

Rt Hon George Osborne, MP  
Chancellor of the Exchequer  
The Correspondence & Enquiry Unit  
HM Treasury  
1 Horse Guards Road  
London  
SW1A 2HQ

16 February 2011

Dear Chancellor,

**Local Government Pension Scheme – Proposed increase in employee pension contributions**

In the public sector Spending Review statement in October 2010 the Government announced its intention to increase employee pension contributions in the public service pension schemes (other than the Armed Forces Pension Scheme) by, on average, 3%. The increases would be introduced progressively over the period 2012/13 to 2014/15 but with protection for the lower paid.

We understand that the Department for Communities and Local Government (DCLG) has been informed by HM Treasury that a 3.2% increase is required in employee contributions to the Local Government Pension Scheme (LGPS), equivalent to an additional £900 million by 2014/15. DCLG has provided us with a paper setting out how the increase in employee contributions to the LGPS could potentially be achieved i.e.

Band	Salary	Current rate	2012/13	2013/14	2014/15
1	> £12,600	5.5%	5.5%	5.5%	5.5%
2	£12,601-£14,700	5.6%	5.6%	5.6%	5.6%
3	£14,701-£18,000	5.9%	5.9%	5.9%	5.9%
4	£18,001-£24,000	6.5%	6.5%	6.5%	6.5%
5	£24,001-£31,500	6.5%	7.8%	9.1%	9.7%
6	£31,501-£42,000	6.8%	8.5%	10.2%	11.0%
7	£42,001-£75,000	7.2%	9.5%	11.8%	13.0%
8	£75,001-£100,000	7.5%	10.1%	12.7%	14%
9	£100,001-£150,000	7.5%	10.3%	13.1%	14.5%
10	£150,001 >	7.5%	10.5%	13.5%	15%

The Local Government Group are very concerned that the implications for local authorities, their workforce and the wider economy may not have been fully considered by HM Treasury. These include:

- with only 6.5% of the LGPS membership earning in excess of £42,000 and with protection for lower paid employees (40% of the LGPS workforce earn less than £18,000), the main burden of the 3.2% increase will fall on middle earners;

- there may be pressure during pay negotiations to recoup, via the pay settlement, the effects of any increase in contributions (or loss of future pension rights upon opting out);
- the demographics of the Scheme's membership makes it difficult to produce a set of tariff tables that are fair and progressive across all salary bands;
- there is strong evidence to suggest that the opt-out rate will be far greater than the 1% envisaged in the Spending Review announcement. Neither is there any evidence to suggest that full account has been taken of the likely reductions in the local government workforce over the Spending Review period, a large proportion of which will be scheme members;
- there is a considerable risk therefore that the £900 million target additional income by 2014/15 will not be achieved unless even greater increases are imposed on those scheme members who remain (leading to the possibility of a vicious circle of even higher opt-out rates);
- a significant increase in employee contributions at a time of pay restraint / pay cuts and increasing inflation is likely to lead to a significant worsening in industrial relations;
- such an increase in contributions will lead to a further dampening of employee spending power at a time when the Government is seeking to promote economic recovery;
- there are real concerns over the disparity between public sector schemes meaning that, for example, highly paid members of some other public service schemes will be paying a lower contribution rate than the lowest paid workers in local government;
- there are consequential recruitment, retention and promotion implications. The pension scheme as an element of the reward package will be less attractive and the cliff edges contained in the above table may act as a disincentive to seek promotion (e.g. an employee earning £24,000 who receives a £1 increase would pay an extra 3.2% on all of their earnings, reducing their take-home pay to significantly less than it was prior to the promotion);
- part-time employees, who constitute the overwhelming majority of low paid workers in local government, have their contribution rate assessed by reference to their whole-time equivalent salary. Thus, many of those part-time employees with part-time salaries below the low pay protection threshold will, in fact, not benefit from the protection (because their whole-time equivalent salary is greater than £24,000);
- a significant level of opt outs would result in:
  - i. a serious and detrimental impact on the Scheme's future sustainability and viability;

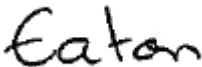
- ii. LGPS Funds would become more mature leading to a move away from equities into bonds. This could distort the bond market and a move out of UK equities (in which the LGPS Funds have significant holdings) could have an impact on the UK investment sector (FTSE).
- iii. fewer employees would be making adequate pension provision for themselves, ultimately leading to further reliance on the State via means tested benefits in retirement.

**The LGPS is different to the other public sector schemes in that it is a funded scheme and currently has a positive cash flow.**

For some years the LG Group has pursued a policy position of the LGPS being sustainable and affordable. In our opinion these proposals seriously undermine these principles. All political Groups within the LGA strongly urge that this is recognised and that the Government enters into dialogue with employers and unions in order to consider further how best to achieve the Government's aims ahead of the outcomes from the report of the Independent Public Service Pensions Commission.

We are prepared to consider amendments to Scheme benefits with CLG as regulator and the trade unions to try and find alternatives to mitigate the rising cost of pensions to the public purse.

Yours sincerely,



Baroness Eaton DBE DL  
Chairman, Local Government Association



Mayor Sir Steve Bullock,  
Chair, Workforce Programme Board.

Cc:

Rt Hon Eric Pickles, MP – Secretary of State for Communities and Local Government  
Rt Hon Danny Alexander, MP – Chief Secretary to the Treasury