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Your ref:
Our ref: LGT/GMP

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To: Administrators of the Local Government Pension Scheme (Scotland)

Dear Colleague

THE LOCAL GOVERNMENT PENSION SCHEME IN SCOTLAND
GUARANTEED MINIMUM PENSION (GMP) ENTITLEMENT

This circular should be brought to the attention of administrators of the Local Government Pension Scheme (LGPS) as a matter of urgency. It informs them:

a) that a problem has been identified with the way that the Annual Percentage Increase has been applied to some pensions with a Guaranteed Minimum Pension (GMP) entitlement
b) that this problem may affect pensions they are paying
c) of the action they should take to identify and deal with any pensions that are currently being overpaid as a result of this problem

Background

On 16 December 2008, the Cabinet Secretary for Finance and Sustainable Growth informed the Scottish Parliament of a problem that affects a small proportion of retired public sector employees throughout the UK. The problem concerns the way that the Annual Percentage Increase has been applied to some pensions with a Guaranteed Minimum Pension (GMP) entitlement.

Public service pensions are up-rated in April each year in line with the Retail Price Index (RPI). Occupational pension schemes pay for any up-rating before State Pension is claimed, but thereafter part of the up-rating is paid by the state scheme, depending on the GMP entitlement.

To enable the correct pension increases to be applied, pension scheme administrators need accurate GMP information. That information comes from the individual's national insurance contribution record and is passed to scheme administrators by HMRC. This supply of information to the pension administrator has worked in the majority of cases. But it is now apparent that it has not worked in every instance. In those cases where someone was entitled to a GMP but where the scheme administrator was not informed of that entitlement, scheme administrators will have paid the full annual inflationary increase to a pensioner each year instead of an adjusted sum which reflects the GMP entitlement. In other words, those pensioners have received part of the annual increase twice: once through their occupational pension scheme and once through DWP, who pay their State Pension.

The result is that some occupational pensions have been overpaid. Though individual annual overpayment amounts are small, in some of the affected cases this problem has existed for many years, compounding the overpayments to a more significant level.

Scottish Ministers are responsible for five public sector schemes: the NHS, Teachers, Local Government, Police and Firefighters schemes. The SPPA has worked with COSLA to ensure that key stakeholders of these schemes have been informed of this problem and advised how to manage any queries that may arise. An example of the letter they have received is attached for reference at Annex C.

Scale of the problem

Across the UK as a whole, the issue affects approximately 100,000 pensioners within the main central government schemes covering the NHS, Teachers, the Civil Service, the Armed Forces and the Judiciary. Collectively, this represents around 4.5% of the total number of pensioners in those schemes.

Within Scotland, 6,009 members of the Scottish NHS and Teachers scheme are affected. This total comprises 3,148 NHS and 2,861 Teacher pensioners and represents 4.8% of all pensioners across both schemes. These figures are broadly consistent with the proportion of erroneous cases existing in the NHS and Teachers schemes in England and Wales.

It is also likely that the Local Government, Police and Fire schemes in Scotland are affected. Preliminary sample work undertaken by COSLA suggests that around 4% of pensioners in these schemes may be affected. If these early results are scaled up across Scotland as a whole, this would represent approximately 4,500 pensioners from the local government scheme; 300 police scheme pensioners; and 150 firefighter pensioners. Some of these cases could be among the pensions administered by your organisation.

GMPs were provided by public service schemes between 1978 and 1997. The problem will not affect any pensioner unless they have reached State Pension Age, have service in this period and for whom administrators have no record of a GMP. There may also be cases where a GMP has been inherited.

The solution

Recovery of past overpayments

Scottish Ministers have decided that all past overpayments that have arisen as a result of this problem should be written off for the five public sector schemes they are responsible for. This means that no pensioner is required to repay any of the overpayments they have received, in good faith, as a result of this problem. A similar decision has been reached by UK Ministers for the schemes for which they are responsible.

