

## **The Local Government Pension Scheme (Scotland)**

Addressing discrimination – amendments to the statutory underpin

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# 1. Scope of the consultation

Topic of this consultation:	This consultation seeks views on changes to the Local Government Pension Scheme (LGPS) in Scotland. It outlines proposed changes to the LGPS statutory underpin protection to remove unlawful discrimination found by the Courts in relation to public service pension scheme ‘transitional protection’ arrangements. Specifically, we propose to remove the condition that required a member to have been within ten years of their normal pension age on 1st April 2012 to be eligible for underpin protection. In removing the discrimination, we are proposing a number of supplementary changes to ensure the revised underpin works effectively and consistently for all members.
Scope of this consultation:	SPPA is consulting on changes to the regulations governing the Local Government Pension Scheme (Scotland) (LGPS).
Geographical scope:	These proposals relate to the LGPS in Scotland. Separate consultation exercises are being undertaken by the UK Government for the LGPS in England & Wales and another will follow for the scheme in Northern Ireland.
Impact Assessment:	<p><u>Public Sector Equality Duty</u></p> <p>The Scottish Public Pensions Agency (SPPA) has worked with the Government Actuary’s Department (GAD) to analyse the proposals set out in this consultation document in order to fulfil the requirements of the Public Sector Equality Duty (PSED) as set out in section 149 of the Equality Act 2010. This requires the Agency to pay due regard to the need to:</p> <ol style="list-style-type: none"> <li>1) eliminate unlawful discrimination, harassment and victimisation and other conduct prohibited by the Act</li> <li>2) advance equality of opportunity between people who share a protected characteristic and those who do not</li> <li>3) foster good relations between people who share a protected characteristic and those who do not.</li> </ol> <p>An Impact Assessment has been published with this consultation document. The proposals outlined here are intended to remove age discrimination, which had been found to be unlawful in the firefighters’ and judicial pension schemes, from the LGPS rules governing the underpin. We consider that the changes proposed will significantly reduce differential impacts in how the underpin applies based on a member’s age, by removing the age-related qualifying criteria found to be unlawful by the Courts in the context of the firefighters’ and judicial pension schemes.</p> <p>Based on analysis undertaken by GAD using active membership data for the LGPS as at 31st March 2017, we anticipate that some differences in how the underpin would apply to members of different age groups would remain. These are set out separately below, along with our assessment of these differences.</p> <ol style="list-style-type: none"> <li>1) Qualification for the underpin - GAD’s analysis shows that older active members on 31st March 2020 would be more likely to qualify for the revised</li> </ol>

underpin than younger active members. This is principally because of our proposal that the 31st March 2012 qualifying date for underpin protection is retained. The proportion of members active in the scheme as at 31st March 2020 who had been members of the scheme on 31st March 2012 is lower for younger members, where experience shows they have a higher withdrawal rate from scheme membership. We consider that members joining the LGPS after 31st March 2012 do not need to be provided with underpin protection. Members who joined after this date will have joined the LGPS when either it had already transitioned to the career average structure (for post-1st April 2015 joiners), or when it was well publicised that the LGPS benefits were reforming.

2) Members who benefit from the underpin - GAD's analysis also shows that active members between the ages of 41 and 55 as at 31st March 2020 would be more likely to benefit from the revised underpin (i.e. where the calculated final salary benefit is higher than the calculated career average benefit) than their younger and older colleagues. This reflects previous experience and future expectation that:

- this group are more likely than their older colleagues to experience the pay progression that would make the final salary benefit higher over the underpin period and
- this group are more likely than their younger colleagues to remain in active membership until such time as they would receive the pay progression necessary for the underpin to result in an addition to their pension (e.g. through promotions and other pay increases).

These differential impacts reflect the workings of a final salary scheme, and demonstrate some of the effects that can arise under that design. The Government proposes to move all local government pensions accrual to a career average basis, without underpin protection, from April 2022 to apply a fairer system to all future service.

In relation to sex, we anticipate that, broadly, the proportion of men and women who would qualify for the revised underpin and benefit from that protection matches the profile of the scheme. This assessment is also based on analysis undertaken by GAD on active membership data for the LGPS as at 31st March 2017.

Proportionally, GAD's assessment is that men would be marginally more likely to qualify for the revised underpin and to benefit to a greater extent from underpin protection than women. This reflects the fact that, in line with previous scheme experience, the average male LGPS member would be expected to have higher salary progression than the average woman and that women are generally expected to have higher voluntary withdrawal rates than men. Members with longer scheme membership and with higher salary progression would be more likely to benefit from the underpin (i.e. where the final salary benefit is higher).

These small differential impacts also demonstrate some of the effects that can arise under a final salary design. The Government proposes to move all LGPS accrual to a career average basis, without underpin protection, from April 2022 to apply a fairer system to all future service.

Limited data specific to the LGPS in Scotland is available in relation to other protected characteristics. However, we do not consider that the changes to underpin protection proposed in the consultation will result in any differential impact to individuals with the following protected characteristics: disability, ethnicity, religion or belief, gender reassignment, pregnancy and maternity, sexual orientation and marriage/civil partnership.

Further information regarding the equalities impacts of our proposals is contained in paragraphs 110 to 126. In this consultation, we are seeking views from stakeholders on the equalities impacts of the changes proposed. These views will be considered in determining how to proceed following the consultation exercise.

The potential equalities impacts of our proposals will be kept under review. A further equalities impact assessment will be undertaken following the consultation at the appropriate juncture.

#### Other impacts

The proposals in this paper are estimated to cost LGPS employers £355 million in the coming decades, as protected members retire and begin to receive their benefits. This estimate is based on a number of assumptions regarding the demographics of the LGPS in the years to come. Predicting whether the underpin becomes valuable in the future depends heavily on assumptions on long-term future pay growth trends. The £355 million estimate is based on an annual future long-term pay growth assumption of CPI+2.2%, which is the assumption used by GAD for the 2017 valuations of public service pension schemes. If annual future pay growth is less than this, the ultimate costs will be lower (and vice versa).

As the LGPS is a funded scheme, employer contribution rates are set through local fund valuations and take into account a number of factors. As a result of this, it is not possible to say precisely how the proposals may impact on any individual employer's contribution rate.

None of the changes contained in this consultation require a Regulatory Impact Assessment under the Small Business, Enterprise and Employment Act 2015.

## 2. Basic information

To:	<p>This consultation outlines details of proposed changes to the benefits of the LGPS and is particularly aimed at LGPS administering authorities, scheme members, scheme employers and their representatives.</p> <p>Any change to the LGPS is likely to be of interest to other stakeholders as well, such as professional advisers, and local taxpayers. We welcome views on the proposals from all interested parties.</p>
Body/bodies responsible for the consultation:	Scottish Public Pensions Agency
Duration:	This consultation will last for 12 weeks from 31/07/2020 to 23/10/2020
Enquiries:	<p>For any enquiries about the consultation please contact: <a href="mailto:SPPAPolicy@gov.scot">SPPAPolicy@gov.scot</a></p>
How to respond:	<p>Please respond by email to: <a href="mailto:SPPAPolicy@gov.scot">SPPAPolicy@gov.scot</a></p> <p>Alternatively, please send postal responses to:</p> <p>LGPS Policy Team          Scottish Public Pensions Agency          7 Tweedside park          Tweedbank          Galashiels          TD1 3TE</p> <p>When you are responding, please make it clear whether you are replying as an individual or submitting an official response on behalf of an organisation and include:</p> <ul style="list-style-type: none"> <li>- your name,</li> <li>- your position (if applicable),</li> <li>- the name of your organisation (if applicable),</li> <li>- an address (including post-code),</li> <li>- an email address, and</li> <li>- a contact telephone number.</li> </ul>

### 3. Introduction

1. This consultation contains proposals to amend the regulations governing ‘transitional protection’ in the LGPS, required following a successful legal challenge to transitional protection arrangements in the firefighters’ and judicial pension schemes.

2. In April 2015, wholesale changes were made to the Local Government Pension Scheme in Scotland (LGPS) to reform the scheme’s benefits structure. These changes were implemented as part of wider reforms to public sector pensions introduced by the UK Government’s Public Service Pensions Act 2013. In the LGPS, these changes included:

- moving benefit accrual from a final salary to a career average basis, and
- linking members’ normal retirement age to their state pension age.

3. As a result of the negotiations for the new scheme and in agreement with trade unions, ‘transitional provisions’ were introduced by Scottish Ministers for members who were within 10 years of normal retirement age in 2012. These transitional protection arrangements applied across public service pension schemes where older members were permitted to remain in their pre-2015 schemes, In the LGPS all members were moved the new arrangements from 1 April 2015 however those within 10 years of their normal pension age on 1 April 2012 were protected through a statutory ‘underpin’.

4. This underpin protection provides that additional checks are undertaken for qualifying members to ensure that the career average pension payable under the reformed LGPS is at least as high as the member would have been entitled to receive under the final salary scheme. Where it is not as high, scheme regulations provide that an addition must be applied to the member’s career average pension to make up the shortfall.

5. In the ‘*McCloud*’ and ‘*Sargeant*’ court cases (which related to the judicial and firefighters’ pension schemes respectively), the Court of Appeal found that the transitional protection arrangements directly discriminated against younger members in those schemes. In July 2019, the UK government confirmed its view that the ruling had implications for all the main public service pension schemes, including the LGPS, and that the discrimination would be addressed in all the relevant schemes, regardless of whether members had lodged a legal claim. Responsibility for occupational pensions, including public service pensions, is reserved to the UK Government, although Scottish Ministers have executively devolved competence to make regulations for five public service schemes within the overarching framework.

6. This consultation sets out how SPPA propose to amend the Scottish LGPS underpin to address the age discrimination included in scheme reform. The proposals mirror those currently under consultation by the UK Government, and SPPA would like to acknowledge the collaborative approach taken across the UK LGPS schemes and in the preparation of the consultation materials. Primarily, we propose to remove the age requirements from the underpin qualification criteria. We intend to extend the underpin to younger members in respect of service accrued to 31 March 2022 and we are also proposing additional changes to ensure that the underpin works effectively and consistently for all members.

From 1 April 2022, it is proposed that the period of underpin protection will cease and all active LGPS members will accrue benefits in the career average scheme, without a continuing final salary underpin for their post 2022 service.

