

The Local Government Pensions Committee  
Secretary: Terry Edwards

## **CIRCULAR**

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**No. 200 – JUNE 2007**

### **THE “85 YEAR RULE”**

#### **Purpose of this Circular**

1. This Circular has been issued to provide authorities in England and Wales with an update on the latest news regarding the “85 year rule”.

#### **The king is dead, long live the king – an update on the “85 year rule”**

2. Just when we had thought the “85 year rule” was dead and we could crown the new-look LGPS in England and Wales it appears that plans for the coronation could be premature. On 16<sup>th</sup> May 2007, Communities and Local Government (CLG) issued a letter to all authorities in which they said:

*“in response to representations from the local authority trades unions, Ministers have given undertakings that provided affordable and legal alternatives to the current 2016 to 2020 tapered protections can be brought forward, following [a] fresh assessment of the legal and affordability issues involved, a statutory consultation exercise would then proceed on the basis of draft amending regulations. If not, then the current levels of protection would be retained.”*

This brings to mind part of the quote from Mark Twain “*the report of my death was an exaggeration*”.

3. The letter from CLG which, together with their letter of clarification dated 17<sup>th</sup> May 2007, is appended to this Circular, seeks various information from authorities and other consultees by 13<sup>th</sup> June 2007.
4. The LGA will be responding to the letter along the following lines which authorities may find helpful in preparing their own response:

“I am responding to the CLG letter of 16<sup>th</sup> May 2007 regarding additional protection for existing Scheme members from the removal of the 85 year rule.

As the Minister will be aware we [the LGA] agreed to the tapered protection to 2020 during the Tripartite Committee discussions. This was on the basis of legality and affordability, as upheld in the High Court on 27<sup>th</sup> September last year, and we were content that the tapered protection avoided what would otherwise have resulted in an unfortunate cliff edge at 2020. We still wish to avoid the cliff edge that a move away from tapered protection would otherwise entail.

We, and the Government, have consistently maintained that the Scheme in England and Wales is separate from that in Scotland and that the full protection to 2020 offered in Scotland, purportedly on the grounds that the better funding position of the Funds in Scotland permitted such extra protection to be afforded, was a matter for the Scottish Parliament to decide and should not act as a precedent for the Scheme in England and Wales.

At the Tripartite Committee meeting on 21<sup>st</sup> November 2005 it was agreed “that the cost of reinstating the rule of 85 from 1<sup>st</sup> April 2005 [to 30<sup>th</sup> September 2006] could be met by allowing members to increase their tax-free lump sum, up to a maximum of 25% of the capital value of their pension fund”. This was the only purpose the employers have agreed commutation savings could be used for on the grounds that, according to the Government Actuary’s Department (GAD), a reserve for future longevity improvements could well use up all commutation savings over the next 50 years assuming that 50% of Scheme members opt to the maximum extent possible to commute pension into lump sum.

In his statement to the House on 28<sup>th</sup> March 2006, the Minister said that “up to half the savings achieved by the final removal of the rule of 85 can be re-cycled into the development of whatever benefit package is felt by the Stakeholders and membership to be appropriate for the new-look 2008 Scheme”, which would include using the savings towards protections. He also stressed that “no additional costs associated with [the 85 year rule protections] should fall on taxpayers”.

In June 2006, GAD produced a paper on the cost of transitional protection. GAD calculated that:

- i) the capital cost of extending protection for all from 1.10.06. to 31.3.08. would be £0.5bn
- ii) the capital cost of extending protection from 31.3.13. to 31.3.16. for those who would be 60 and meet the 85 year rule by then would be £0.5bn
- iii) the capital cost of tapered reduction on service from 1.4.08. to 31.3.20. for those who would be 60 between 1.4.16. and 31.3.20. and meet the 85 year rule by then would be £0.35bn - £0.4bn
- iv) the capital cost of revoking the earlier removal of the 85 year rule (i.e. to cover service from 1.4.05. to 30.9.06) was £520m - £590m
- v) the total capital cost of protection was therefore £1.90bn - £2.0bn
- vi) the commutation saving on accrued service (assuming a 50% take up) would be £1.25bn
- vii) the net capital cost would therefore be £0.65bn - £0.75bn

Based on an annual pensionable payroll of £25bn, and looking forward 20 years, the average net cost of protection is equivalent to around 0.16% - 0.18% of pensionable payroll which GAD rounded off to 0.2%. This would cost £50m a year over 20 years (in real earnings terms).

Thus, if we assume that the cost shown in (iii) above is broadly linear, we can add a further £0.35bn - £0.4bn to the net costs if full protection to 2020 were to be agreed.

Based on an annual pensionable payroll of £25bn, and looking forward 20 years, this would increase the average net cost of protection by around another 0.1% to the equivalent of around 0.25% - 0.28% of pensionable payroll. This would cost a further £25m (i.e. increase the total to £75m) a year over 20 years (although that cost is expected to increase each year in line with earnings growth).