Currently, write-offs of incorrect pension overpayments in excess of £250 are classified as unauthorised payments and are subject to a tax charge of 40%. However, HMRC regulations planned for the New Year will change the definition of authorised payments, removing the resultant tax charge in these cases. These regulations will be backdated to 6 April 2006.

Treatment of the overpaid amounts

Scottish Ministers' believe that these pensioners should not be penalised for overpayments received in good faith and which resulted from errors which were not their fault.

However, the UK Government has decided that future pensions should be adjusted so that only the correct amount will be paid from April 2009.

For the Scottish Local Government, Police and Fire pension schemes, Scottish Ministers have a range of delegated powers. They are exercising those powers to ensure that from April 2009 the amount of overpayment currently received will continue to be paid though it will be frozen at the current level. This means that future annual inflationary increases will only apply to the pension that pensioners are entitled to and that the overpayment element will not increase in line with inflation.

These actions will be taken forward through revisions to the scheme regulations and the SPPA will be consulting on these shortly.

For the Scottish NHS and Teacher schemes, Scottish Ministers are obliged to seek Treasury consent to any changes to the scheme regulations. They have actively sought such consent to enable them to adopt a similar solution to that being applied to affected members of the Police, Fire and Local Government schemes.

That consent was withheld. As a result we must adopt the same solution being applied by the UK Government to the schemes for which it has responsibility. This is to put the correct payments in place from April 2009. This means that the majority of affected pensioners in the Scottish NHS and Teachers scheme will receive a pensions increase which is less than expected when pensions are up-rated with the RPI in April 2009. A minority will see a reduction in their pension.

Action required by scheme administrators

Local Government pension scheme administrators now need to take urgent action to establish whether any of the pensions they are paying are affected by this problem. This will involve liaison with the National Insurance Contributions Office (NICO). Once affected cases have been identified the overpayment should be calculated up to 5 April and the necessary write-off can be authorised.

In order to resolve this problem we advise administrators to follow a staged approach, as follows.

Stage 1 identify and assess the overpayment

1. Identify relevant pensioners who do not have a GMP record. Relevant pensioners are those who have reached State Pension Age (SPA) (including survivors) and have completed relevant service (between 1978 and 1997).

2. Liaise with NICO to establish whether any of the identified cases should include a record of a GMP entitlement. HMRC's guidance manual CA19 provides detailed advice on steps to follow when providing the necessary data to NICO. NICO's response should indicate those cases where action needs to be taken.

3. Contact affected pensioners to explain how their pension will be paid in future. Administrators may also want to contact unaffected pensioners to put their minds at ease. The SPPA can provide administrators with shell letters that can be adapted, on request.

4. Maintain a record of the numbers of cases affected and of the costs of:

   a) cumulative past overpayments

   b) overpayments in 2008/09

Stage 2 Correcting pensions in payment.

5. It is anticipated that administrators will be in a position to confirm which pensions are affected and the total amount of overpayments involved by no later than 5 April 2009. **If this date is not possible administrators should inform the SPPA as soon as possible, indicating the exact date when this will be possible.**

6. Relevant overpayments up to and including 5 April 2009 should be written off.

7. Further instructions will be issued on how to apply the pension going forward from 6 April 2009

Suggested advice for pensioners

The Cabinet Secretary's announcement may cause some concern to pensioners who are unsure if they are affected. It is likely that scheme administrators will be contacted to provide further information. The key messages for LGPS pensioners are:

a) that they should not worry

b) if it turns out that their pension has been affected it will not be reduced and that this amount will continue to be paid

c) that it will take time to work through this issue

d) but that pensioners will be contacted once that exercise has been completed

A Questions and Answers brief is attached at Annex A to help scheme administrators deal with queries that arise. We are also attaching a more generic Questions and Answers sheet, for your reference, at Annex B.