**7. Views from respondents are sought on questions 1 to 27 as well as on the draft regulations attached as Annex B.**

## **4. Background**

### **4.1 Public service pension reform and transitional protection**

8. Following on from a fundamental structural review by the Independent Public Service Pension Commission (IPSPC) Scottish Ministers required the reform of the Local Government Pension Scheme to meet the legislative requirements of the Public Service Pensions Act 2013.

9. The UK Government commissioned the review because the cost of providing the schemes had increased significantly over the previous decades, with most of this increase falling to the taxpayer. At the same time, occupational pension provision in the private sector significantly changed, with employers moving away from defined benefit schemes towards defined contribution arrangements.

10. In their final report<sup>1</sup>, the IPSPC set out a framework for comprehensive reform of public service pensions that sought to balance concerns about the cost of the schemes to taxpayers and the need to ensure decent levels of retirement income for those who have devoted their working lives in the service of the public.

11. The UK Government accepted Lord Hutton's recommendations as the basis for consultation with scheme employers, trades unions and other interested parties. New scheme designs were agreed with representatives in some workforces, such as in respect of local government, but not accepted in others. During negotiations the UK Government agreed to improve the value of the schemes offered and to allow schemes to include protections for those public service workers who, as of 1 April 2012, had ten years or less to their pension age.

12. The reforms were implemented in the LGPS in Scotland from 1<sup>st</sup> April 2015. The main features of the reformed scheme included later retirement ages to reflect the fact people have been living longer, higher employee contributions to rebalance the costs of the schemes between the members and taxpayers, and pensions based on average earnings rather than on pay at the point members retire or otherwise leave the scheme.

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<sup>1</sup> <https://www.gov.uk/government/publications/independent-public-service-pensions-commission-final-report-by-lord-hutton>

13. The schemes were designed to ensure that members would have pensions that at least met the target levels identified by Lord Turner's Pension Commission in its reports to Parliament in 2004 and 2005 on the levels of income needed in retirement.

In addition, the new designs were designed to ensure that most low and middle earners working a full career receive pension benefits at least as good, if not better than under the previous arrangements.

14. The UK Government considers that the reformed schemes remain among the most generous available in the UK, and an important part of the remuneration of public service workers. Public service pension provision compares favourably with pension provision in the private sector

## 4.2 Reform in the LGPS

15. In the LGPS, the final salary scheme that existed prior to these reforms was known as '**the 2009 Scheme**'. The reform package implemented from April 2015 ('**the 2015 Scheme**') through [The Local Government Pension Scheme Regulations 2014](#) ('**the 2014 Regulations**')<sup>2</sup> consisted of the following main elements:

- fundamentally, and consistent with the approach taken across the public sector, a move to future benefit accrual based on a member's pay over their career (a 'career average' structure), from a structure where member's benefits were based entirely on a member's pay at leaving the scheme (a 'final salary' structure). Importantly, where active members had membership of the LGPS prior to April 2015 and did not have a disqualifying break in service<sup>3</sup>, they retained a 'final salary link' that meant their pay at point of leaving the scheme would still be used in calculating their pre-April 2015 scheme benefits, even where this is after April 2015.
- a move from a normal pension age of 65 to a normal pension age linked to a member's state pension age (ranging from 65 to 68), but with members still able to retire as early as 55 or as late as 75, with actuarial reductions or increases applied, respectively.
- a move from a 1/60<sup>th</sup> accrual rate to a 1/49<sup>th</sup> accrual rate. A pension scheme's accrual rate is the proportion of a member's pay that they receive for each year of membership. The change in the LGPS accrual rate in the 2015 Scheme was a 22% improvement from that which applied in the 2009 Scheme.
- revisions to employee contribution bandings. From April 2015, employees' contributions to the LGPS were banded from 5.5% of earnings (for members earning less than £20,300 per year) up to 12.5% of earnings (for members earning over £45,300 per year). Contribution rates had also been banded in the 2009 Scheme, but the range had been narrower, from 5.5% to 12% of earnings.

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<sup>2</sup> Subsequent changes to the 2014 Regulations have been consolidated in the Local Government Pension Scheme (Scotland) Regulations 2018 [S.S.I. 2018/141 "the 2018 Regulations"].

<sup>3</sup> Where referred to in this document, a 'disqualifying break in service' is a continuous break of more than five years in active membership of a public service pension scheme.

- the introduction of a 50/50 section, giving scheme members the flexibility to pay half the contributions for half the pension accrual for a period of time, whilst still retaining full life cover and ill-health cover.

16. As a whole, the package was designed to achieve the government's aim to make the scheme more sustainable, affordable and fairer in the longer term. In particular, the combination of the move to a career average basis and the improvement to the LGPS accrual rate means that most low and medium paid members will receive a pension from the 2015 Scheme at least as good as the pension they would have received from the 2009 Scheme. In addition, whilst LGPS employer contributions vary, members will continue to benefit from significantly higher employer contributions than the average applicable in the private sector.

### 4.3 The statutory underpin

17. Unlike most other public service pension schemes, the LGPS provided transitional protection to its older workers via a statutory underpin. All members moved into the 2015 Scheme on the reform date of 1<sup>st</sup> April 2015, but protected members were given a statutory underpin that provides their retirement pension cannot be less than it would have been in the 2009 Scheme. In some public service pension schemes, tapered protections were provided to members who were between 10 and 14 years from their normal pension age on 1<sup>st</sup> April 2012, and so were not eligible for full protection (which was reserved for those within ten years of their normal pension age on 1<sup>st</sup> April 2012) However, in the LGPS, there were no tapered protections.

18. Underpin protection differs from the approach used in other public service pension schemes<sup>4</sup> where older workers who met the criteria for transitional protection stayed in their final salary schemes when new career average schemes were introduced in April 2015. In those schemes, different rules may therefore apply to protected and unprotected members in relation to areas of scheme design including contribution rates, survivor benefits and ill health retirement.

19. By contrast, the existing LGPS underpin only has application in relation to the value of a member's pension at their 'underpin date' (see paragraph 19 for further details). All members have participated in the reformed career average scheme from April 2015 and the same rules in relation to contributions and benefits apply to all members in the same way.

20. Underpin protection in the LGPS was implemented through regulation 4 of the Local Government Pension Scheme (Transitional Provisions and Savings) (Scotland) Regulations 2014<sup>5</sup> (**'the 2014 Transitional Regulations'**). At a high level, underpin protection under regulation 4 works in the following way:

- Underpin protection is granted to those who were active members in the LGPS on 31<sup>st</sup> March 2012 and who on 1<sup>st</sup> April 2012 were 10 years or less from the normal

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<sup>4</sup> with the exception of the local government pension schemes in E&W and Northern Ireland who took a similar approach to the LGPS in Scotland

<sup>5</sup> <https://www.legislation.gov.uk/ssi/2014/233/introduction/made> (as amended)

pension age applicable to the member under the 2009 Scheme (usually 65<sup>6</sup>). (regulation 4(1)(a))

- Those who meet the basic criteria for underpin protection retain this so long as they are:
  - in active membership in the 2015 Scheme the day before their ‘underpin date’ (see below),
  - do not have a disqualifying break in service after 31<sup>st</sup> March 2012, and
  - have not drawn benefits from the 2015 Scheme before their underpin date. (regulation 4(1)(b) to (d) and (3))
  
- The underpin test is carried out on an individual’s ‘underpin date’ which is the earlier of:
  - the date the member reaches their normal pension age under the 2009 Scheme (usually 65), or
  - the date the member ceased to be an active member of the scheme with an immediate entitlement to a benefit (regulation 4(2) of the 2014 Transitional regulations.
  
- The underpin test is carried out by comparing the ‘assumed benefits’ (i.e. the career average benefits the member has accrued) against the ‘underpin amount’ (i.e. the final salary benefits the member would have accrued if the scheme had not been reformed) (regulations 4(5) and (6)). These paragraphs contain detailed provisions which enable administrators to take into account a variety of factors in the comparison of benefits. For example, where the member is due to receive an enhancement to their 2015 Scheme benefits as a result of retiring on ill-health grounds, the difference between that enhancement and the enhancement they would have received under the 2009 Scheme would be considered.
  
- If the underpin amount is calculated to be higher than the assumed benefits on the underpin date, the member’s pension account is to be increased by the difference. (regulation 4(4))

#### **4.4 The *McCloud* and *Sargeant* cases**

21. Soon after the reformed scheme benefit structures were introduced in other public service pension schemes in April 2015, legal challenges were brought against the transitional protection arrangements in the judicial and firefighters’ pension schemes (*McCloud* and *Sargeant*, respectively) on grounds that the transitional protections offered to older workers constituted unjustified direct age discrimination. In those cases, younger firefighters and judges argued that younger workers were treated less favourably than older

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6 By virtue of regulation 24(4) of the 2014 Transitional Provisions and Savings Regulations, members of Learning Teaching Scotland, Skills Development Scotland, Scottish Legal Complaints Commission, and Social Care and Social Work Improvement Scotland have a protected NPA of 60 in relation to pre April 2015 benefits.

workers who were given transitional protection. The Court of Appeal ruled in December 2018 that transitional protection in the judicial and firefighters' pension schemes gave rise to unlawful age discrimination.

22. The UK Government sought permission to appeal to the Supreme Court.

This application was refused on 27 June 2019. In a written ministerial statement on 15 July 2019<sup>7</sup>, the government explained that it accepted that the Court of Appeal's judgment had implications for all schemes established under the Public Service Pensions Act 2013, as all schemes had provided transitional protection arrangements for older members. The government confirmed that it would take steps to address the difference in treatment across all schemes and for all members with relevant service, regardless of whether they had lodged a claim. The matter has been remitted to the Employment Tribunals to agree a remedy for claimants<sup>8</sup>. Since summer 2019, SPPA have been considering the changes necessary to remove the unlawful discrimination from LGPS regulations.

## 5. Addressing the discrimination

### 5.1 Our Approach

23. Through the *McCloud* and *Sargeant* cases, the Courts identified unjustified age discrimination in transitional protection arrangements in the Judicial and Firefighters' Pension Schemes. This unlawful discrimination exists between two groups of LGPS members:

- those who were in service on 31 March 2012 and were within ten years of Normal Pension Age (NPA) on 1<sup>st</sup> April 2012, therefore benefiting from underpin protection; and,
- those who were in service on 31 March 2012 and were more than ten years from NPA, and so were not eligible for underpin protection.

