st June 2007 but many of the amendment have retrospective effect as highlighted in the relevant sections below.

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Managing Director Jan Parkinson

Key provisions of the Local Government Pension Scheme (Amendment) (No. 2) Regulations 2007 [SI 2007/1488]

5. The main changes made by the Amendment Regulations are set out below:

Active membership – age 75

Employees will not be able to be an active member of the Scheme on or after the day before their 75th birthday. This is to ensure that they will be a pensioner, not an active member, on the day before their birthday. This is so that pension benefits can be paid on the day before their 75th birthday and that the payments are thus authorised benefit payments under the terms of the Finance Act 2004

This change is retrospective to 6th April 2006.

Ill health enhancement not limited to 40 years membership

The amount of ill health enhancement that can be awarded following ill health retirement is no longer to be restricted by an overall maximum membership period of 40 years. Previously, an ill health benefit would have been calculated based on the following:

<u>Accrued Membership</u>	<u>Total Membership after Ill Health Increase Awarded</u>
Less than 5 years	Actual membership only
5 but less than 10 years	Membership doubled
10 yrs to 13 yrs 122 days	Membership increased to 20 years
13 yrs 123 days to 33 yrs 122 days	Membership increased by 6 yrs 243 days
33 yrs 123 days but less than 40 years	Membership increased to 40 years
40 or more years	Actual membership only

The increased membership could not exceed the total membership the person could have accrued had they continued in employment until age 65 (or, in the case of Coroners, until age 70).

The removal of the 40 year limit means that an ill health benefit will now be calculated based on the following¹:

<u>Accrued Membership</u>	<u>Total Membership after Ill Health Increase Awarded</u>
Less than 5 years	Actual membership only
5 but less than 10 years	Membership doubled
10 yrs to 13 yrs 122 days	Membership increased to 20 years
13 yrs 123 days or more	Membership increased by 6 yrs 243 days

The increased membership cannot exceed the total membership the person could have accrued had they continued in employment until age 65 (or, in the case of Coroners, until age 70).

The removal of the 40 year limit is retrospective to 6th April 2006 and so administering authorities will need to recalculate the benefits for any Scheme member who retired on or after that date (and before age 65) with an ill health pension and who either:

- a) already had 40 years membership (and so received no ill health enhancement), or
- b) had more than 33 years 122 days but less than 40 years membership and whose enhanced benefit was limited to 40 years membership

Flexible retirement – how membership counts in the continuing employment

Where a Scheme member, with the employer's consent, takes flexible retirement, the membership accrued up to the date of flexible retirement will count as "qualifying service" in the continuing employment. In other words, it will count for the purpose of determining whether or not the member, in that continuing employment, has:

¹ For part-time employees, the period of extra membership is scaled down in proportion to the whole-time equivalent. Similarly, where an employee's membership consists of a mixture of whole-time and part-time employment, the period of extra membership is adjusted to reflect the employee's historic work pattern (but not if the total membership includes at least 13 1/3 years of whole-time employment) but the adjustment must not produce benefits less than those that would have been paid based solely on the period of whole time employment (i.e. ignoring the part time employment). No enhancement is granted if the person has previously been awarded an ill health pension under the Scheme.

- a) the 3 months membership necessary to qualify for a benefit when they finally leave the ongoing employment, and
- b) the 5 years membership necessary to qualify for an enhanced ill health pension, should they cease the ongoing employment on the grounds of permanent ill health

The membership accrued up to the date of flexible retirement will not, however, count towards the 85 year rule in the continuing employment. This will be a major issue for those members wishing to make use of flexible retirement who would have satisfied the 85 year rule before age 65. This is because, following flexible retirement, the benefits from the continuing employment will be subject to an actuarial reduction if drawn before age 65 whereas, if the member had not taken flexible retirement, none of the benefits (when paid) would have been subject to an actuarial reduction (or, if drawn before the 85 year rule was met, would have been subject to a smaller actuarial reduction based on the shortfall to the 85 year rule being met, rather than the shortfall to age 65).

This change is retrospective to 6th April 2006.

No death grant on death after age 75

If a member dies on or after his / her 75th birthday, no death grant can now be paid. This change is retrospective to 6th April 2006. The Statutory Instrument does not contain an opt out clause to cover any cases where an administering authority has already paid a death grant in respect of a person aged 75 or over who died on or after 6th April 2006. However, section 12(4) of the Superannuation Act 1972 is overriding and says "No provision shall be made by any regulations unless any person who is placed in a worse position than he would have been in if the provision had not applied in relation to any pension which is being paid or may become payable to him is by the regulations given an opportunity to elect that the provision shall not so apply in relation to that pension".

Any death grant paid by an administering authority since 6th April 2006 in respect of a member who at the date of death was aged 75 or over would have to be reported to HMRC (as, for HMRC purposes, it would constitute an unauthorised payment).

Commutation of small pensions

Amendments have been made to regulation 49 of the LGPS Regulations 1997 which provides that small pensions can be commuted into a one off lump sum payment. The amendments to regulation 49 are retrospective to 6th April 2007. Regulation 49(1) now provides that a lump sum which is a trivial commutation lump sum within the meaning of section 166 of the Finance Act 2004 or a trivial commutation lump sum death benefit within

the meaning of section 168 of that Act may be paid in accordance with the rules² relating to the payment of such benefits under the Finance Act 2004.