It is likely that some scheme administrators will already have robust process checks in place that have ensured that this problem has not affected the pensions they administer. However all administrators should ensure that proper checks are now in place to make sure that similar overpayments do not arise in the future. The agreement to write off the overpayments and to the continued level of pension income for those PPS/FPS/LGPS pensioners applies only to current cases identified under this exercise.

Yours sincerely

David Lauder
Policy Manager, LGPS

What is a GMP?

A GMP is the minimum pension which an occupational scheme must provide as one of the conditions of contracting out for service before 1997. The Police Pension Scheme is contracted out of the Second State pension, previously known as State Earnings Related Pension Scheme (SERPS). If you or your deceased spouse or partner had police service between 6 April 1978 and 5 April 1997, you will have earned the right to a GMP.

GMP is not a separate benefit paid in addition to your police pension, but ensures that the pension we pay you must at least equal your GMP.

Her Majesty's Revenue and Customs work out the level of your GMP. Your GMP comes into force normally when you ask for your State Pension to be paid to you. (There are circumstances when the GMP comes into force at a later date but the effect on your police pension is the same).

What is pensions increase?

The Pensions (Increase) Act 1971 governs the cost of living increases that apply to public service pensions. We increase your pension each year to reflect rises in the cost of living. The annual increase in public service pension is at the same rate as that applied to additional State retirement pensions and other Social Security benefits.

How is pensions increase applied to my GMP?

We apply pensions increase to the whole of your police pension, including the GMP element, until your GMP comes into force. At that point your police pension is paid as follows:

- <u>For service up to 5 April 1988</u>
  The Government will pay the pensions increase relating to the GMP you earned up to this date with your State Pension.
- <u>For service between 6 April 1988 and 5 April 1997</u>
  We will pay increases on the GMP you earned in this period up to 3%. In years when the increase is more than 3% the Government will pay the balance with your State Pension.

What effect does this have on the pension you pay me?

When your GMP comes into force the National Insurance Contribution Office (NICO) tell us the amount of your GMP. We then adjust our records to reflect the fact that the Government now pays some of the annual pensions increase on the GMP element of your police pension with your State Pension. The overall increase in your pension will however be the same.

So why have I been overpaid?

Unfortunately we have learned that the transfer of information to us was not always successful. This meant that we were not able to take the necessary action to adjust the pension increase we applied to your GMP to reflect that an element of the pensions increase was now being paid with your State Pension.

As a result, you have received increases on the GMP element of your pension twice; once from the Police Pension Scheme and once with your State Pension. This means we are paying you too much pension.

Will my pension reduce?

No. Scottish Ministers believe that you should not be penalised for overpayments received in good faith and which resulted from errors which were not your fault.

In the case of the Local Government, Police and Fire schemes, they have been able to exercise delegated powers to enable you to keep the overpayment. However, that overpayment amount will not be increased by inflation. It will be frozen at April 2009 levels. Your correct pension entitlement will, however, be up-rated by inflation, as usual.

Will I have to pay anything back?

No. The Scottish Government has decided that pensioners affected by this problem should not have to pay back the amounts by which they have already been overpaid.

Q: What is the Issue?

A: Some pensioners who worked in the public sector have been receiving a larger than expected increase to their pensions each year.

Q: Why?

A: Some pensioners are entitled to a Guaranteed Minimum Pension (GMP) as part of their occupational pensions. They receive an annual increase in line with the Retail Price Index (RPI). In the affected cases, part of the GMP increase has been paid by both the scheme pension administrator and the Department for Work and Pensions (DWP), resulting in an overpayment of pension to some pensioners.

Q: What is a GMP?

A: A GMP is the minimum pension which an occupational pension scheme must provide. It applies to schemes which contracted out of the State Earnings Related Pension Scheme from 1978. All public service schemes, for example NHS, Teacher and Local Government, are contracted out.

People who were members of a contracted out pension scheme between 1978 and 1997 may be eligible for a GMP element within their occupational pension. It is a notional benefit which is only paid if the occupational pension is less than the guarantee element and is not a separate benefit to be paid in addition to their occupational pension.