24. At a high-level, our proposal for removing the unlawful age discrimination from the LGPS is to extend underpin protection to the second group of members listed above i.e. those who were not old enough to receive underpin protection when it was originally introduced. This should ensure that the two groups listed are treated equally for benefits accrued from April 2015 onwards. This proposal is described in more detail in the next section ('Detailed proposals'). The updated underpin is referred to here as 'the revised underpin'.

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<sup>7</sup> <https://www.judiciary.uk/wp-content/uploads/2018/12/lord-chancellor-v-mcloud-and-ors-judgment.pdf>  
[s-answers-statements/written-statement/Commons/2019-07-15/HCWS1725/](https://www.judiciary.uk/wp-content/uploads/2019/07/written-statement-commons-2019-07-15-hcws1725/)

<sup>8</sup> The LGPS in Scotland does not have any ongoing court cases relating to its underpin protection.

25. Consultees may be aware that HM Treasury have recently launched a consultation<sup>9</sup> seeking views on this matter as it applies to other public service pension schemes<sup>10</sup>. As noted already, transitional protection arrangements were different in other public service pension schemes and therefore different issues arise in considering an appropriate way to address the discrimination found in *McCloud* and *Sargeant*. The HM Treasury consultation seeks views on two options for removing the discrimination in those schemes, both involving an element of member choice between the reformed career average schemes and the legacy final salary schemes.

26. Member choice is being considered in other public service pension schemes. In those schemes, the two groups of members have participated in different pension schemes since April 2015 with different benefits between reformed and legacy schemes and potentially, different employee contribution rates. This is not the case in the LGPS because underpin protection is designed to ensure that a qualifying member is better off without needing to make a choice. It is therefore appropriate for members in those schemes to be given a choice, at a point in time, as to whether they would prefer their benefits to be provided from the reformed scheme or the legacy scheme.

27. As set out in paragraphs 17 to 20, the underpin is principally an administrative test undertaken at the earlier of the date a qualifying member leaves active service and the date they reach their 2009 Scheme normal pension age. It is designed to guarantee that a qualifying member's pension calculation gives them the better of a) the pension they have built up in the career average 2015 Scheme and b) the pension they would have built up in the final salary 2009 Scheme, over the same time period.

**Question 1 – Do you agree with our proposal to remove the discrimination found in the *McCloud* and *Sargeant* cases by extending the statutory underpin to younger scheme members?**

28. To achieve the full benefits of the career average reforms made in April 2015, it is the Government's view that the underpin period should end for all qualifying members at a specified point in time.

29. Under the rules governing the existing underpin, no further underpin dates will be able to take place beyond 31 March 2022, as this is the last date a protected member can reach their 2009 Scheme normal retirement age. In considering how to equalise treatment between the unprotected and protected groups, we propose that both groups will be given underpin protection from 1 April 2015 to 31 March 2022 (or to the members' underpin date, where this is earlier). We consider that, this approach will mean there is a consistent period of protection for all qualifying members i.e. those who were members of the scheme on 31 March 2012 and who went to on to have 2015 Scheme membership without a disqualifying break in service (and who aggregated their membership), regardless of their age.

30. From 1 April 2022 it is our intention that all service in the LGPS will be on a career average basis, with no underpin. As set out in the Background section, we believe that the move from a final salary to a career average pension scheme design in April 2015 created a fairer structure for LGPS members. Under the 2015 Scheme, those public servants who

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<sup>9</sup> [HM Treasury Consultation 16 July 2020](#)

<sup>10</sup> All LGPS schemes are out of scope for the HM Treasury consultation.

see considerable increases in earnings over their career – and particularly towards the end of their career – are no longer likely to be relatively favoured compared with their colleagues who did not. Phasing out underpin protection is an important step to achieving the full benefits of a career average scheme design.

## **Question 2 – Do you agree that the underpin period should end in March 2022?**

31. We are keen to ensure that the group of younger members who, under our proposals, would gain underpin protection have an equivalent level of protection to their older colleagues. It is therefore proposed that the underpin comparison would not, for most qualifying members, take place upon the underpin period ending in March 2022. Instead, the comparison of 2009 Scheme and 2015 Scheme benefits would take place at a qualifying member's underpin date (generally, the earlier of the member's date of leaving and age 65), even if this is after March 2022 – i.e. qualifying members will retain an ongoing 'final salary link', consistent with their pre-2015 pension accrual.

For those who are currently at an earlier stage of their career, and who may have promotions and other salary increases later in their career, this ensures a fairer comparison of the two schemes' benefits. The final pay calculation would be based on a member's pay over their last 365 days of active membership, and would take into account the existing 'lookback' provisions where members have had a reduction in pay.

32. As part of this project we have considered how the existing underpin regulations work and the following section contains details of changes we are proposing. Collectively, the changes mean that the revised underpin regulations will differ in a number of respects from the existing underpin provisions contained in regulation 4 of the 2014 Transitional Regulations. We consider that these amendments are essential to ensure that the underpin regulations are clear and consistent and provide a framework of protection that works more effectively for all stakeholders and which, at the same time, provides in essence the same level of protection to scheme members.

33. Nonetheless, to avoid creating new differences in treatment in the LGPS, we propose that the amended regulations will apply retrospectively from 1 April 2015, ensuring that all qualifying members are subject to the same detailed provisions. We believe this is the best approach to addressing the findings of the Courts, and removing differences in treatment between older and younger workers. We do not plan that members' accrued rights would be detrimentally affected as a result of this approach, but we welcome comments from stakeholders if there are specific concerns about potential accrued rights issues.

34. In proposing these changes, we have considered the legal principle of 'minimum interference'. The courts have found this principle generally applies to pensions changes following an equal pay issue. Whilst it has not been recognised outside the context of equal pay, it could be considered in other contexts too. 'Minimum interference' means that the scheme is obliged to make the minimum necessary interference to ensure the scheme operates lawfully. Whilst some of the changes outlined in this consultation paper are not a direct consequence of the Courts' findings in the *McCloud* and *Sargeant* cases, we believe that they are necessary for the effective and consistent application of underpin protection to members of the LGPS.

35. Retrospective application of the proposed regulations means that certain cases will need to be revisited by scheme administrators. Below are examples of such cases:

- Cases where a member had underpin protection originally and the revised underpin may have applied differently to them. In practice, this may be all cases where a member already has underpin protection and has since had their underpin date.
- Cases where a member does not currently have underpin protection, but would have under the revised underpin, and has since retired or left the LGPS with a deferred benefit.
- Cases where a member does not currently have underpin protection, but would have under the revised underpin, and has since transferred out of the LGPS or trivially commuted their benefits.

36. There will also be more difficult cases, for example, where members who may have benefitted from the proposals outlined in this consultation have died.

In such cases, it is our view that administrators should take all steps to ensure that any retrospective increase in a member's pension arising from the underpin is taken into account in respect of relevant survivor benefits that became payable at the time of the member's death.

37. We are aware that retrospective application of the proposed draft regulations will lead to significant administrative complexity. We do not anticipate any recalculations would result in members' benefits being detrimentally affected. Further consideration of the complexities arising from retrospection are considered in the Implementation and Impacts section.

**Question 3 – Do you agree that the revised regulations should apply retrospectively to 1<sup>st</sup> April 2015?**

38. This consultation sets out proposals which are principally about removing unlawful discrimination from the LGPS. Achieving this key aim, and minimising the risk of further issues arising, has therefore been our primary concern in coming forward with these proposals. However, in doing so, we have been conscious of the additional administrative burden these changes would create and have sought to minimise the impacts wherever possible. We consider that the proposed approach is the simplest way we can effectively ensure that the revised underpin works effectively and fairly for all. Further consideration of the potential administrative impacts of the proposals is outlined in paragraphs 132 to 134.

## **6. Detailed proposals**

39. This section contains our detailed proposals on the proposed amendments to the underpin, contained in annex B. We welcome general comments on those draft regulations, as well as specific comments on the below questions.

**Question 4 – Do the draft regulations implement the revised underpin which we describe in this paper?**

**Question 5 – Do the draft regulations provide for a framework of protection which would work effectively for members, employers and administrators?**

**Question 6 – Do you have other comments on technical matters related to the draft regulations?**

**6.1 The revised underpin**

40. The approach we have taken to the revised underpin consists of a number of basic elements, as described here.

**Qualification criteria**

41. Fundamentally, under the revised underpin, members will no longer need to have been within ten years of their 2009 Scheme normal retirement age to qualify for underpin protection.

Members who were active in the 2009 Scheme on 31 March 2012 and who have accrued benefits under the 2015 Scheme without a disqualifying break in service (five or more years) would have underpin protection.

42. An aspect of the existing underpin regulations that we are seeking to change is the requirement that a member must leave active service with an immediate entitlement to a pension for underpin protection to apply to them (regulation 4(1)(b) of the 2014 Transitional Regulations). We anticipate that when underpin protection is extended to younger workers, it is much more likely that members will leave the scheme before having an immediate entitlement to benefits, meaning they would not, as things stand, benefit from underpin protection. Under the revised underpin, we propose that underpin protection would apply where a member leaves with either a deferred or an immediate entitlement to a pension. This approach is also more likely to ensure that LGPS regulations are compliant with preservation requirements under the Pension Schemes Act 1993, which broadly require that schemes do not contain rules which mean that leavers prior to normal pension age are treated less favourably than leavers at normal pension age. The retrospective application of this change would also aim to ensure that any members protected under the existing underpin who have suffered detriment due to the current wording would regain their underpin protection.

43. As per existing requirements, members who leave the LGPS without an immediate or deferred entitlement to a pension would not have underpin protection, as they would only be eligible for a refund of their contributions, aggregation with another LGPS record or a transfer to another scheme

**Question 7 – Do you agree that members should not have to have an immediate entitlement to a pension at the date they leave the scheme for underpin protection to apply?**

**Question 8 – Are there any other comments regarding the proposed underpin qualifying criteria you would like to make?**

## 6.2 Aggregation

44. In reviewing the operation of the existing underpin, it has become clear that the current regulations do not implement our policy intent as clearly as we would like in one important respect, and the existing regulations could cause substantial new issues to arise. Whilst the LGPS is one pension scheme, it is a locally administered scheme, with 11 administering authorities throughout Scotland. It is an important principle for the effective and efficient administration of the scheme that administrators are generally able to calculate pension benefits independently and do not need to obtain data from other LGPS administrators to be able to undertake basic pension calculations. Such an approach also ensures that the scheme is run in accordance with the principle of 'data minimisation', where personal data is not shared between data controllers any more than is necessary for the effective administration of a member's pension.

