

# Reduction of Earnings – Protecting Pensions

## Local Government Pension Scheme – LGPS

This leaflet is designed to inform scheme members, in general terms, of the options available to them, should they move to a lower graded post on or after 1st April 2014 and suffer a reduction in pensionable earnings.

### Can my pension be protected by using earlier, higher year's earnings to calculate my pension?

The LGPS changed from a final salary scheme to a Career Average Revalued Earnings Pension Scheme or CARE scheme on 1st April 2014. This in effect means that pensions are no longer calculated by reference to a single years pay (e.g. the final years pay) but are assessed on the average revalued earnings the person has earned over their total career. However pension rights earned in the LGPS up to the 31st March 2014 are protected and still calculated on a final salary basis. So to answer this question we need to look at when you joined the LGPS.

#### Persons who joined the LGPS on or after 1st April 2014.

If you first joined the LGPS on or after 1st April 2014 and you do not have any previous membership of the LGPS earned before 1st April 2014 and you have not transferred previous public sector pension rights (e.g. from the Teacher's, NHS, Civil Service pension scheme or LGPS (Scotland)) into the Northumberland LGPS Pension Fund with final salary protection, your pension will be calculated on the revalued average of your earnings over the whole of your period of LGPS membership and no mechanism exists to enable your pension to be calculated by reference to a higher years pay in circumstances where your earnings have been reduced.

#### Persons who joined the LGPS before 1st April 2014 or who have transferred previous public sector pension rights into the Northumberland LGPS Pension Fund which carry a protected final salary entitlement.

If you fall into this category it may be possible to protect the value of your pension by having it calculated by reference to a previous higher years pay **but this only applies to protected final salary rights earned before 1st April 2014 (or transferred rights which carry former public sector final salary protection).**

### I do have protected final salary rights what options are available to me if my pay is reduced?

If **you have protected final salary rights** and suffer a reduction in your earnings (the reduction to your earnings can be either voluntary i.e. it's your choice to move to a lower graded post; or the change can result from a decision made by your employer e.g. you are moved to a lower graded post as a result of a review of the service provision) then please read this leaflet which explains the options available to you. These options may also apply where your pay is not reduced but future increases in your pay are restricted (e.g. you will not receive an increase in pay until your earnings coincide with a revised grade).

Basically there are 2 options available to you:-

#### Option 1

Simply notify the Pension Section that your earnings have been reduced. We will then ensure that, should you retire/leave within 10 years of the reduction in pay, your pension relating to pre 1st April 2014 LGPS service (or which carries a final salary protection) is based upon the highest of the following pay figures:-

- a) the highest single years pensionable pay out of your last 3 years service (each year ending on the anniversary of your leaving date), or
- b) the average of the best 3 consecutive years pensionable pay out of the last 13 years (each year in the averaging period ending on the 31st March).

#### Option 2

You can elect to take a deferred pension for the period of service prior to the change to your contract of employment (the deferred benefits would relate to both pre 1st April 2014 service which carry final salary protection and rights earned from 1st April 2014 on a CARE basis). You would then accrue a separate CARE pension in your new lower paid job.

## How do these arrangements work?

### Electing for a “better” years pay to apply

If you are moving to a lower graded job in the ten years prior to retirement, you can elect **at retirement or when benefits are awarded**, to have your pension benefits earned before 1st April 2014 which carry final salary protection based upon:-

- i) The highest pensionable earnings of any one year out of your least 3 years of service, each year ending on the anniversary of your leaving date, or
- ii) the highest **average** of any 3 consecutive years pensionable earnings out of the last 13 years, each 3 year period ending on 31st March.

#### NOTE

◆ Pensionable earnings in relation to protected final salary rights where mentioned in this leaflet means pensionable pay as defined in the LGPS 2008 (which would not include non-contractual overtime).

◆ the formal election to have your pension based either i) or ii) above needs to be made when you leave service, however we would ask you to notify us when the reduction to your pay actually takes place. We will then note your file and ensure that appropriate action is taken when benefits become due.