Q: Does every pensioner have a GMP?

A: No. Only those who were employed between 1978 and 1997 and who paid the full employed persons national insurance contribution have an entitlement. Various groups of pensioners will not have a GMP entitlement, for example those who were paying the married women's rate of National Insurance.

Q: Who is affected?

A: A proportion of pensioners (about 4-5%) who were members of a public service pension scheme between 1978 and 1997 and who have a GMP entitlement are affected. Some 6,000 people in Scottish NHS, and teachers pensions schemes are affected out of a total of 129,000 pensioners. Pensioners of UK schemes covering the civil service, MOD and judiciary may also be affected.

Scottish Local Government, Police and Fire Schemes are still finalising their investigation into the matter.

Q: Does this affect private sector schemes, as well?

A: We are not aware of any private sector schemes that are affected. However, Scottish Ministers have concentrated on the schemes they are responsible for, the Local Government, the NHS, Teachers, Police and Firefighters schemes in Scotland.

Occupational pensions is a matter that is reserved to the UK Government. The Department for Work and Pensions (DWP) http://www.dwp.gov.uk may be able to answer this question.

Q: How did the overpayments occur?

A: Public service pensions are increased each year in line with the Retail Prices Index (RPI). The occupational scheme pays the increase on the whole pension, including the GMP element, until pensioners begin to receive their state pension. Thereafter the GMP element is shared between the scheme and the State. A proportion of public service pensioners did not have a GMP shown on their pension record which has meant that they have received the increase twice: once with their occupational scheme and again with their State pension. The result of this is that they have been overpaid.

Q: Why was the GMP not recorded on the pension record?

A: The agreed procedure whereby Her Majesty's Revenue and Customs (HMRC) provides information to occupational pension scheme administrators has failed in a small proportion of cases. All public service schemes are working with HMRC and DWP to identify any patterns to the missing information. Administrative processes are being amended to prevent a recurrence of the issue.

Q: If someone has not received a letter, is the pension correct?

A: Every NHS and Teachers scheme pensioner in Scottish schemes should have received a letter to advise, either that the pension was correct, or potentially wrong. If no letter has been received they can write to the Director of Operations at SPPA for information. The UK Government intends to write only to those pensioners who have received an overpayment from schemes that it administers. Scottish Local Government, Police and Fire Schemes are still finalising their investigation into the matter

Q: When will letters about the inflation adjustment from April be sent?

A: The annual inflation amounts are not normally announced until later in March. SPPA will write to everyone as soon as they have more information on this from HM Treasury

Q: How will pensioners of Local Government, Police and Fire pension schemes know if they are affected?

A: The individual pension scheme administrators for the Local Government, Police and Fire schemes will be examining their systems to see if the problem affects them.

They will contact affected pensioners once they have completed that work, which may take some time.

However, even if pensioners in these schemes are affected, they will continue to receive the overpayment they are currently getting along with their correct pension.

Q: Why are local government/police/fire scheme pensioners not having to lose pensions?

A: The Scottish Government will put in place regulations which will allow current levels of payment to continue. From April 2009, the correct increases to GMP will be in place. Because of devolved powers, the Scottish Government does not have to seek the consent of the Treasury , and therefore a different solution is possible.

Q: Why can't this be done for NHS and Teachers scheme pensioners?

A: Changes to the regulations for these schemes require the consent of HM Treasury, and such consent was withheld, despite the request of the SG. The SG therefore have no option but to implement the decision of the UK Government, and correct wrong pensions caused by the GMP issue from April 2009.

Q: Why has the Scottish Government adopted a different approach to the rest of the UK?

A: Scottish Ministers took the view that no-one should have to repay money because of mistakes by Government Departments/Agencies and therefore decided that it was appropriate to write-off any overpayments.

The SG also felt that it was wrong to reduce someone's pension, which would have been in payment for many years, and especially since there was no-way that the individual would have realised they were receiving the wrong amount.