45. To prevent such complications, the LGPS has aggregation provisions which mean that separate pension records can be joined together<sup>11</sup>. This means that, in most cases<sup>12</sup>, members can choose whether to have LGPS records aggregated or kept separate from one another. Since 1st April 2015, aggregation is usually automatic - where a member leaves an employment with a deferred benefit and then rejoins the LGPS in another employment (potentially in another pension fund), they have 12 months to elect to their administrator for aggregation not to apply.<sup>13</sup>

46. Where a member takes a decision which means their LGPS benefits are not aggregated, these are generally administered as separate entitlements. Where a member takes a decision which means their LGPS benefits are aggregated, their combined record is generally administered as one period of membership. For example, where a member with 2009 Scheme membership has not had a disqualifying break in service and aggregates that record with another LGPS membership, they would retain their final salary link on the combined record. By contrast, if the same member decides not to aggregate their membership they would lose their final salary link on the non-aggregated record. These rules preserve the approach described above, through which local administrators are generally able to calculate separate benefits independently.

47. However, regulation 4 of the 2014 Transitional Regulations does not appear to include an aggregation requirement for underpin protection to apply. A strict interpretation of regulation 4(1)(a) therefore appears to suggest that where, for example, a member was:

a) active in the LGPS on 31st March 2012,

b) subsequently active in the 2015 Scheme in a separate employment without a disqualifying break in service, and

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<sup>11</sup> This does also require data sharing between administering authorities. However, the transfer of a record from one authority to another following a structured aggregation process is likely to be simpler and less prone to error than ad hoc sharing necessary to undertake pension calculations from time-to-time over a member's career.

<sup>12</sup> Where a member only has a deferred refund entitlement from a ceased period of LGPS membership, this must be aggregated with their subsequent LGPS membership and there is no choice (regulation 22(5) and (6) of the 2014 Regulations.

<sup>13</sup> Regulation 22(5)&(6) of the 2014 Regulations

c) the two records were not aggregated,

the underpin protection would still apply. In our view, this would be extremely difficult for scheme administrators to effectively administer in the coming decades. It is also inconsistent with the general approach adopted in relation to the administration of the LGPS, as described in paragraph 45, and as has been applied in relation to the final salary link.

48. Where there is no requirement to aggregate benefits, administrative difficulties would not only arise in determining who has underpin protection (as a previous record may be held in another fund), but also in actually undertaking the underpin comparison. One scenario that may be likely to occur more frequently, as a result of the significant expansion of the underpin proposed in this document, would be that:

- A member has two, un-aggregated LGPS records in separate funds:
- Membership one – active from 2011 to 2016, and
- Membership two – active from 2017 to 2022.
- As the member was in active service on 31 March 2012 and had 2015 Scheme membership, without a disqualifying break in service, they have underpin protection.
- On leaving membership one, the member would have an underpin date (calculated in the normal way).
- On leaving membership two, the member would also have an underpin date for their active membership in the scheme over the underpin period (for this member, 2015 to 2016 and 2017 to 2022). This would require the second fund to undertake an underpin comparison for the whole period using data they hold and data they need to obtain from the other fund (in relation to membership one).
- In this situation, it may also need to be considered whether any underpin addition arising should be split between the two funds and the two employers, so as to ensure liabilities are appropriately held.

49. This would clearly be extremely administratively complex and potentially increase risk that members do not receive their full entitlement. It is likely that other similar scenarios would also arise, and that the administrative complexities would continue for many years (as some members' underpin date may not take place for 30 or 40 years).

50. In light of this, we are proposing that regulation 4 of the 2014 Transitional Regulations is amended to make clear that members must meet the qualifying criteria in a single membership (a 'relevant Scheme membership' as defined in the proposed regulations) for underpin protection to apply. So, where a member has had a break in service, or a period of concurrent employment, their benefits must be aggregated for underpin protection to apply. The introduction of the concept of 'relevant scheme membership' has allowed us to define more clearly in the regulations the benefits administrators should be assessing when undertaking underpin calculations.

51. As our intention is for the revised underpin regulations to apply retrospectively, it is possible these changes will mean that some members of the LGPS who have underpin

protection at the moment (across separate LGPS memberships) would lose this. To ensure that no member is worse off as a result of our proposed amendments, we are proposing that active and deferred members are given an additional 12 months to elect to aggregate previous periods of LGPS membership, where such a decision would mean they have 'relevant Scheme membership' and therefore would have underpin protection. It is not proposed that this decision would be required for pensioner members, whose existing pensions would be unaffected by the aggregation changes outlined here. Circumstances where current pensioner members have underpin protection which is based on un-aggregated membership and they have received an addition to their pension as a result of their underpin protection are expected to be rare.

52. The additional 12 months would apply from the date the regulations come into force. This additional election period would not apply in respect of other periods of membership members may wish to aggregate, only to periods where a failure to aggregate would mean the member would not obtain underpin protection. Good communications with members in this situation will be crucial so that they understand whether this election period applies to them and the implications of the decision they are being asked to consider. As set out in paragraphs 131 and 132, SPA would plan to work closely with the Scheme Advisory Board on member communications to support the changes proposed in this paper.

53. The Public Service Pensions Act 2013 applies certain requirements where a responsible authority<sup>14</sup> proposes to make scheme regulations containing retrospective provisions which appear to the authority to have 'significant adverse effects in relation to the pension payable to or in respect of members of the scheme' (section 23(1))<sup>15</sup>. Specifically, where this is the case, the following applies:

- The authority must obtain the consent of persons who appear to the responsible authority to be likely to be affected by the provisions (sections 23(1) and (3)).
- The authority must lay a report before the Scottish Parliament (section 23(4)).
- The regulations become subject to the affirmative procedure and they have to be approved by a resolution of the Delegated Powers and Law Reform Committee of the Scottish Parliament (sections 24(1)(b) and 38).

54. We welcome stakeholders' views on whether the changes we describe in paragraphs 50 to 52 would have 'significant adverse effects' in relation to the pension payable to or in respect affected members. Whilst the changes would have retrospective application, the additional 12 month election period we are proposing would ensure that members have the opportunity to aggregate their pension records and obtain underpin protection if they wish. Members who wish to keep their records separate (perhaps as they have re-joined the LGPS in a lower paid post and do not want a final salary link) would also be able to retain this position by doing nothing.

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<sup>14</sup> Under section 2 and schedule 2 of the Public Service Pensions Act 2013, the Scottish Ministers are the responsible authority for the LGPS in Scotland.

<sup>15</sup> Certain requirements also apply under section 23(2) of the Public Service Pensions Act 2013 where the responsible authority proposes to make scheme regulations that are retrospective in nature, but which have significant adverse effects in other ways (for example, in relation to injury or compensation benefits). We are content that these provisions would not apply in respect of these proposed changes.

**Question 9 – Do you agree that for underpin protection to apply, members should meet the underpin qualifying criteria in a single scheme membership?**

**Question 10 – Do you agree with our proposal that certain active and deferred members should have an additional 12 month period to decide to aggregate previous LGPS benefits as a consequence of the proposed changes?**

**Question 11 – Do you consider that the proposals outlined in paragraphs 50 to 52 would have ‘significant adverse effects’ in relation to the pension payable to or in respect of affected members? (as described in section 23 of the Public Service Pensions Act 2013, ‘Achieving a fair and consistent underpin’)**

55. Alongside the changes necessary to address the discrimination found by the Courts, and the aggregation proposal above, we are also proposing some changes to underpin provisions to ensure that the underpin works effectively and consistently for all members.

56. Breaks in service of less than five years – the 2014 Transitional Regulations do not currently make clear whether it is permitted for the underpin to be re-calculated if a protected member leaves active service and returns without a disqualifying break in service (i.e. within five years). We propose that where a qualifying member leaves active service, re-joins within five years and aggregates their benefits, a further underpin comparison would be undertaken when they next reach their underpin date (i.e. leave active service or reach their 2009 Scheme NPA), using their final salary at the most recent date of leaving (and the results of the previous comparison disregarded). Taking this approach means that promotional pay increases that may apply where a qualifying member progresses in their career are taken into account in their underpin calculations. It also ensures younger members of the scheme have equivalent protection to their older colleagues (whose final salary benefit is based on their pay at the end of their career, after relevant promotions and pay rises). It may also benefit those qualifying members who are more likely to have a break in employment, such as women or those who have a disability. However, it is proposed that qualifying members who re-join the LGPS after their 2009 Scheme NPA would not have a further underpin date, even if they aggregate their previous pension rights. This is consistent with our general approach that underpin protection only provides protection until a member’s 2009 Scheme NPA.

57. **Early/Late retirement factors** - When a protected member leaves the scheme, the current underpin calculation does not take into account the impact of early/ late retirement factors which may mean the calculation does not correctly identify the scheme in which the member would receive the higher benefits. This situation arises because of differences in normal pension ages in the 2009 and 2015 Schemes, which may mean early and late retirement factors apply at different rates. We therefore propose that the revised underpin should include a ‘check’ to ensure that, at the point a member takes their benefits from the scheme, a member is still due to receive at least the pension they would have received under the 2009 Scheme, after the application of any early/late retirement factors. Further detail on how this will work is outlined in the next section regarding the two-stage process we intend to adopt.

58. **Survivor benefits** – it is not always clear how the survivor benefits provisions in the 2018 Regulations apply in relation to the underpin, and whether increases in benefits arising from the underpin should be included in the calculation of survivor benefits following the death of a member (from any status). We intend that the amended regulations will make

clear how the underpin applies in relation to survivor benefits. In general terms, it is our policy that where a member has an addition to their pension arising from the underpin, this should be taken into account in determining the value of relevant survivor benefits, where such benefits are based on the value of the member's pension. The next section of this paper outlines our policy on the underpin and survivor benefits in more detail.

59. Together and individually, the changes we describe in paragraphs 46 to 50 are intended to be beneficial for scheme members, and are intended to ensure that the revised underpin works for all members with underpin protection in a consistent and effective way.

