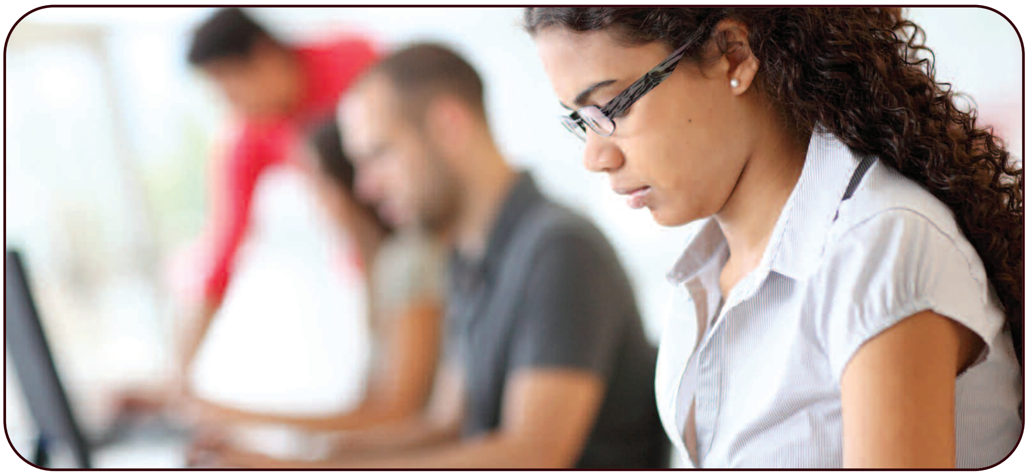
PENSIONS NEWS LETTER

Winter 2014

Introduction

Welcome to the latest edition of the Northumberland LGPS Newsletter. The main purpose of this edition is to give scheme members an update on the changes which will be made to the LGPS in April 2014. We will however also be covering some general pension topics.



The 2014 LGPS

As from the 1st April 2014 the LGPS will change from a "final salary" pension scheme to a "Career Average Revalued Earnings" pension scheme or CARE scheme.

- This change will only apply to pension rights earned in the LGPS from the 1st April 2014. LGPS rights earned prior to this will retain their final salary status i.e. those rights will normally be based upon the person's final years pensionable pay as now.
- Additional to this for members who were in the pension scheme on 31 March 2012 and were aged 55 or over as at 1st April 2012, if they retire **at age 65 or later,** there will be an "underpin" to the effect that their pension will be no less than it would have been had they remained subject to the current final salary scheme.

The table below looks at the main provision of the current scheme and compares them with the new 2014 scheme.

	LGPS 2008 The Current Scheme	LGPS 2014 The New Scheme
Type of Scheme	Final Salary	Career Average Revalued Earnings or CARE Scheme
Accrual Rate	1/60th	1/49th
Revaluation Rate	Based upon Final Years Pensionable Earnings	Consumer Price Index (CPI)
Pensionable Pay	Pay *Excluding* Non-Contractual Overtime	Pay *Including* Non-Contractual Overtime

	LGPS 2008 The Current Scheme	LGPS 2014 The New Scheme
Employee Contribution Rates	Earnings up to £13,700 5.5% £13,701 to £16,100 5.8% £16,101 to £20,800 5.9% £20,801 to £34,700 6.5% £34,701 to £46,500 6.8% £46,501 to £87,100 7.2% More than £87,100 7.5%	Earnings up to £13,500 5.5% £13,501 to £21,000 5.8% £21,001 to £34,000 6.5% £34,001 to £43,000 6.8% £43,001 to £60,000 8.5% £60,001 to £85,000 9.9% £85,001 to £100,000 10.5% £100,001 to £150,000 11.4% More than £150,000 12.5% These earnings bands are subject to periodic review.
Employee Contribution Flexibility	None	Scheme members can opt to pay 50% of the normal contribution and accrue 50% of the pension. For example a person who would normally pay 5.8% can opt to pay 2.9% and for the period that they pay this reduced contribution rate they would be earning pension at a 1/98th of pay i.e. 50% of the normal 1/49th.
Normal Retirement Age	65	Equal to the individual member's State Pension Age (but no younger than 65)
Death In Service Lump Sum	3 x Pensionable Pay	3 x Pensionable Pay
Death in Service Survivor Pensions i.e. widows and widowers pensions etc.	1/160th of final year's pensionable pay for each year of scheme membership and added years to age 65 e.g. for a person who dies aged 45 with 10 years scheme membership the pension would be based upon 30 years (10 years + 20 added years to age 65).	1/160th of pensionable pay for each year of scheme membership and added years to State retirement Age (SPA) e.g. for a person who dies aged 45 with 10 years scheme membership and an SPA of 66 the pension would be based upon 31 years (10 years + 21 added years to age 66).

