

Ten facts about the Local Government Pension Scheme

Pension provision has long been a hot topic for discussion. However, currently the spotlight is firmly on the public sector pension schemes, particularly given the impending Independent Public Service Pensions Commissions led by Lord Hutton. The cost of public sector pensions has also been highlighted once again, this time within the debate about public sector spending cuts. As a result much information has been put into the public domain about public sector pension schemes which is sometimes confused and often misrepresented.

To help you through the minefield of information currently available we thought it would be useful to state some of the key facts about the Local Government Pension Scheme (LGPS):

1. The LGPS is often referred to as “gold-plated”. This may be because, unlike the private sector, the pensions are secure and pensions will be paid on retirement from the local LGPS fund regardless of financial position of the employer. However, some facts to bear in mind about LGPS pensions are as follows:

- The average pension paid under the LGPS is approximately £4,000 per year or equivalent to 23% of gross average pay in local government. This is around half the average pension paid by all open Defined Benefit schemes including the public sector schemes.
- For women the average pension payment is just £2,600 per year
- In the Avon Pension Fund, 70% of pensions paid are less than £5,000 per year and 86% of pensions paid are less than £10,000 per year.

2. The LGPS is a “funded” scheme like private sector defined benefit schemes and **unlike** other public sector schemes (e.g. NHS, police and the civil service) which are “**unfunded**”. As a funded scheme the LGPS has investment assets in place to meet pension benefits that have accrued. In addition to the income generated by these assets, the costs are met from employer contributions (which in the case of the councils come from a combination of government grant and council tax) and employee contributions. It represents a viable and sustainable scheme; however, its funded nature makes the costs far more transparent than other public sector schemes.

In the unfunded public sector schemes, no assets are set aside from contributions to meet future pension payments. These “pay as you go” schemes are financed in such a way that this years pensions paid to pensioners are paid for from the employees contributions with any further sum required to meet the pensions bill met by a pre-set employer contribution and if there is still a shortfall, it is topped up by the Treasury. Therefore the employer contributions and any top up from the Treasury are funded by the taxpayer.

3. The cost of the total pension liabilities of the LGPS is about 0.5% of Gross Domestic Product (GDP) – however about 0.3% of this is funded by the

investment assets so the costs not yet funded represent about 0.2% of GDP. In contrast, the cost of the other unfunded public sector schemes accounts for about 1.5-2% of GDP. In other words other public sector schemes have an unfunded element which is significantly more than that of the LGPS. This means that a much greater proportion of taxation is funding the other public sector pension schemes compared to the LGPS

4. The LGPS has positive cashflow with income from contributions and investments exceeding expenditure on pension payments by around £4 - 5 billion each year.

5. The LGPS has assets in excess of £100 billion which is sufficient to pay benefits for over 20 years given the current benefits structure. This makes the LGPS collectively the largest pension fund in the country and, importantly, a major shareholder in businesses and the UK economy.

6. There are more than 4 million members in the LGPS and more than 7,000 employers, many of which are private sector companies and charities providing local public services.

7. The average contribution paid into the LGPS by the employees is 6.3% of pay. The contributions are tiered to reflect salary levels ranging from 5.5% to 7.5% of pay. This compares to around 5% of pay on average for private sector Defined Benefit schemes. The government has already indicated a new 10% rate for those earning more than £100,000.

8. The average employer contribution for future service is around 14% of pay which is similar to the average private sector employer contribution rate of around 15% (for defined benefit schemes). As is the case with the private sector, most employers are paying additional contributions to reduce the deficit.

9. The normal retirement age is 65 years for all members (limited protections that exist will be phased out by 2016). In other public sector pension schemes the normal retirement age for existing members is 60, increasing in some schemes to 65 for recent entrants.

10. There is already statutory provision for a “cap and share” mechanism to be put in place for the LGPS. The cap will limit the contribution rate that employers will pay and employees will be asked to share some of the extra costs as they arise. This is particularly relevant as we live longer, and scheme members may be asked to share the costs of improving longevity in the future.

Avon Pension Fund
03/08/2010