**Question 12 – Do you have any comments on the proposed amendments described in paragraphs 56 to 58?**

### **6.3 A two-stage process**

60. Under current provisions, the underpin calculation takes place at a single point in time – a member's underpin date, being the earlier of the date a member leaves active service with an immediate entitlement to a pension, and the date they reach their 2009 Scheme normal retirement date. This has its advantages, such as in respect of administration. However, in the round, we now consider a two-stage underpin process would provide a more robust form of protection and the draft regulations attached propose such an approach. Under this, all members would have an 'underpin date' and an 'underpin crystallisation date':

- the purpose of the underpin date would be to provide for a provisional assessment of the underpin, comparing the member's 2015 Scheme benefits in a relevant scheme membership against the 2009 Scheme benefits they would have accrued over the same period, in respect of the same membership. The underpin date would take place at the earlier of the date the member:
  - leaves active service in a relevant scheme membership,
  - reaches their 2009 Scheme normal retirement age,
  - or dies.

Regardless of the outcome of this provisional comparison, there would be no adjustment to a member's pension at their underpin date. The purpose of the comparison at a member's underpin date would primarily be so that the member has early information on how the underpin may apply to them. This recognises that there may be many years between a qualifying member's underpin date and their underpin crystallisation date, when the final comparison is due to take place.

- The purpose of the underpin crystallisation date would be to provide for a final check at the point the member's benefits from the scheme are 'crystallised' (where the member takes their pension from the scheme). The check would be designed to ensure that members always receive at least the higher of the pension they would have been due from the 2015 Scheme and the 2009 Scheme, taking into account the impact of factors like early/ late retirement adjustments.

61. We consider that the use of a two-stage process will achieve the following:

- Fundamentally, it should give members greater confidence that the underpin process has given them the benefit that is better for their own personal situation, even if they take their benefits many years after they leave the scheme.
- By undertaking an initial comparison at a member's underpin date, it would give qualifying members information about how the underpin may apply to them at the earliest possible date, even if such calculations would only be provisional.
- It is more compatible with the revised underpin where members can re-join, aggregate their membership and have a further underpin date at a subsequent point in time. There will be no change to a member's active or deferred pension arising from the underpin, until the final underpin check at a member's underpin crystallisation date,
- It reflects the fact that for most members retiring on age grounds, early and/ or late retirement factors will apply in calculating their 2009 and/ or 2015 Scheme benefits. As these will not apply in the same way to a member's 2009 and 2015 Scheme entitlements (unless their 2009 Scheme normal retirement age is the same as their state pension age), a final check at the point benefits are paid is necessary to ensure the member is getting the higher benefit.

62. Further detail on the proposed two-stage process is contained in annex C.

### **Question 13 – Do you agree with the two-stage underpin process proposed?**

#### **Underpin period and final salary link**

63. As discussed earlier in the consultation (paragraphs 28 to 31), we propose that:

- the revised underpin be extended to provide underpin protection to all qualifying members for service from 1st April 2015 up to and including 31 March 2022, except where a member's underpin date is sooner.
- from 1 April 2022, all LGPS membership accrues on a career average basis, with no underpin,
- but to ensure that there is an equivalent level of protection between older and younger members, the comparison of 2009 Scheme and 2015 Scheme benefits would take place at a qualifying member's underpin date, even if the underpin period ends sooner. The revised underpin – application

64. This section describes how the revised underpin is intended to apply to protected members at different stages of their membership of the scheme, and at different life events.

#### **Whilst in active membership**

65. Whilst a qualifying member is in active service below their 2009 Scheme normal retirement age, they will remain a member of the 2015 Scheme. For the period up to 31 March 2022, active members will accrue underpin protection. From 1 April 2022, accrual will be on a career average basis alone, but active qualifying members will retain a final salary link in relation to their underpin protection. Each year, a member's annual benefit statement will include an estimate of how the underpin would have applied to them if they had left the

scheme at the end of the scheme year (i.e. as if their underpin date had been 31 March in that year). In these estimates, no account would be taken of actuarial adjustments relating to a member's age.

66. If a qualifying member remains in active service at their 2009 Scheme normal retirement date (normally 65), their underpin date will be triggered in relation to their relevant scheme membership, meaning a comparison of their 2009 Scheme and 2015 Scheme benefits (relating to the period from 1 April 2015 up to 31 March 2022, or their 2009 Scheme NPA if earlier) would be undertaken. This calculation would be based on the member's final pay as at their 2009 Scheme normal retirement age (taking into account appropriate lookback provisions where appropriate). The member would be informed of the results of this comparison, but also informed that a check at their underpin crystallisation date would be undertaken at the point they take their benefits to ensure they are getting the higher benefit. Final salary increases or reductions beyond the member's 2009 Scheme normal retirement age would not impact on the member's underpin protection.

### **Concurrent employments**

67. Underpin protection may apply to members who hold two or more active memberships of the scheme at the same time ('concurrent employments'). Under our proposals, underpin protection would be linked to specific scheme memberships, with members who have 'relevant scheme membership' having underpin protection on that membership. Relevant scheme membership applies where:

- a member was an active member on 31 March 2012,
- a member has been an active member of the 2015 Scheme, and
- they did not have a disqualifying break in service.

68. Relevant scheme membership would apply in the normal way where a qualifying member has concurrent employments – for example, if a member has two posts and meets the criteria in one but not the other, they would have underpin protection in the former post, but not the latter. Where a qualifying member leaves a concurrent post in which they had relevant scheme membership before reaching their 2009 Scheme NPA their underpin date would apply in relation to that employment. If they were to then aggregate that membership with their ongoing post, the member would have a further underpin date at the earlier of the date they leave that post or the date they reach their 2009 Scheme NPA.<sup>16</sup>

### **At date of leaving (without taking scheme benefits)**

69. Where a protected active member leaves the LGPS before their 2009 Scheme normal retirement age with a deferred or immediate entitlement to benefits, their underpin date would apply at their date of leaving. A provisional underpin comparison would be undertaken for the period up to 31 March 2022, or the member's date of leaving if earlier. The member would be informed of the results of this comparison, but also informed that a check at their

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<sup>16</sup> Under regulations 22(6) or (7) of the 2018 Regulations refer to automatic aggregation

underpin crystallisation date would be undertaken at the point they take their benefits to ensure they are getting the higher benefit.

### **Whilst a deferred member**

70. For deferred members who have had an underpin date after leaving active membership of the scheme, annual benefit statements sent to the member would include details of the provisional calculations undertaken at their underpin date. The results of these calculations would be adjusted to reflect cost of living changes between the member's underpin date and the date of their annual benefit statement.

### **Re-joiners**

71. Where a member who has had an underpin date in respect of a relevant scheme membership re-joins the scheme without a disqualifying break in service and aggregates their previous scheme membership with their active pension account<sup>17</sup>, they will retain continuing underpin protection for any service up to 31 March 2022. For service from April 2022 onwards, the member will retain a continuing final salary link in relation to their underpin protection (as well as in respect of their pre-2015 final salary membership). A further underpin date will occur at the date the member leaves active service or the date they reach their 2009 Scheme NPA.

### **Age retirement**

72. When a member takes voluntary payment of their benefits in a relevant scheme membership at any age between 55 and 75, their underpin crystallisation date will apply. This means that the final comparison of their benefits will be undertaken to determine whether the 2015 Scheme or 2009 Scheme benefits would be better. For qualifying members who retire from active status and do so before their 2009 Scheme normal retirement age, the member's underpin date will take place as at their date of leaving. The underpin crystallisation date will take place upon their pension coming into payment.

73. In the underpin crystallisation date calculation, the scheme administrator will take the provisional calculations from a qualifying member's underpin date and update these to take into account the effects of cost of living changes since the member's underpin date, as well as the impact of early/ late retirement factors. Where the final values shows that the member would have been better off under the 2009 Scheme, an addition will be made to the member's 2015 pension account. The member's total pension in that relevant scheme membership for the period from 1 April 2015 to 31 March 2022 would also be payable without any further actuarial adjustment relating to the member's age.

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<sup>17</sup> Under regulation 22 of the 2018 Regulations, all scheme members must have a pension account. Unless aggregated, members have multiple pension accounts for multiple periods of scheme membership.

## Ill-health retirement

74. For most protected members retiring on ill-health grounds, their date of leaving will be their underpin date<sup>18</sup>. As applies under the existing underpin provisions, the underpin calculation at a member's underpin date will take into account any enhancements that they may be due where they are receiving 'tier 1'<sup>19</sup> or 'tier 2'<sup>20</sup> benefits under regulation 37 of the 2014 Regulations, and compare these against the relevant enhancements that would have applied under the 2009 Scheme. This comparison of enhancements would apply up to the earlier of a member's 2009 Scheme normal retirement age and 31 March 2022.

75. A qualifying member's ill-health retirement date will be their underpin crystallisation date, in all cases. This calculation will take into account cost of living adjustments between the member's underpin date and their underpin crystallisation date for members retiring from deferred or deferred pensioner status. No account will be taken of actuarial reductions relating to a member's age as these do not apply in relation to ill-health retirements, but where the member is over their 2009 Scheme or 2015 Scheme NAP, the impact of actuarial increases will be considered.

76. We consider in most cases that a member will only have one underpin crystallisation date, although we would be grateful for views on this.

## Death benefits

77. Under existing scheme regulations, it is sometimes unclear how scheme death benefits interact with the underpin. Our policy intent is set out in this section, and we have aimed to make these points clearer in the draft regulations. These clarifications are essential to ensuring that the underpin works effectively and consistently.

78. **Death in service** - For a protected member in active service, their date of death will be their underpin date and their underpin crystallisation date. It is proposed that the underpin comparison will take into account the enhancements that apply under the 2009 and 2015 Scheme regulations in relation to deaths in service. This comparison of enhancements would apply up to the earliest of the member's 2009 Scheme normal retirement age and 31 March 2022. This would be a new addition to the underpin regulations, and would be consistent with the approach taken in relation to ill-health retirements (outlined above in paragraph 74).

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<sup>18</sup> With the exception of deferred or deferred pensioner members taking ill-health retirement under regulation 36 of the 2014 Regulations, and members who have previously reached their 2009 Scheme normal retirement age.

<sup>19</sup> Subject to other criteria that apply, tier 1 benefits apply to members retiring on ill-health grounds who are unlikely to be able to undertake gainful employment before their normal pension age (regulation 34(4)). Members receiving tier 1 benefits receive an adjustment to their pension equalling the full benefits they would have accrued between date of leaving and their 2015 Scheme normal pension age.