### There are a number of points which we should clarify regarding the “better year” options:-

- ◆ Clearly a lot of people do not know when they will retire. Take for example a person aged 47 who is redeployed to a lower graded post, normally the assumption would be that this person is more than 10 years away retirement. However if he/she was granted early retirement at age 55 the reduction in pay would have fallen within the period 10 years prior to retirement and he/she could have opted to have their pension based on the best average of 3 years pensionable pay from the last 13 years. This effectively would include earnings from his previously higher paid job.
- ◆ This arrangement can apply where any “retirement pension benefits” are calculated under the LGPS. Most people reading this will think of pension benefits which are paid immediately at retirement age, but this does not have to be the case. If we have a person who moves to a lower graded post aged 35 and then at the age of 42 they leave local government employment they have two choices regarding their LGPS pension:-
  1. they can leave their pension rights deferred within the Northumberland Pension Fund. As the pay reduction happened in the 10 year period prior to her leaving the deferred pension relating to pre 1st April 2014 service could be calculated on the best average 3 years pensionable pay out of the last 13 years if this is to his/her advantage. See later section of this leaflet for more information regarding deferred pensions.
  2. As an alternative to retaining a deferred pension the person could transfer the cash equivalent value of their pension rights to an alternative pension scheme (i.e. a new employer’s occupational scheme or a personal pension type arrangement). If it was to his/her advantage he/she could elect to have the cash equivalent transfer value payment relating to pre 1st April 2014 service calculated using an average of 3 years pensionable pay falling within the 13 years prior to leaving. The cash equivalent transfer value payment is not linked to the employee contributions, rather it relates to the amount the Scheme must hold in the pension fund to pay the deferred pension and other benefits (put in simple terms its your slice of the pension fund).
- ◆ Where your pension relating to pre 1st April 2014 service is based upon earnings for a period, **other than your last year of service**, the benefits would attract pensions increase with a start date of the day following the pay assessment period. In effect what this does is, more or less, index-links the former rates of pay.

## How does the deferred benefit option work?

If the reduction in pay results from a permanent change to your contract of employment, then provided you have completed at least 2 years pensionable service, you may elect to be awarded a deferred pension for service prior to your change of contract and pension rights for service earned up to 31st March 2014 would be calculated by reference to your final years pensionable pay (as defined in the LGPS 2008). You would then start to accrue a separate pension in respect of your new job. This would mean at retirement that you would have 2 pensions.

1. The deferred pension for the period up to the contract change.
2. A second pension earned in your new lower paid post.

## How are deferred benefits calculated?

Deferred pension benefits for service up to 31st March 2014 are normally based upon your pensionable earnings (as defined in the LGPS 2008) for the 12 months immediately prior to your change of contract (but the rules governing better years earnings can apply if this is to your advantage). The deferred pension benefits would be calculated as follows:

### Service accrued prior to 1st April 2008.

$\text{Pension} = \text{pensionable earnings} \times 1/80 \times \text{years of scheme membership prior to 1st April 2008.}$

### Plus:

$\text{a lump sum} = \text{Pre April 2008 Pension} \times 3$

### Service accrued on and from 1st April 2008 and before 1st April 2014.

$\text{Pension} = \text{pensionable earnings} \times 1/60 \times \text{years of scheme membership on or after 1st April 2008 and before 1st April 2014.}$

### Service from 1st April 2014.

$\text{Pension } 1/49\text{th of each years revalued pensionable pay (as defined in the LGPS 2014 including overtime) earned on or after 1st April 2014.}$

### Your pension would then be the total of:-

$\text{Your pre 1st April 2008 pension (1/80th basis)} + \text{your pension earned 1st April 2008 to 31st March 2014 (1/60th basis)} + \text{the CARE pension you have earned from 1st April 2014.}$



## When would my deferred pension become payable?

Deferred benefits are payable from normal pension age (normally equal to your State Retirement age, but no earlier than age 65). You would have the option to retire and take your deferred pension from age 55 onwards; however your pension benefits would be subject to reductions if taken before normal pension age. A deferred pension can be paid early (without reduction), where the employer's occupational health physician certifies that you have become permanently incapable of performing the duties of the post which gave rise to the deferred pension and that you are unlikely to be able to undertake gainful employment within a 3 year period (or before normal pension age if earlier).

## Are deferred benefits index linked?

Yes. Index linking is applied to the deferred pension benefits during the period which the pension is deferred, that is they are subject to the public service pension increase arrangements. The pension will continue to attract annual pension increases once in payment.

## What happens if I opt for deferred benefits but at a later date regain my former position, with this or some other local authority?

If you take up new employment (i.e. a new contract of employment) your deferred pension would normally be cancelled and the pension would be linked with your new job. Any pre 1st April 2014 pension rights which enjoy final salary protection would then link to your new job and be calculated by reference to what your final years pensionable pay (as defined within the LGPS 2008 excluding overtime) would be. Alternatively you may elect within 12 month of starting your new job to retain your deferred pension. You would then earn a separate pension in your new job.



## Are there any other issues regarding a deferred pension which I should consider?

You may also wish to consider how an option for a deferred pension could impact upon the prospect of early retirement at a future date. Let us assume that a person defers their pension at age 45 and accrues a separate pension in their new job. At the age 55 he/she is made redundant. The pension rights accrued between ages 45 and 55 would be paid early as a right without reductions, however the deferred pension accrued up to age 45 would **not** be payable early as a right without reductions. The person could opt to take their deferred pension on a reduced basis as they have attained age 55 or they could leave the first pension earned up to age 45 deferred for payment on an unreduced basis at normal retirement age.