The LGPC Secretariat believes that, as the Amendment Regulations delete regulation 49(5) of the 1997 Regulations, the words “and the amount shall be calculated in accordance with guidance issued by the Government Actuary” should be added to the end of regulation 49(1). This is necessary because the Finance Act 2004 does not specify how much the commutation payment should be.

Commutation in exceptional ill health cases

A corrective amendment has been made to regulation 50(1), effective from 6th April 2007, to clarify that the whole of a member’s pension, not just that element in excess of the member’s Guaranteed Minimum Pension (if any) can be commuted on the grounds of serious ill health (where the member has life expectancy of less than one year). The

Increase in amount of augmented membership an employer may award

The maximum period an employer may grant to an active scheme member as augmented membership under regulation 52 of the LGPS regulations 1997 has been increased from the shorter of:

- a) 6 years 243 days, or
- b) the period by which the member’s total membership falls short of the total membership he / she would have had had he / she continued as an active member until age 65

to the shorter of:

- a) 10 years, or
- b) the period by which the member’s total membership falls short of the total membership he / she would have had had he / she continued as an active member until age 65

The increase in (a) to 10 years matches the maximum period that employers used to be able to award as Compensatory Added Years under the Local Government (Early Termination of Employment) (Discretionary Compensation) (England and Wales) Regulations 2000 to employees who were retired on the grounds of redundancy or efficiency of the service when aged 50 or over with 5 or more years membership.

It should be noted, however, that where more than 6 years 243 days CAY were awarded under those Regulations, 30% of any redundancy payment was clawed back for each year and part year awarded above 6 years 243

² The commutation rules are covered in more detail in the Tax Guide at <http://www.lge.gov.uk/lge/core/page.do?pageld=59075>

days. Thus, where 10 CAY were awarded, all the redundancy payment was clawed back. There is no equivalent statutory provision to claw back redundancy pay if an authority decides to augment membership under regulation 52 of the LGPS Regulations 1997 by more than 6 years 243 days.

Although the amendment that increases the maximum award of augmented membership under the LGPS from 6 years 243 days to 10 years is retrospective to 1st April 2007, employers can only make an award to active Scheme members (not to Scheme members who have already left with a pension or a deferred pension).

Elections to pay AVCs

As foreshadowed in the draft regulations issued for consultation by CLG last year, the Amendment Regulations have been changed to limit the amount of Additional Voluntary Contributions (AVCs) that a Scheme member may pay to a maximum of 50% of remuneration. A member who holds more than one pensionable employment may pay AVCs in each employment but is limited in each one to a maximum of 50% of remuneration from that employment.

The regulations now require that AVC contributions have to be deducted from pay. This, for example, would preclude members from paying a cheque over in the last week of the financial year (after the final payroll had been run).

The change comes into effect on 21st June 2007 and is retrospective to 6th April 2007. The policy intention is that the change should apply to all members, irrespective of when they started paying AVCs. Unfortunately, the regulatory amendments, as presently worded, do not seem to quite deliver the policy intention. This is because new regulation 60(2B) has introduced a limit for new elections but does not appear to cover elections that had already been made (prior to 6th April 2007). Equally, regulation 60(8), which permits a member to vary their contributions, does not contain a 50% limit – so a person could apparently make an election to pay up to 50% and then subsequently vary the election to pay more than 50%. This is clearly not the policy intent. The advice is that authorities should comply with the policy intent and limit the maximum AVCs from 2007/08 onwards to a maximum of 50% of remuneration. This will avoid any potential embarrassment should any further retrospective amendments be made to ensure the policy intent is delivered. Any payments in excess of 50% made in the 2006/07 or earlier tax years are unaffected and no adjustments are necessary in respect of them. However, any payment in excess of 50% of pay already made in April and May 2007 should be dealt with by an adjustment in subsequent months. The Statutory Instrument does not contain an opt out clause to cover any cases where a member has paid AVCs of more than 50% of remuneration since 6th April 2007 and leaves before the amending regulations come into force on 21st June 2007. However, section 12(4) of the Superannuation Act 1972 is overriding and

so such leavers are covered by that section. It says "No provision shall be made by any regulations unless any person who is placed in a worse position than he would have been in if the provision had not applied in relation to any pension which is being paid or may become payable to him is by the regulations given an opportunity to elect that the provision shall not so apply in relation to that pension".

6. The Amendment Regulations make a number of other minor changes which serve to clarify the meaning of certain regulations and to delete some obsolete cross-references.
7. They also make two corrections to the Local Government Pension Scheme (Benefits, Membership and Contributions) Regulations 2007 [SI 2007/1166] thereby ensuring that, under the new-look LGPS from April 2008:
 - a) benefits can be calculated on the best one of the last 3 years pensionable pay (and not, as would have applied prior to the amendment, just the last years pay), and
 - b) all members (not just whole-time members) whose post is downgraded or who voluntarily downgrade (other than as a result of flexible retirement) can, if they wish, choose to have benefits based on the average of any 3 consecutive years in the last 10 (ending on a 31st March).

Where final pay from a year earlier than the final year is used, pensions increase will be added to compensate for the intervening inflation.

The corrections mentioned in (a) and (b) above are covered in more detail in Circular 198.

Actions for administering authorities

8. In consequence of the items in this Circular, administering authorities may wish copy this Circular to employers in their Fund (other than to Local Authorities to whom this Circular has already been sent direct) or bring the Circular to the attention of employers by directing them to the Circular on the LGE website at:
<http://www.lge.gov.uk/lge/core/page.do?pageld=71952>

Terry Edwards
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May 2007

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