<sup>20</sup> Subject to other criteria that apply, tier 2 benefits apply to members retiring on ill-health grounds who are unlikely to be able to return to their previous occupation but likely to undertake gainful employment, before reaching their normal pension age (regulation 34(5)). Members receiving tier 2 benefits receive an adjustment to their pension equalling 25% of the benefits they would have accrued between date of leaving and their 2015 Scheme normal pension age.

79. No adjustment relating to the underpin would apply to a qualifying member's death grant, as death grants for active members are based on a member's pay, not their pension.

80. Where survivor benefits are payable following a death in service of a qualifying member, the underpin comparison will be based on the provisional calculations and will not take into account the impact of early or late retirement factors which do not apply in relation to survivor benefits. Where there is an addition (i.e. the 2009 Scheme benefit is higher based on the unadjusted values), this addition will apply in the calculation of the survivor's benefit, at the appropriate accrual rate for each type of survivor.

81. **Deaths from deferred status** - Where a qualifying member dies from deferred status, their underpin date will have already taken place (on the date the member left active service, or on their 2009 Scheme normal retirement date, if earlier). The day of the member's death will be their underpin crystallisation date.

82. Where survivor benefits are payable following a death from deferred status, the underpin comparison will be based on the provisional calculations and will not take into account the impact of early or late retirement factors which do not apply in relation to survivor benefits. Where there is an addition (i.e. the 2009 Scheme benefit is higher based on the unadjusted values), this addition will apply in the calculation of the survivor's benefit, at the appropriate accrual rate for each type of survivor.

83. Any addition arising from the provisional underpin calculation will also apply in the calculation of the death grant. For deferred members, a death grant applies at 5 times the annual rate of pension, without actuarial adjustment relating to the age of the member.

84. **Deaths from pensioner status** – Where a protected member dies from pensioner status, the underpin date and the underpin crystallisation date will already have taken place.

85. Where survivor benefits are payable following the death of a pensioner, the underpin comparison will be based on the provisional calculations undertaken at a qualifying member's underpin date and will not take into account the impact of early or late retirement factors which do not apply in relation to survivor benefits. Where there is an addition (i.e. the 2009 Scheme benefit is higher based on the unadjusted values), this addition will apply in the calculation of the survivor's benefit, at the appropriate accrual rate for each type of survivor.

86. Any addition arising from the provisional underpin calculation will also apply in the calculation of the death grant, where applicable. For pensioner members, a death grant applies at 10 times the annual rate of pension, reduced by the actual amount of pension the member received prior to their death and by any lump sum commutation.

### **Public Sector Transfer Club transfers**

87. The LGPS is a member of the Public Sector Transfer Club. The Club is an arrangement that facilitates the mobility of employment within the public sector by, for example, enabling employees to avoid the reduction in the value of their accrued pension that could otherwise occur as a result of changing employment. Final salary pension transferees are awarded a service credit that maintains the member's final salary link for the pension accrued in their previous scheme. CARE transferees are awarded a pension credit that continues the rate of in-service revaluation that was provided in the member's previous scheme. The intention

of the Club is that a member should not lose out as a result of changing employment within the public sector. Equally, the member should not receive benefits that are higher in value than if they had not changed employment.

88. Separately, the UK Government is consulting on proposals to remove the unlawful discrimination from the other main public service pension schemes. That consultation includes a section seeking views on how transfers under the Public Sector Transfer Club may work in relation to the remedy proposals outlined in that consultation. It sets out that one option would be for a member to make a choice between career average and final salary benefits at the date of transfer, so that only one set of scheme benefits for the remedy period needs to be considered for the transferred service.

89. The consultation also notes that considerations in the LGPS may be different, given the different nature of transitional protection in the LGPS and that we would consult on more detailed proposals in relation to Club transfers between the LGPS and the other public service pension schemes.

90. One approach, which would be consistent with the option outlined in the wider consultation, would be for the same principle to apply. This would mean the following:

- For Club transfers of protected service (accrued between April 2015 and March 2022) into the LGPS - the receiving LGPS fund would give the member the option of deciding whether they wanted to use the transfer to buy final salary membership or career average pension in relation to the transferred service. Quotations would be provided to help members make an informed choice.
- For Club transfers of protected service (accrued between April 2015 and March 2022) out of the LGPS – the receiving scheme administrator would give the member the option of deciding whether they wanted to use the transfer to buy final salary membership or career average pension in relation to the transferred service (which in the LGPS would have provided them with underpin protection). Quotations would be provided to help members make an informed choice.

91. It should be noted that, in certain situations, a transferring member might be at an advantage if the transitional protection could continue in their new scheme (for example, if members transferring into the LGPS were to obtain underpin protection for protected service they transfer in, or LGPS members transferring out were to obtain a choice in their new schemes). However, such an approach would likely lead to significant administrative complexity across the public sector.

92. We propose that, consistent with existing LGPS regulations that, where a member with final salary membership in another public service pension scheme transfers that membership into the LGPS, and they would have met the qualifying criteria for underpin protection in the LGPS had they been a member of the scheme, they would be granted underpin protection for their LGPS membership up to 31st March 2022. This would apply even if the initial transfer into the LGPS was not a Club transfer.

93. We welcome views from respondents on the options set out here. The final approach in relation to transfers within the Public Sector Transfer Club will be considered by the UK Government, taking into account the responses to this consultation along with those to their wider consultation.

## **Non-Club transfers**

94. Where a qualifying member transfers relevant scheme membership and the transfer is not a 'Club' transfer, a different approach is proposed. The date of transfer would be their underpin crystallisation date. In the draft regulations we propose the detailed requirements in relation to such cases will be contained in actuarial guidance issued by the Scottish Ministers. We propose that the actuarial guidance we issue will require the following approach:

1) Calculate Cash Equivalent Transfer Value (CETV) of the following:

a) the member's accrued rights,

b) the member's 'provisional assumed benefits' (see annex C), and

c) the member's 'provisional underpin amount' (see annex C).

2) Where c) is greater than b), add the difference between the two amounts to a) and that is the total CETV.

3) Where c) is not greater than b), just pay the CETV based on the member's accrued rights (i.e. the CETV calculated at a)).

95. This approach would be consistent with the general approach taken to calculating pension benefits under the underpin and should achieve a similar outcome.

96. Where a member with underpin protection has transferred in pension rights from another scheme that is not a public service pension scheme, the value of the transfer would not be taken into account for the purposes of the member's underpin calculations. This is the same as applies in relation to transfers under the existing underpin regulations.

## **Other ways of taking benefits**

97. **Flexible retirement** – Where a qualifying member makes an election to reduce their working hours or grade in an employment, with their employer's consent, that will be their underpin date, even though they remain in active employment after this date. As applies under the existing underpin provisions, no further underpin protection will apply after a member's date of flexible retirement. The underpin crystallisation date calculation, also undertaken at the point of a member's flexible retirement, will take into account the impacts of early and late retirement factors to determine which scheme benefit is better for the individual.

98. There is a question about the appropriate treatment of the underpin where a qualifying member takes 'partial' flexible retirement i.e. they do not take all the benefits they accrued prior to their flexible retirement date straight away. We propose that, in partial flexible retirement situations, where there is an addition to the member's pension arising from the underpin (i.e. because the 2009 Scheme benefit is higher), the amount of the addition given to the member at that point in time should be proportionate to the amount of the 2015 Scheme pension they are choosing to receive. For example, if a member is only receiving 20% of their 2015 Scheme pension upon flexibly retiring, they would only receive 20% of the underpin addition. The remainder would be payable at the point the member takes the rest of their benefits.

99. **Redundancy**<sup>21</sup> – Redundancy below a protected member’s 2009 Scheme NPA will trigger their underpin date. For members aged 55 or over, who have an immediate entitlement to their pension at point of redundancy, the date their redundancy pension commences will be their underpin crystallisation date. As actuarial reductions do not apply in this situation, no account should be taken of these in the final underpin comparison. However, actuarial increases, where the member is made redundant after their 2009 Scheme or 2015 Scheme normal pension age, should be considered in the usual way.

100. **Trivial commutation**<sup>22</sup> –

Under regulation 33 of the 2018 Regulations, members with small total pension rights can extinguish their future right to a pension from the scheme and receive a lump sum instead (‘trivial commutation’).

Under our proposals, qualifying members trivially commuting their pension will already have had their underpin date, as at their date of leaving the LGPS or reaching their 2009 Scheme NPA. If a qualifying member has not yet taken their pension, the date they trivially commute their benefits would be their underpin crystallisation date and the draft regulations propose the detailed requirements in relation to such cases will be contained in actuarial guidance issued by the Scottish Ministers. This is consistent with the general approach set out in the 2015 Regulations. We propose that the actuarial guidance we issue will require the following approach:

- 1) Calculate the trivial commutation sum due of the following:
  - a) the member’s total accrued rights,
  - b) the member’s ‘provisional assumed benefits’ (see annex C), and
  - c) the member’s ‘provisional underpin amount’ (see annex C).
- 2) Where c) is greater than b), add the difference between the two amounts to a) and that is the total sum due.
- 3) Where c) is not greater than b), just pay the trivial commutation sum based on the member’s accrued rights (i.e. the sum calculated at a)).

101. This approach would be consistent with the general approach taken to calculating pension benefits under the underpin and should achieve a similar outcome. Where a qualifying member who trivially commutes their benefits has already taken their pension from the LGPS (and had an underpin crystallisation date in doing so), there would be no further underpin calculations due at the point of the trivial commutation.

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<sup>21</sup> This paragraph also covers members leaving active membership of the LGPS on grounds of business efficiency.

<sup>22</sup> This paragraph also covers members taking benefits via any of the other means referred to in regulation 33 of the 2018 Regulations. Through these options, members with small total pension rights can extinguish their future right to a pension from the scheme and receive a lump sum instead. These payments are made at the discretion of administering authorities.

**Question 14 – Do you have any comments regarding the proposed approaches outlined above?**

**Question 15 – Do you consider there to be any notable omissions in our proposals on the changes to the underpin?**

## **6.4 Supplementary matters**

### **Annual benefit statements**

102. Pension schemes are vitally important workplace benefits. For many people contributing to a pension scheme, the annual benefit statement (ABS) is the main way that they receive updates on the value of their pension and when they will be able to receive it. Whilst it is true that information presented on an ABS about the underpin cannot provide certainty to a member on their underpin protection (in most cases, there will not be certainty until a member's underpin crystallisation date), we believe it is important that estimates are provided on a member's ABS if scheme regulations are amended in the manner outlined in this paper. Appropriate wording will need to be considered so that members have the information needed to understand how the underpin works and that the figures included in their statement are provisional, and may change. SPPA is willing to work with administering authorities and the scheme advisory board to propose standardised wording on underpin protection that all Scottish LGPS funds can use when issuing ABS to members.

