

Pension Fund Committee

28 January 2008



Third-tier ill health benefits

Report of Stuart Crowe, County Treasurer

Purpose of the Report

- 1 The purpose of the report is to advise Members of a recent consultation exercise on a proposal to introduce a third level of ill health benefit into the new-look Local Government Pension Scheme (LGPS),

Background

- 2 The regulations for the new-look LGPS coming into force from 1 April 2008 include two different levels or tiers of ill health benefit. The original intention was for a third tier of ill health benefit to be payable outside of the Scheme as discretionary payment or payments made from an employer's revenue budget.
- 3 On 21 November 2007 Communities and Local Government (CLG) issued a consultation document setting out a proposal to include the third tier of ill health benefits within the Scheme. Responses were required by 12 January 2008. A copy of the consultation letter is included at Appendix A and the Council's response is included at Appendix B.

The proposed revised ill health arrangements

- 4 Under the new-look LGPS to qualify for ill health benefits an individual needs to meet the following criteria:
 - They must have at least 2 years scheme membership
 - Their employment must have been terminated because they are permanently incapable through ill health of carrying out their own job
 - They must have a reduced likelihood of obtaining a job elsewhere
- 5 If they are then judged to have no reasonable prospect of getting gainful employment before age 65 they will be entitled to the first-tier of ill health benefits and get enhanced membership of full prospective service to age 65.
- 6 If they are judged to be unable to obtain gainful employment within a reasonable period of leaving but probably able to before age 65 they will be entitled to the second-tier of ill health benefits and get enhanced membership of 50% of prospective service to age 65.
- 7 Under the latest proposal if they are then judged to be able to obtain gainful employment quite soon after leaving they will be entitled to the third-tier of ill health benefits. This is access to unreduced benefits based on service earned in the Scheme with no enhancements.

- 8 The proposals also suggest a review system where those awarded third-tier benefits would be monitored to see whether they obtain gainful employment and their benefit could be stopped if they did.

Council's response

- 9 The consultation response sets out our preferred approach in order of preference as follows:
- a) Our preferred approach would be for there not to be a third tier of ill health benefits. The proposed two tiers provide reasonable protection for members and are more generous than the existing LGPS regulations.
 - b) If there has to be a third tier of ill-health provision our preference is for it to be kept out of the scheme and to be a one-off discretionary compensation payment made from an employer's revenue account.
 - c) If these two approaches are not acceptable to all parties, our third preference would be for the third tier to be pension paid for a set number of years (2 or 3) followed by a regular medical review to determine continuing eligibility.

Recommendation

- 10 Members are asked to note this report.

Contact: Nick Orton Tel: 0191 383 4429



21 November 2007

Our ref: Third tier ill health provision

To: addressees below

Dear Colleague,

Draft proposals to amend Regulation 20 of the Local Government Pension Scheme (Benefits, Membership and Contributions) Regulations 2007 (*the benefit regulations*) to provide a third tier of ill health provision.

1. With Ministers' agreement, draft proposals for a third tier of ill health provision in the Local Government Pension Scheme (Benefits, Membership and Contributions) Regulations 2007 (*the benefit regulations*) are set out below. This consultation also seeks comments on proposals to reduce the qualifying period for ill health benefits and clarify certain sections of Regulation 20 and 31. It is intended that these Regulations take effect from 1 April 2008.

2. Your comments are invited by 12 January 2008. Consultees who wish to discuss the proposals are invited to get in touch without delay to allow any meetings to take place within the consultation period.

Draft proposals

3. The proposed measures would provide local authority employers with powers to award benefits for those scheme members who are permanently incapable of their local authority employment but are judged by an occupational health practitioner to be capable of gainful employment quite soon after leaving that employment.

4. It remains the Government's policy that any proposal remains affordable and fair within the cost envelope of 19.5% of payroll for the revised new look LGPS which comes into effect in April 2008, and that the third tier of ill health provision equates to some 0.1% of payroll.

5. The benefit improvement being proposed involves providing a pension based on the annual equivalent of the member's accrued pension benefits at the point of leaving employment. Payments would continue provided that other gainful employment was not found but would cease when it was. It will be necessary to monitor the third tier's practical application because the recipient is expected to be able to obtain alternative employment within a reasonable period. We are proposing that the recipient should notify the relevant administering authority, giving details, if they obtain employment. The administering authority would have powers to then suspend the payment of the benefit if gainful employment had been obtained.