If this person had only suffered a small drop in pay, in pension terms they could have lost out significantly by taking the deferred pension option because they have lost the opportunity to access the early payment of the pension accrued before age 45 on an unreduced basis. If you are considering the deferred pension option you should be aware of the possible impact upon future early retirement options.

## I am remaining on the same grade but moving to a part-time post; do the options outlined apply to me?

NO. Pension benefits earned before 1st April 2014 in respect of part-time employees are always calculated by reference to what the employee's **whole-time** equivalent pensionable earnings (as defined in the LGPS 2008) would have been, with the service for any part-time employment before 1st April 2014 being equated to a whole-time equivalent (e.g. a person who worked 50% of full-time before 1st April 2014 would have been credit with 6 months whole-time service for each year of scheme membership before 1st April 2014).



## Part-time Example – Pre 1st April 2014 Service

A person has 2 years whole-time service followed by 4 years during which they worked 18.5 hours a week. An equivalent whole-time employee would have worked 37 hours a week. This person earns £10,000 a year in their part-time post. All service is taken to have accrued in the 1/60th scheme.

$$\begin{aligned}\text{Whole-time equivalent pay} &= £10,000 \times 37/18.5 \text{ hours} \\ &= £20,000\end{aligned}$$

$$\begin{aligned}\text{Whole-time equivalent service} &= 2 \text{ whole-time years}\end{aligned}$$

$$\begin{aligned}\text{Plus: 4 part-time years} & \\ \quad \times 18.5/37 \text{ hours} &= 2 \text{ whole-time equivalent years.}\end{aligned}$$

$$\begin{aligned}\text{Total whole-time equivalent years} &= 4\end{aligned}$$

$$\text{Pension} = £20,000 \div 60 \times 4 \text{ years} = £1333 \text{ a year.}$$

This method of calculating the pension in effect means that pensionable whole-time service with final salary protection still attracts whole-time benefits, with periods of part-time working attracting the appropriate percentage of whole-time benefits again only for pre 1st April 2014 service with final salary protection.



### Are the options outlined, an effective way of protecting pre 1st April 2014 final salary benefits where an employee moves to a lower paid post?

Both of the arrangements described in this leaflet try to protect the employee's former earnings by linking the benefits to consumer price inflation (CPI), they are therefore normally protected to that extent. However, should wage awards be greater than CPI inflation this, in real earnings terms, would erode the value of either of the arrangements available.

### What action should I take now?

If you have been moved to a lower paid post and you have LGPS rights earned before 1st April 2014 (or you have transferred in former public sector pension rights which have a final salary protection) and wish to avail yourself of either of these options, please complete the enclosed form.

### Can someone advise me of which option to take?

No. This is a decision you must make.

**NOTE:** It is impossible to cover all the permutations which could affect the benefits of an employee in this situation. Any employee wanting advice on any specific point should contact the Pensions Section. The Pensions Section are however unable to advise employees as to which of the options available they should choose.

### The Local Government Pension Scheme Regulations.

The Local Government Pension Scheme is governed by statutory regulation and nothing in this leaflet can override those statutory provisions. In all cases, benefits must be determined by reference to the appropriate statutory regulations. This leaflet is provided for general guidance only and cannot impart any entitlement upon an individual. For further information please contact: -

**The Pensions Section,  
Finance Directorate,  
Northumberland County Council,  
County Hall,  
Morpeth,  
Northumberland  
NE61 2EF.  
Telephone: 01670 623576**

# The Local Government Pension Scheme Regulations

## Reduction In Earnings

- \* 1. As I have suffered a reduction in my pensionable earnings I request that my file be noted to this effect and should pension benefits become due to me within 10 years of this reduction taking effect please inform me of the options available with regard to having that part of my pension which carries final salary protection based upon either, the best years pensionable earnings ^ of the last 3 years of my service or the best average of 3 years consecutive pensionable earnings ^, ending on the 31st March each year, out of the last 13 years.
- \* 2. I elect to defer my pension benefits in respect of my former post and accrue a separate pension in respect of my new employment.
- ^ Pensionable earning in relation to protected final salary pension rights means pensionable pay as defined in the LGPS 2008 (which would not include non-contractual overtime).
- \* **Delete as appropriate.**

Full Name: (Please Print) .....

Employer: .....

Department: .....

National Insurance No: .....

Signed: ..... Date: .....

*Please return to:*

The Pensions Section, Finance Directorate, Northumberland County Council, County Hall, Morpeth,  
Northumberland, NE61 2EF

(Please enclose a copy of the letter or contract advising you of your redeployment or change of employment, if available).