103. For members who meet the underpin qualifying criteria and have relevant scheme membership, our draft regulations propose the following approach:

- That where a member is in active service below their 2009 Scheme NPA, their ABS should estimate the value of the underpin as if the end of the Scheme year<sup>23</sup> was their underpin date – including the provisional assumed benefits, the provisional underpin amount and any provisional guarantee amount.
- That where a member remains in active service beyond their 2009 Scheme normal retirement age, their ABS should include the provisional estimates from the member's underpin date, as updated to reflect cost of living changes to the end of the Scheme year.
- For deferred and deferred pensioner members, their ABS should include the provisional estimates from the member's underpin date, as updated to reflect cost of living changes to the end of the Scheme year.

**Question 16 – Do you agree that annual benefit statements should include information about a member's underpin protection?**

**Question 17 – Do you have any comments regarding how the underpin should be presented on annual benefit statements?**

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<sup>23</sup> Under Schedule 1 of the 2018 Regulations, a period of one year beginning with 1 April and ending with 31 March.

## Annual allowance

104. The annual allowance is the maximum amount of tax-relieved pension savings that can be accrued by an individual in a year. The standard annual allowance is currently £40,000, but for those on the highest incomes, it tapers down to a minimum level of £10,000 (from April 2016 to March 2020) and to £4,000 (from April 2020). For defined benefit pension schemes like the LGPS, liability for tax charges above the annual allowance is calculated using the value of pension accrued in a particular year. Where an individual's pension accrual in a single year exceeds the annual allowance, then a tax charge may be due on the amount accrued above the member's annual allowance to claw back the excess tax relief.

105. Whilst we would not expect a significant number of qualifying members to experience any change to their tax liability as a result of the proposals in this consultation document, it is important that underpin protection is considered for the purposes of determining a qualifying member's annual allowance.

106. LGPS regulations do not contain detailed provisions regarding the application of pensions tax to scheme benefits. Scheme administrators must follow the pensions tax framework as set out in the Finance Act 2004 and secondary legislation, as explained in HMRC's Pensions Tax Manual<sup>24</sup>.

Consistent with our approach generally, we do not plan to include in scheme regulations specific details regarding the tax treatment of the revised underpin.

107. We understand that, in accordance with guidance provided by the Local Government Association (LGA)<sup>25</sup>, LGPS administrators have generally been taking the following approach in relation to the current underpin and the annual allowance:

- Whilst a protected member is in active service and their underpin date has not yet occurred, no account has been taken of a member's underpin protection for the purposes of determining a member's pension input amount in a given pension input period. This reflects that, under existing scheme regulations, a member may only receive an addition to their pension at the point of their underpin date.
- In the year of a protected member's underpin date, any addition in the member's pension arising from the comparison undertaken at the member's underpin date would be considered for the purposes of determining a member's pension input amount in that pension input period.

108. Whilst interpretation and application of the requirements of the Finance Act 2004 is a matter for individual administrators to consider, we believe that this approach is correct and would remain so if our proposals were to be implemented in scheme regulations. As described in paragraphs 60 and 61, we propose that the underpin moves to a 'two stage process'. Under our proposals, a member's underpin protection will only result in a change to their pension entitlement at their 'underpin crystallisation date' and it would be this pension

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<sup>24</sup> <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual>

<sup>25</sup> 'The Underpin' technical guide, <http://scotlgpsregs.org/resources/guidesetc.php>

input period that the underpin should first be given consideration for the purposes of the annual allowance. As there would be no change to a member's pension entitlement at the point of a member's underpin date, so the underpin should not be considered for annual allowance purposes in that pension input period<sup>26</sup>.

109. We recognise that there may be circumstances where this approach means that a qualifying member has a higher pension input amount in the year of their underpin crystallisation date than if the potential value of the underpin is considered on an annual basis whilst a qualifying member remains in active membership. This may particularly be the case for qualifying members who have a relatively low career average pension for the years from 1 April 2015 to 31 March 2022, but a relatively high final salary pension over the same period. This may occur where a qualifying member is at an early stage of their career now, but goes on to be a high-earner in the future. We would appreciate views from stakeholders on the potential likelihood of this issue arising, the scale of the issue and how any impacts might be mitigated, if appropriate.

**Question 18 – Do you have any comments on the potential issue identified in paragraph 109?**

## **6.5 Public sector equality duty**

110. The Scottish Public Pensions Agency (SPPA) has analysed the proposals set out in this consultation document to fulfil the requirements of the Public Sector Equality Duty (PSED)<sup>27</sup> as set out in section 149 of the Equality Act 2010. This requires public authorities in Scotland to pay due regard to the need to:

- 1) eliminate discrimination, harassment and victimisation and any other conduct prohibited by or under the Act
- 2) advance equality of opportunity between persons who share a relevant protected characteristic and persons who do not share it
- 3) foster good relations between persons who share a relevant protected characteristic and persons who do not share it.

### **Data**

111. In undertaking our assessment of the equalities impacts of our proposals, we have drawn upon analysis provided to us by GAD. The analysis particularly looks at the protected characteristics of age and sex and is based on membership data supplied to GAD by LGPS administrators as at 31 March 2017. The following points should be borne in mind when considering the analysis:

- GAD's analysis has principally considered those who would benefit from the proposals outlined in this consultation. Members who already have underpin protection under existing provisions (being those aged 62 and older on 31st March 2017 who were aged at least 55 on 1 April 2012) have not been considered directly.

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<sup>26</sup> Except where the member's underpin crystallisation date occurs in the same pension input period.

<sup>27</sup> [https://www.equalityhumanrights.com/sites/default/files/redraft\\_of\\_psd\\_tech\\_guidance\\_-\\_v6sc.pdf](https://www.equalityhumanrights.com/sites/default/files/redraft_of_psd_tech_guidance_-_v6sc.pdf)

- GAD’s analysis is based on active membership records totalling 214,617 from data as at 1 April 2017. The analysis has been conducted on a per-member basis, meaning additional records where members have more than one active employment have been removed.
- The proportion of the qualifying membership which is eventually likely to be better off as a result of underpin protection is heavily influenced by the rate of future pay growth in the LGPS. Consistent with the assumption used for the 2016 valuations of public service pension schemes, the long-term annual future pay growth assumption used is CPI + 2.2%.
- The analysis is based on active membership in the LGPS, as at 31 March 2017. Under our proposals, the proposed changes to the underpin would be backdated to 1st April 2015. We would therefore expect that a number of additional members not included in the analysis would benefit from our proposals. However, we do not anticipate this limitation would significantly change the results of the analysis.
- The analysis is based on an “average” member at each particular age. Allowing for variations in individual members’ future service or salary progression could produce different figures.

112. Limited data specific to the LGPS in Scotland is available in relation to other protected characteristics.

## **Age**

113. The proposals outlined here are intended to remove age discrimination, which had been found to be unlawful in the firefighters’ and judicial pension schemes, from the LGPS rules governing the underpin. We consider that the changes proposed will significantly reduce differential impacts in how the underpin applies based on a member’s age, by removing the age-related qualifying criteria found to be unlawful by the Courts.

114. Based on analysis undertaken by GAD on active membership data for the LGPS as at 31 March 2017, we anticipate that some differences in how the revised underpin would apply to members of different age groups would remain. These are described below, along with our assessment of these differences.

115. Qualification for the underpin – GAD’s analysis shows that older active members on 31 March 2017 would be more likely to qualify for the revised underpin than younger active members. This is principally because of our proposal that the 31st March 2012 qualifying date for underpin protection is retained. The proportion of members active in the scheme as at 31 March 2017 who had been members of the scheme on 31st March 2012 is lower for younger members, as experience shows they have a higher withdrawal rate from active scheme membership. We consider that members joining the LGPS after 31st March 2012 do not need to be provided with underpin protection. Members joining the LGPS after 31 March 2012 fall into two groups:

a) members who joined after 1st April 2015 when the LGPS had already reformed to a career average structure, and

b) members who joined between 1st April 2012 and 31st March 2015, who joined the LGPS when it was still a final salary scheme, but when a well-publicised reform process was already underway.

116. In relation to both groups, it is the Scottish Ministers' view that providing them with underpin protection would not be appropriate. Transitional protection, as applied across public service pension schemes, was always designed to help members with the transition from the old scheme designs to the new (in the LGPS, mainly in relation to the move from a final salary to a career average structure). Members who joined after 31st March 2012 will have joined the LGPS when either it had already transitioned to the career average structure, or when it was well publicised that the LGPS benefits were reforming.

117. Members who benefit from the underpin – GAD's analysis shows that active members between the ages of 41 and 53 would be more likely to benefit from the revised underpin (i.e. where the calculated final salary benefit is higher than the calculated career average benefit) than both their younger and older colleagues. This reflects previous experience and future expectation that:

- this group are more likely than older colleagues to experience the pay progression that would make the final salary benefit higher over the underpin period (bearing in mind that the career average accrual rate (1/49) is better than the final salary accrual rate (1/60) so above inflation pay increases are needed for the underpin to lead to an increase in pension), and
- this group are more likely than younger colleagues to remain in active membership and receive the pay progression necessary for the underpin to result in an addition to their pension. Younger members are estimated to have a higher voluntary withdrawal rate than older members, and so would be less likely to remain in the LGPS until such time as they have the pay increases for the final salary benefit to be higher.

118. These differential impacts reflect the fact that final salary schemes typically benefit members with particular career paths (for example, they usually favour high-earners with long service). Scottish Ministers propose to move all local government pensions accrual to a career average basis, without underpin protection, from April 2022. to apply a more equitable system to all future service.

## **Sex**

119. In relation to sex, GAD's analysis shows that broadly the proportion of men and women who would qualify for the revised underpin protection and benefit from that protection matches the profile of the scheme. As at 31st March 2017:

- 66% of scheme members were female, and 34% male
- 65% of the scheme members who were estimated to qualify for the revised underpin protection were female, and 35% male
- 64% of the scheme members who were estimated to benefit from the revised underpin were female, and 36% male

120. Proportionally, GAD's assessment is that men would be marginally more likely to qualify for the revised underpin and to benefit to a greater extent from underpin protection than women. This reflects the fact that, in line with previous scheme experience, the average male LGPS member would be expected to have higher salary progression than the average woman and that women are generally expected to have higher voluntary withdrawal rates than men. Members with longer scheme membership and with higher salary progression would be more likely to receive an addition to their pension through the underpin (i.e. where the final salary benefit is higher).