Despite these views being presented to the UK Government, no HM Treasury consent was given and this is why the final decisions in Scotland are different to the rest of the UK.

Q: Who can those affected talk to if they need further information or advice?

The helpline number for NHS and Teachers' pensioners is **01896 892463**. Pensioners in other schemes should contact their pension scheme administrators.

Q: What help is available in the event of any hardship this may cause?

A: Once the figures are known in April 2009 individuals may be eligible for other financial assistance. They may be eligible for Pension Credits from the Pension Service, who can be contacted on **0800 99 1234.** They are open from 8am to 8pm Monday to Friday.

People can also contact their local Council Offices and inform them of the change in their income, in case they are eligible for assistance with Housing Benefit or with their Council Tax.

Q: Can those affected take the matter further?

A: The SPPA has an internal dispute resolution procedure (IDRP) for pensioners who are unhappy with a decision affecting their pension and full details are contained in the SPPA web site at http://www.sppa.gov.uk/complaints.htm. They can also write to the Director of Operations at SPPA and ask for the IDRP guide which explains what their rights are if they remain dissatisfied with the decision.

Other schemes have similar arrangements.

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Your ref:
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Date: 16 December 2008

Chief Executive of Scottish Local Authorities
Finance Directors of Scottish Local Authorities
Chief Executives of Health Boards
HR Directors of Health Boards
Chief Constables
Chief Fire Officers
Clerks of Joint Police Boards
Clerks of Joint Fire Boards

Dear Colleague

Pensioner overpayment

I am writing to you to make you aware of an issue that affects a small percentage of public sector pensioners in Scotland. This letter explains what that issue is and how it is being addressed. Because you may be contacted by former employees or their representatives, I also want to explain how they can get more information or advice and to suggest actions which employers may wish to consider.

The Cabinet Secretary for Finance and Sustainable Growth today informed the Scottish Parliament of a problem that affects a small proportion of retired public sector employees throughout the UK. The problem concerns the way that the Annual Inflationary Pension Increase has been applied to some pensions with a Guaranteed Minimum Pension (GMP) entitlement. The problem does not affect anyone who is not currently receiving a pension.

The problem

Some pensioners who worked in the public sector have been getting a larger than expected increase in their pensions year on year. This is because of the way that annual pension increases have been paid.

Public service pensions are up-rated in April each year in line with the Retail Price Index (RPI). Occupational pension schemes pay for any up-rating before State Pension is claimed, but thereafter part of the up-rating is paid by the state scheme, depending on the GMP entitlement. In affected cases, incorrect information on GMP entitlement has been held by scheme administrators. This has resulted in interest on the GMP element being paid twice, in error – once by the pension scheme administrator and once by the Department for Work and Pensions (DWP). The problem appears to have been primarily caused by the failure of Her Majesty's Revenue and Customs, over many years, to pass correct pensioner details to pension scheme administrators.

Number of people affected

Across the UK as a whole, the issue affects approximately 100,000 pensioners within the main central government schemes covering the NHS, Teachers, the Civil Service, the Armed Forces and the Judiciary. Collectively, this represents around 4.5% of the total number of pensioners in those schemes.

Within Scotland, 6,009 members of the Scottish NHS and Teachers scheme are affected. This total comprises 3,148 NHS and 2,861 Teacher pensioners and represents 4.8% of all pensioners across both schemes. These figures are broadly consistent with the proportion of erroneous cases existing in the NHS and Teachers schemes in England and Wales.

It is also likely that the Local Government, Police and Fire schemes in Scotland are affected. Preliminary sample work undertaken by COSLA suggests that around 4% of pensioners in these schemes may be affected. If these early results are scaled up across Scotland as a whole, this would represent approximately 4,500 pensioners from the local government scheme; 300 police scheme pensioners; and 150 firefighter pensioners.