It appears to us, therefore, even assuming a legally effective objective justification for full protection to 2020 could be provided, that adding to costs by extending the existing protections in England and Wales would not meet the Minister's commitment to Parliament and to taxpayers unless there were to be a further adjustment to the benefit package in the new-look Scheme or a further increase in the employees' contribution rate. This will, of course, be a matter for the Minister to decide but we would not be in favour of such an approach as it would mean that new Scheme members would, in effect, be paying towards the cost of additional protections for existing members."

5. The Minister will make a decision based on the responses received.

## **Actions for administering authorities**

6. 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  
Head of Pensions  
May 2007



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**17 May 2007**

Dear all,

#### **LOCAL GOVERNMENT PENSION SCHEME**

Further to Terry Crossley's letter of 16 May 2007 (sent 14 May), subsequent

input from the Government Actuary's Department has highlighted a number of necessary revisions of figures, which are outlined below for the sake of clarification.

The figures in paragraph 3 setting out the present arrangements explained in paragraph 2 (£1.35 billion - £1.4 billion) are correct but these translate as 0.3% of pensionable payroll, not the 0.2% as suggested in the letter. Additionally, it should be noted that the £25 million figure in paragraph 3 is expected to increase each year in line with earnings growth.

The amended version of the letter will appear on the LGPS website shortly ([www.xoq83.dial.pipex/whatsnew.htm](http://www.xoq83.dial.pipex/whatsnew.htm)).

Yours sincerely

**Charlotte Hine-Haycock**  
**LGPS**



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16 May 2007

Dear Colleague

## **LOCAL GOVERNMENT PENSION SCHEME**

1. With the agreement of Ministers, your views are being sought as part of the process of freshly assessing the current provisions in the LGPS 2006 Regulations regarding the 2016 to 2020 tapered protections which apply in England and Wales.

### **Background**

2. The present arrangements, which came into force on 1 October 2006, provide that:-
  - (i) All members of the scheme as at that date continue to accrue membership under the rule of 85 terms until 31 March 2008;
  - (ii) if a qualifying member is 60 by 31 March 2016 and would have satisfied the rule of 85, no actuarial reduction will apply should he choose to retire at that age; and
  - (iii) if a qualifying member is 60, would have satisfied the rule of 85 between 1 April 2016 and 31 March 2020 and he chooses to retire at that age, an actuarial reduction will apply on a tapered basis.
3. The capital costs of these protections, has been estimated on current available data by the Government Actuary's Department (GAD) to total some £1.35 billion - £1.4 billion. This equates to some 0.2% of pensionable payroll a year. Within that overall level of protection, the estimated capital cost of the tapered protections is some £0.35 billion - £0.4 billion, which, in turn,

GAD has estimated equates to some 0.1% of pensionable payroll, or about £25 million annually for 20 years.

4. At the time these protections were introduced, an objective justification for retaining a provision which had been confirmed by the Courts as discriminatory had to be made. This led to a protection for those within 10 years of age 60 at the time of the regulatory change, and the introduction of a tapered reduction associated with changes to state retirement age in order to avoid the cliff-edge effects of earlier proposed levels of protections.
5. In response to representations from the local authority trades unions, Ministers have given undertakings that provided affordable and legal alternatives to the current 2016 to 2020 tapered protections can be brought forward, following this fresh assessment of the legal and affordability issues involved, a statutory consultation exercise would then proceed on the basis of draft amending regulations. If not, then the current levels of protection would be retained.

### **Assessment**

6. It is essential for this stage of the assessment to be authoritative and comprehensive. Consultees, therefore, are invited to consider carefully the questions set out below, and to demonstrate directly their local experience when replying.
7. To provide a sound evidential basis for this consultative phase, all consultees are invited to provide whatever appropriate information they have to the following questions: -

- (i) What is your position on the appropriateness of having protections in the Scheme for the 2016 to 2020 period? Do you agree with the tapered protections already provided? Would you prefer to see the tapering removed? If so, would you be content with the "cliff-edge" so produced?**
- (ii) If the 2016 to 2020 tapering in the regulations was removed, what would be the effect on your pension fund and on you as a Scheme employer?**
- (iii) What would be the net effect of such a change on your employer contribution rate?**
- (iv) What offsetting measures within the Scheme would you identify as a means to meet any additional costs?**
- (v) Do you see any employment / workforce advantages, or costs arising from the change from a tapered 2016 protection to full protection at 2020?**

## **Next steps**

8. Your responses to this consultation exercise are requested **no later than 13 June** and should be sent to: -

Nicola Rochester  
Zone 2/F7 Ashdown House  
123 Victoria Street  
London SW1E 6DE

or e-mailed to [nicola.rochester@communities.gsi.gov.uk](mailto:nicola.rochester@communities.gsi.gov.uk)

9. The results of the exercise will be carefully considered and reported to Ministers. The responses will be summarised and placed on the LGPS website. ([www.communities.gov.uk/lgps](http://www.communities.gov.uk/lgps)).
10. At the close of the consultation, Ministers will decide in the light of the responses received, whether or not to proceed to a full statutory consultation exercise with draft amending regulations.

Yours sincerely

**Terry Crossley**

ADDRESSEES

The Chief Executive of:

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South Yorkshire Pensions Authority  
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NAPO

Association of Educational Psychologists

Audit Commission

Other Government Departments with public service pension interests:

GAD

DoE (NI)

SPPA

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