### **Other protected characteristics**

121. As noted in paragraph 112, there is limited data specific to the LGPS in Scotland available in relation to other protected characteristics. However, we have considered wider data from the LF (Q1 2020) and the APS (2019) in looking at these characteristics. The LFS breaks down results to public sector level, which we have used as a proxy for LGPS membership for ethnicity, disability and marital status. For religion, the APS has been used as a proxy for the public service pension schemes as it also includes a public sector breakdown.

122. Whilst these data sets show some differences in the demographic make-up of the UK population generally and the public sector workforce, we do not consider that the changes to underpin protection proposed in the consultation will result in any differential impact to LGPS members with the following protected characteristics: disability, ethnicity, religion or belief, pregnancy and maternity, sexual orientation and marriage/civil partnership.

123. Data on sexual orientation, gender reassignment, pregnancy and maternity is not available. However, we expect there to be no differential impacts in relation to these groups as they won't be explicitly affected by any changes to transitional arrangements.

### **Next steps**

124. Whilst we have detailed data on the protected characteristics of age and sex in relation to the LGPS membership, we are aware that our analysis of the impacts on other protected characteristics may be limited as it has not been based on local government specific data. We welcome suggestions from stakeholders of other data sets that may be available that may help us better understand the impacts on the LGPS membership more specifically.

125. We welcome views from stakeholders on our analysis. These views will be considered in determining how to proceed following the consultation exercise. The potential equalities impacts of our proposals will be kept under review. A further equalities impact assessment will be undertaken following the consultation at the appropriate juncture.

**Question 19 – Do the proposals contained in this consultation adequately address the discrimination found in the *McCloud* and *Sargeant* cases?**

**Question 20 – Do you agree with our equalities impact assessment?**

**Question 21 - Are you aware of additional data sets that would help assess the potential impacts of the proposed changes on the LGPS membership, in particular for the protected characteristics not covered by the GAD analysis (age and sex)?**

**Question 22 – Are there other comments or observations on equalities impacts you would wish to make?**

## **7. Implementation and impacts**

126 Following the closure of the consultation, we will consider the consultation responses received in detail and determine how best to proceed. Upon reaching a remedy solution which we are content will adequately resolve the discrimination and which will work effectively for all key stakeholders, our intention is to make scheme regulations at the earliest opportunity, recognising the unlawful discrimination which currently exists in scheme rules. Making regulations at an early opportunity will also maximise the time available to administrators and their software suppliers to implement the changes that will be necessary.

127. The draft regulations at **annex B** have been prepared based on existing powers under the Public Service Pensions Act 2013. As noted in the wider UK Government consultation on removing the unlawful age discrimination from public service pension schemes, the UK Government also intends to bring forward new primary legislation regarding public service pensions.

128. We recognise that in the period between now and scheme regulations being amended, some members of the scheme who would be due to benefit from the changes outlined in this paper will crystallise scheme benefits. This will include voluntary age retirements, as well as ill-health retirements, redundancies and transfers. There will also be dependants of those scheme members who sadly die before changes are implemented. In respect of all such cases, we would expect the retrospective application of our proposed amending regulations to ensure that, overall, members and their dependents would get the full benefit of the revised underpin.

### **7.1 Communications**

129. Member communications in relation to the proposals outlined here will be vitally important to ensure members understand what underpin protection is and how it may or may not apply to them. This is particularly important due to the complexities of the underpin. The two-stage process we describe in paragraphs 60 and 61 is designed to protect members and to provide clarity, but it is important its purpose is well explained, so that members understand that they may have an addition to their pension arising from the underpin, even if there was not an addition at their underpin date. Equally, qualifying members should be aware that the benefits payable from the 2015 Scheme are very good, and, for many, underpin protection will not result in an increase to their pension entitlement.

130. Achieving good member communications, and deciding on the appropriate medium for those communications, will require input from stakeholders across the LGPS, including administering authorities, employers and trade unions. We would be grateful for your input on how best to accomplish this.

**Question 23 – What principles should be adopted to help members understand the implications of the proposals outlined in this paper?**

131. We are conscious that the proposals outlined in this consultation paper would require significant changes to administration practices and systems. Amongst other matters, local

administrators would need to consider the appropriate prioritisation of cases after amendments to regulations are made. Recognising that the LGPS is a single scheme, albeit locally administered, we are supportive of there being consistency across the scheme in respect of prioritisation and hope to work with the sector and the Scheme Advisory Board to agree a standard approach.

132. Prioritisation decisions will be influenced by the fact that the revised underpin would have retrospective effect to April 2015, meaning that some members would already be in receipt of pensions that need to be re-calculated in line with the new regulations.

133. A major challenge of implementing the changes proposed would apply in respect of obtaining additional data from employers for members who are newly benefitting from underpin protection. Under the 2015 Scheme, certain members' data which was required for administering the 2009 Scheme (such as details of members' working hours, and breaks in service) are not required for calculating member benefits. To administer the revised underpin, administrators would need to obtain this data for protected members for the period back to April 2015.

This would be a highly significant bulk exercise for the scheme's 11 administering authorities and their employers. Particular challenges are likely to arise where employers have changed their payroll provider, and the data isn't stored in current systems.

**Question 24 – Do you have any comments to make on the administrative impacts of the proposals outlined in this paper?**

**Question 25 – What principles should be adopted in determining how to prioritise cases?**

**Question 26 – Are there material ways in which the proposals could be simplified to ease the impacts on employers, software systems and scheme administrators?**

134. We will continue working closely with the scheme advisory board after the closure of the consultation as the sector prepares for the potential changes to scheme regulations. In particular, we intend to ask that the scheme advisory board consider what guidance may be necessary to help administrators implement the proposed changes, and we are grateful for respondents' views on this.

135. Guidance would also help support a consistent approach across the LGPS which would be desirable, in particular on matters like prioritisation. It would also potentially help on the complex issues connected with the fact that scheme employers would need to provide administrators with membership data going back to April 2015.

**Question 27 – What issues should be covered in administrative guidance issued by the Scheme Advisory Board, in particular regarding the potential additional data requirements that would apply to employers?**

**Question 28 – On what matters should there be a consistent approach to implementation of the changes proposed?**

## 7.2 Costs

136. The LGPS is a locally administered, funded scheme with funding valuations to determine employer contribution rates taking place every three years. The next funding valuation is due based on information up to 31<sup>st</sup> March 2020<sup>28</sup>. Employer contribution rates are, in most cases, determined on an individual employer basis, and take into account a number of factors, some related to the individual employer (such as membership demographics) and some related to the fund more broad (such as the performance of fund investments since the previous valuation).

137. As a result of this backdrop, it is not possible to say precisely how these changes would impact employer contribution rates at future valuations. However, the proposals in this paper can only lead to improvement in scheme benefits for members and it is therefore likely that there will be an upward cost pressure for employers. Where any fund or employer would like to understand how these proposals may affect their own position, they should speak to their fund actuary.

138. At a scheme level, costing estimates have been provided by the scheme actuary<sup>29</sup>, the Government Actuary's Department, based on data provided by LGPS funds for the 2017 valuation. Assuming future member experience replicates the average 2017 scheme valuation assumptions the future cost to LGPS employers could be around £355 million in the coming decades.

139. The costs are sensitive to both individual member experience and future pay. Predicting whether the underpin becomes valuable in the future depends heavily on assumptions on long-term future pay growth trends. In this estimate, we have used the [2017 valuation assumption](#) that annual long-term pay growth is CPI + 2.2%. However, if long-term pay growth in the LGPS is lower than this, the costs may be lower (and vice versa).

140. The UK Government cost control mechanism was paused in February 2019 given the uncertainty arising from the McCloud judgment. The UK Government has made a separate announcement on the cost control mechanism.

**Question 29 – Do you have any comments regarding the potential costs of McCloud remedy?**

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<sup>28</sup> Under regulation 60 of the 2018 Regulations. In 2020, we consulted on potential changes to the funding valuation cycle - <https://www.gov.uk/government/consultations/local-government-pension-scheme-changes-to-the-local-valuation-cycle-and-management-of-employer-risk>. A formal Scottish Government response outlining our plans in relation to the LGPS valuation cycle has yet to be published

<sup>29</sup> As appointed under regulation 100 of the 2018 Regulations

## 7.3 About this consultation

Comments are invited on the draft regulations. All respondents should be aware that the Scottish Government is subject to the provisions of the Freedom of Information (Scotland) Act 2002 and would therefore have to consider any request made to it under the Act for information relating to responses made to this consultation exercise.

A Respondent Information Form is also provided at Annex D for completion and return to SPPA. Using this form will simplify our task of collating responses and will make the process more efficient.

### Next steps in the process

Where respondents have given permission for their response to be made public these will be made available to the public on the Scottish Public Pensions Agency website after the consultation period. We will check all responses where agreement to publish has been given for any potentially defamatory material before publishing.

Once the consultation has closed we will consider all responses when preparing the final Regulations.

### Completed information

The completed Respondent Information Form and any comments you wish to make should be returned, by (add date TBA) to Roddy MacLeod, Policy Officer, Scottish Public Pension Agency, 7 Tweedside Park, Tweedbank, Galashiels TD1 3TE.

Copies of the proposals and Respondent Information form can be accessed on the Local Government Pension Scheme pages of the SPPA website under 'Scheme Governance and Legislation'. Your responses and completed Respondent Information form can be sent electronically to [roddy.macleod@gov.scot](mailto:roddy.macleod@gov.scot). If you would prefer to have a set of these consultation documents and draft regulations sent to you in hard copy, please contact [roddy.macleod@gov.scot](mailto:roddy.macleod@gov.scot) to request a set.

### Comments and complaints

Information on the Scottish Government Consultation Process can be found in Annex D of this letter. If you have any comments about how this consultation exercise has been conducted, please contact Iain Coltman by e-mail to [iain.coltman@gov.scot](mailto:iain.coltman@gov.scot).

**Your opinions are valuable to us. Thank you for taking the time to read this document and respond.**