The solution

Recovery of past overpayments

Scottish Ministers have decided that all past overpayments that have arisen as a result of this problem should be written off for the five public sector schemes they are responsible for. This means that no pensioner is required to repay any of the overpayments they have received, in good faith, as a result of this problem. A similar decision has been reached by UK Ministers for the schemes for which they are responsible.

Treatment of the overpaid amounts

Scottish Ministers believe that these pensioners should not be penalised for overpayments received in good faith and which resulted from errors which were not their fault.

However, the UK Government has decided that future pensions should be adjusted so that only the correct amount will be paid from April 2009.

For the Scottish Local Government, Police and Fire pension schemes, Scottish Ministers have a range of delegated powers. They are exercising those powers to ensure that from April 2009 the amount of overpayment currently received will continue to be paid, though it will be frozen at the current level. This means that future annual inflationary increases will only apply to the pension that pensioners are entitled to and that the overpayment element will not increase in line with inflation.

These actions will be taken forward through revisions to the scheme regulations and the SPPA will be consulting on these shortly.

For the Scottish NHS and Teacher schemes, Scottish Ministers are obliged to seek Treasury consent to any changes to the scheme regulations. They have actively sought such consent to enable them to adopt a similar solution to that being applied to affected members of the Police, Fire and Local Government schemes.

That consent was withheld. As a result we must adopt the same solution being applied by the UK Government to the schemes for which it has responsibility. This is to put the correct payments in place from April 2009. This means that the majority of affected pensioners in the Scottish NHS and Teachers scheme will receive a pensions increase which is less than expected when pensions are up-rated with the RPI in April 2009. A minority will see a reduction in their pension.

What will happen next and where can people get more information

The SPPA administers both the NHS and Teachers' schemes in Scotland. We have already written to those people who have been overpaid to explain how their pension will be put right so that it is correct from April 2009. We have explained that we will write to them again once HM Treasury have formally told us what next year's pensions increase will be. We expect that to be in the New Year, at which time we will be able to tell people what their correct pension amount will be.

We have also written to NHS and Teachers' pensioners who are unaffected, because we do not want them to worry unnecessarily about something that does not affect them.

Both letters give details of a dedicated Helpline number that can be contacted for more information. People are also being advised that more information on the problem and how it is being dealt with is available on the SPPA website (www.sppa.gov.uk). That also includes the detailed Questions and Answers material that has been enclosed with this letter.

Scheme administrators for the LGPS, PPS and FPS will need to establish the nature and scale of the problem for their pensioners. We have written to them to alert them to this problem and propose that they carry-out an urgent review of their records. That letter also includes advice on how that work can be progressed.

How you can help

Your organisation may be contacted by former employees or their representatives to ask whether they have been affected by this issue. It is obviously a matter for you to decide how your organisation will deal with any queries you receive. However, in the first instance we would be grateful if you would make sure that the relevant people in your organisation have seen a copy of this letter and the accompanying Questions and Answers.

If your staff would like to provide first line help to people who will obviously be quite concerned, we suggest that they take the following action:

- reassure anyone who is not an existing pensioner that they are not affected because this only affects a small proportion of existing pensioners
- reassure people that no-one is being asked to repay past overpayments
- reassure NHS or Teachers' scheme pensioners who contact you about this that the SPPA has written to them to explain whether or not they are affected by this problem and provide contact details
- advise any NHS or Teachers' scheme pensioners who contact you about this to contact the SPPA on our dedicated Helpline number **01896-892463**

- advise any LGPS, PPS or FPS pensioners that their scheme administrators will be looking into this and that:
  - they should not worry, because if it turns out that their pension has been affected it will not be reduced and will continue to be paid
  - that it will take time to work through this issue and that pensioners will be contacted once that exercise has been completed
  - to refer to our website www.sppa.gov.uk or to their scheme administrator if they would like more information.

A copy of the Cabinet Secretary's memorandum to the Scottish Parliament's Finance Committee will shortly be available from our website.

Yours sincerely

Neville Mackay
Chief Executive