6. The administering authority will have powers to ask the recipient, after the benefit has been in payment for a period (for example, a year) if their circumstances have changed. If it is found that gainful employment has been obtained, the administering authority will have powers to suspend the benefit. Comments are welcomed on how long the period should be before a review is undertaken.

7. When benefits are stopped, the recipient would become a pensioner member with suspended benefits.

8. When benefits are suspended, and should a 3rd tier member subsequently become an active member of the LGPS, the earlier period of membership which resulted in ill health benefits will not be aggregated with the later active membership. Two pension payments would, ultimately, be payable in these circumstances.

Monitoring of the proposed provision

9. The effectiveness and practical application of the new tiered ill health provisions will require careful monitoring. To achieve this, CLG is recommending the setting up of an ill health monitoring group as a sub group of the Policy Review Group.

Statutory Guidance

10. Statutory guidance will be prepared for practitioners when the entire framework for ill health retirement provisions are finalised.

Technical amendments to Reg 20 and Reg 31

11. Your comments are also invited on proposals to make changes to Regulation 20 and Regulation 31 of Local Government Pension Scheme (Benefits, Membership and Contributions) Regulations 2007. The proposal is to reduce the qualifying period from 2 years to 3 months as it is considered that some ill health retirees with membership more than 3 months but less than 2 year's may be unable to qualify for ill health benefits and that was not the intention of the benefit regulations.

12. Three technical amendments are also proposed to clarify the intention in Regulation 20 (5) regarding protections for those members aged 45 as at 31 March 2008 and 20 (6) regarding the certification by an Independent Occupational Health Practitioner (IOHP), and Regulation 31 regarding certification by an IOHP in respect of early payment of pension for deferred members.

Draft Statutory Instrument

13. In the absence of a draft SI, a detailed explanation of the proposals is provided at Annex A. A draft statutory instrument will be discussed with key stakeholders as soon as it becomes available.

Responses

14. Your comments should be sent by 12 January 2008 to Lynda Jones, Local Government and Firefighters' Pensions Schemes Division, Department for Communities and Local Government, Zone 2/F7, Ashdown House, 123 Victoria Street, London, SW1E 6DE. Electronic responses can be sent to lynda.jones@communities.gsi.gov.uk.

Yours sincerely,

Lynda Jones
Head of Branch LGFPS1

Annex A

Local Government Pensions Scheme (LGPS) -3rd tier ill health provisions

Background

1. The Local Government Pension Scheme (Benefits, Membership and Contributions) Regulations 2007 make provision for an ill health retirement pension where a LGPS member is judged permanently incapable of their local government employment and either has no reasonable prospect of obtaining gainful employment before normal retirement age *or* is judged permanently incapable of their local government employment but, although judged unable to obtain gainful employment within a reasonable period of leaving local government employment, there is a likelihood that they will be able to obtain gainful employment before normal retirement age. These provisions have been referred to as the 1st or 2nd tiers.

Draft proposals - the 3rd tier

2. The proposed measures would provide local authority employers with powers to award benefits for those scheme members who are permanently incapable of their local authority employment but are judged by an occupational health practitioner to be capable of gainful employment quite soon after leaving that employment.

It is proposed that the benefit should be framed as follows:

3. a) A pension of an amount equivalent to the members accrued benefits at the point of ill health retirement with a qualifying period of three months membership (see h) below).

b) An employer should only make a determination where there is certification by an independent registered medical practitioner qualified in occupational health medicine (IOHP) that the member is permanently incapable of discharging efficiently the duties of the relevant local government employment because of ill-health or infirmity of mind or body and the certifying IOHP is of the opinion that the member is capable of gainful employment quite soon after leaving that employment.

c) the ex-employee will be required to notify the paying authority when employment is found providing details, including how many hours, of that employment and the employer would then suspend payments if this was gainful employment.

d) when benefits have been in payment for a period (it is thought that this should be after one year) the paying authority should ask the recipient if there has been a change in circumstances and where it is found that the recipient has obtained gainful employment, the benefit will be suspended.

e) When benefits are suspended as alternative employment is being undertaken (following either the beneficiary's notification or ex-employer's enquiry) the beneficiary will become a pensioner member with suspended benefits.

f) when benefits are suspended, and if the 3rd tier member subsequently becomes an active member of the LGPS, the earlier period of membership which resulted in ill health benefits will not be aggregated with the later active membership.

g) the following table sets out how the three tiers of ill health would apply:

	Those eligible	Terms	Protections	Review
1 st tier	those employees who leave because they are permanently incapable of their local authority employment but are not likely to work before normal retirement age (NRA),	100% enhancement to accrued retirement benefits	Those aged 45 before 1 April 2008 will receive the greater of the amount under either 2007 or 1997 ill health Regulations	NO
2 nd tier	those employees permanently incapable of their current employment but are likely to be capable of work before NRA.	25% enhancement to accrued retirement benefits	Those aged 45 before 1 April 2008 will receive the greater of the amount under either 2007 or 1997 ill health Regulations	NO
3 rd tier	those assessed as being permanently incapable of their current employment but medical evidence indicates that gainful employment could be obtained at the point of leaving.	Accrued retirement benefits at the point of leaving but payments can be suspended when gainful employment is obtained	Not applicable	YES

Other proposed changes to Regulation 20

h) The qualifying period will be amended to be the same as regulation 5 of the *benefit regulations*.

i) 20 (5) this sub section is to be clarified to read “*in the case of a person who is a member before 1st April 2008 who has attained the age of 45 before that date and where the period to be added under paragraph (3)(b) is less than the period that would have been added had regulation 28 of the 1997 Regulations applied, then his benefits are increased by adding the latter period*”.

j) 20 (6) this sub section is to be clarified to read “*Before making a determination under this regulation, an authority must obtain a certificate from an independent registered medical practitioner qualified in occupational health medicine as to whether in his opinion the member is permanently incapable of discharging efficiently the duties of the relevant local government employment because of ill-health or infirmity of mind or body and, if so, whether that condition is likely to prevent the member from carrying out other gainful employment within a reasonable time of leaving local government employment or, as the case may be, before reaching his normal retirement age.*”

Proposed change to Regulation 31

k) This regulation will be amended to clarify the need for certification by an independent occupation health practitioner.

(0191) 383 4429

nick.orton@durham.gov.uk
Nick Orton

11 January 2008

Lynda Jones
By email

Dear Ms Jones

**Local Government Pension Scheme Regulations 1997
Draft proposals to amend Regulation 20 of the Local Government Pension Scheme
(Benefits, Membership and Contributions) Regulations 2007 (*the benefit regulations*)
to provide a third tier of ill health provision.
Consultation response on behalf of Durham County Council**

I am writing in response to your letter dated 21 November 2007, which asked for comments on draft proposals to amend Regulation 20 of the Local Government Pension Scheme (Benefits, Membership and Contributions) Regulations 2007 (*the benefit regulations*) to provide a third tier of ill health provision. We welcome the opportunity to comment on this guidance.

Durham County Council is the largest local authority in the North East of England with a population of 499,800. It is also a major employer within the Local Government Pension Scheme with over 10,000 current employees contributing to the Scheme. The Council also has a key role to play as an administering authority within the Local Government Pension Scheme and is responsible for the administration (including investments) of the Durham County Council Pension Fund.

Please find enclosed a response sent on behalf of Durham County Council.

I hope this is useful, please contact me if you need to discuss any of the issues raised in this response.

Yours sincerely

Stuart Crowe
County Treasurer

**Local Government Pension Scheme Regulations 1997
Draft proposals to amend Regulation 20 of the Local Government Pension Scheme
(Benefits, Membership and Contributions) Regulations 2007 (*the benefit regulations*)
to provide a third tier of ill health provision.**

**Consultation response on behalf of Durham County Council as an Administering
Authority.**

General comments

Cost implications

The draft proposal introduces a third tier of ill-health benefits into the new-look LGPS where previous proposals had suggested that this third tier would be a discretionary benefit payable from employers' revenue accounts and outside of the Scheme. Including the third tier within the Scheme would mean the cost would not be immediately met by the employer, however the payment would not be discretionary and so employers would not control the costs.

Under the proposed third tier an un-enhanced, unreduced pension would be payable to all those judged permanently incapable through ill health of carrying out their current job but capable of obtaining gainful employment "quite soon". This could significantly increase the number of individuals being paid ill-health benefits and so increase employer contribution rates in the long term. Our actuary has recently commented that the 31 March 2007 valuation for the Fund shows a significantly lower level of ill-health pensions being awarded than was anticipated, and this has helped to reduce employer costs. There is a danger that these proposals could undo the good work that has been done over the years in controlling ill-health retirements (and their associated costs) within the LGPS.

Difficulties for medical practitioners

All three tiers require an independent registered medical practitioner qualified in occupational health medicine (IOHP) to certify that the member is permanently incapable of discharging efficiently the duties of their employment because of ill-health or infirmity of mind or body. The IOHP then has to determine the likely period before which the member will be able to obtain "gainful employment" currently defined as "paid employment for not less than 30 hours in each week for a period of not less than 12 months". Clear guidance will be required to assist IOHPs in deciding which category of ill-health benefits a member will be entitled to. Our Occupational Health Doctor who also acts as an IOHP for other employers has commented:

"I think the difference between tiers 2 and 3 will be socioeconomic - not medical. It is rare for someone to be completely incapacitated for all work. Consequently the limiting factor to rejoining the workforce will be the availability of suitable work, not normally the nature of the medical condition itself. Asking a doctor to make the determination on likely duration of disengagement with the workplace is not altogether rational.

The process as written may save some money but may also act as a deterrent to return to the workplace for some members (if you are a middle aged former manual worker would it be rational to give up a regular pension for poorly paid insecure work?).

The timing of pension decisions in relation to termination of service needs clarifying otherwise speculative applications will become the norm again.

Guidance on the terminology used is required.”

Monitoring re-employment

The draft proposals invite individuals to manipulate the system. If the suspension of the third tier pension is to be based on whether an individual actually obtains gainful employment, there is a clear incentive for individuals to avoid this by, for example, taking up employment at 29 hours a week. If monitoring and suspension is to be used individuals should be assessed as to their capability of getting gainful employment rather than their actual success or otherwise in getting it.

The process of monitoring third tier recipients as described in the guidance relies entirely on the honesty of the recipients. A more realistic approach (although one that needs greater input from IOHPS and so greater administrative costs) would be for individuals to be awarded third tier benefits for a set period (say 2 or 3 years) with a medical assessment at the end of that period to determine whether the pension should continue.

Proposal to reduce qualifying period for ill health benefits to 3 months

We do not support the proposal to reduce the qualifying period for ill health benefits from 2 years to 3 months. Individuals do not have to pass any medical test to be allowed Scheme membership so there would be nothing to stop an employee who had previously opted out of the Scheme membership deciding to rejoin for a very short period once they were aware they were likely to retire on ill-health grounds.

Between a quarter and a third of the workforce are not Scheme members and there is a significant cost danger to employers that non-scheme members will opt in just prior to ill health retirement to get the benefit potentially of a significantly increased pension after as little as 3 months membership.

There is an argument that a 3 month qualification period for ill health benefits is preferable as it would be consistent with the period for qualification period for other scheme benefits. However, for the reason stated above, if a 3 month qualification period is introduced anyone with less than 2 years membership should only be entitled to ill health benefits based on their accrued scheme membership regardless of their level of incapacity.

Detailed comments on the text of the proposal

Eligibility criteria for the third tier: There is a discrepancy between 3 c) of Annex A which refers to the member being capable of gainful employment “quite soon after leaving” and the table in 3 g) which refers to medical evidence indicating “gainful employment could be obtained at the point of leaving”.

Review period: 3) d of Annex A suggests that individuals could be reviewed after a year to see whether they have obtained “gainful employment”. Either the review period should be extended or the existing definition of gainful employment should be changed for this review to be meaningful as gainful employment is currently defined as “paid employment for not less than 30 hours in each week for a period of not less than 12 months.”

Definitions: Clear guidance is required for such terms as “reasonable time”, “permanently” and “reduced likelihood”.

Suspension of pension: If a third tier pension is suspended, when will it be reinstated? Will it be age 65 or the age at which unreduced benefits are payable if earlier? If so, those who would have been entitled to draw reduced benefits at 60 will be penalised. Alternatively if age 60 is chosen this will increase costs further and will not be compatible with the Scheme's normal retirement age of 65.

Summary

Our preferred approach would be for there not to be a third tier of ill health benefits. The proposed two tiers provide reasonable protection for member and are more generous than the existing LGPS regulations. If there has to be a third tier of ill-health provision our preference is for it to be kept out of the scheme and to be a one-off discretionary compensation payment made from an employer's revenue account.

If these two approaches are not acceptable to all parties, our third preference would be for the third tier to be pension paid for a set number of years (2 or 3) followed by a regular medical review to determine continuing eligibility.

I should add that we have recently had sight of the Local Government Employers' detailed response to the consultation and would like to stress that we are broadly supportive of this.