	LGPS 2008 The Current Scheme	LGPS 2014 The New Scheme
Ill Health Pensions	**Tier 1 (not able to work again)** Pension based upon actual scheme membership and added years equal to the -period to age 65 e.g. a person aged 45 at retirement with 10 years scheme membership would get a pension based upon 30 years service. **Tier 2 (permanently unable to do local authority job – unlikely to be able to do some work within 3 years of leaving but likely to be able to do so before age 65).** Pension based upon actual scheme membership and added years equal to 25% of the period to age 65 e.g. a person aged 45 at retirement with 10 years scheme membership would get a pension based upon 15 year's service i.e. 10 years + (20 years x 25%). **Tier 3 (permanently unable to do local authority job – likely to be able to do some work within 3 years of leaving).** A temporary pension for up to 3 years based on actual scheme membership only. After the temporary payment period the pension is then suspended until retirement age.	**Tier 1 (not able to work again)** Pension based upon actual scheme membership and added years equal to the period to State Pension Age (SPA) e.g. a person aged 45 at retirement with 10 years scheme membership and a SPA of 66 would get a pension based upon 31 years service. **Tier 2 (permanently unable to do local authority job – unlikely to be able to do some work within 3 years of leaving but likely to be able to do so before normal pension age.** Pension based upon actual scheme membership and added years equal to 25% of the period to SPA e.g. a person aged 50 at retirement and a SPA of 66 with 10 years scheme membership would get a pension based upon 14 years service i.e. 10 years + (16 years x 25%). **Tier 3 (permanently unable to do local authority job – likely to be able to do some work within 3 years of leaving).** A temporary pension for up to 3 years based on actual scheme membership only. After the temporary payment period the pension is then suspended until retirement age.

	LGPS 2008 The Current Scheme	LGPS 2014 The New Scheme
Early Retirement At Employees Option	Only available from age 60 as a right. The employer can allow early retirement from age 55 but employer consent needed before age 60. Pension Benefits may be subject to early payment reductions.	Available as a right from age 55 i.e. no employer consent needed but Pension Benefits subject to early payment reductions. (See further note on Rule of 85).
Early Retirement On Redundancy Grounds	Pension paid as a right where redundancy termination happens on or after age 55.	Pension paid as a right where redundancy termination happens on or after age 55.
Lump sum options	Can convert (subject to HMRC limits) pension to lump sum with every £1 of annual pension given up providing £12 of lump sum.	Can convert (subject to HMRC limits) pension to lump sum with every £1 of annual pension given up providing £12 of lump sum.
Indexation Of Pensions In Payment	Based upon CPI	Based upon CPI
Qualifying Period	A person with 3 months or more scheme membership qualifies for a pension	A person with 2 years or more scheme membership qualifies for a pension

Rule of 85

The Rule of 85 was a provision of the LGPS Regulations1997 that enabled some members with long service to retire before age 65 with an unreduced pension (employer consent was required to retire before age 60). This provision has been phased out of the scheme but some members still have protected status.

It is understood that previously agreed protections will continue to apply in respect of voluntary retirements from age 60 onwards **however** DCLG have stated that rule of 85 protections will not apply where a person chooses to retire on or after age 55 but before age 60 under the terms of the new the 2014 scheme. Details regarding the reductions which will apply to pensions in such cases is not yet available from the Government Actuary.

An example of a Career Average Revalued Earnings or CARE Pension Calculation

This example is based on a person who has been a member of the LGPS CARE scheme for 5 years and assumes CPI inflation at about 3%.

Year	Pay	Accrual Rate	Cumulative Inflation Factor	Pension Earned
1	£17,000	X 1/49th	X 1.15	= £399
2	£18,000	X 1/49th	X 1.11	= £408
3	£19,500	X 1/49th	X1.06	= £422
4	£19,900	X 1/49th	X 1.03	= £418
5	£23,000	X 1/49th	X 1.00	= £469
		Total Due	Pension	= £2,116

If he/she had still been subject to the old final salary LGPS his pension for 5 years membership, based upon final earnings of £23,000, would have been:-

£23,000 ÷ 60 x 5 years scheme membership = £1,916 a year.

As this example illustrates it is certainly not the case that everyone will be worse off under the CARE arrangements, some staff on low earnings could well pay less in and get more out under these proposals but the way the changes will impact upon people will vary from person to person.

Let's look at an example based on the above person but assuming that they also have 10 years pension scheme membership prior to April 2014 and retire at State Pension Age.

- This person therefore has 4 years in the "pre 2008" "80ths Scheme" which applied up until 31st March 2008.
- 6 year in the "post 2008" "60ths Scheme" which was in place during the period 1st April 2008 until 31st March 2014.
- 5 years in the 2014 CARE Scheme which will run from 1st April 2014.

This person's membership prior to April 2014 is protected and would still attract rights based upon the final year's pensionable salary (as defined in the LGPS as at 31st March 2014 i.e. in the "old" scheme).

His/her pension would be the sum of:-

£23,000 ÷ 80 x 4 years in the *80th scheme	**=**	**£1,150**
£23,000 ÷ 60 x 6 years in the 60th scheme	**=**	**£2,299**
Post 2014 CARE Pension (see earlier example)	**=**	**£2,116**
Total Annual Pension	**=**	**£5,565**

They would also be entitled to an automatic lump sum of:-

£1,150 x 3 = £3,450 in respect of the 80th scheme.

The person would have the option of converting some of the £5,565 pension into additional lump sum (within limits imposed by the tax authorities) with every £1 of annual pension converted giving a lump sum of £12 i.e. if the person gave up £1,000 annual pension they would get an additional tax free lump sum of £12,000.

Financing The New 2014 Scheme

The costs of pensions are a concern throughout the western world. Basically as people live longer the cost of providing them with pensions will rise. The introduction of the new 2014 scheme will include a mechanism to deal with increasing pension cost pressures and potentially share additional costs, coming from such things as increasing longevity, between the employees and the employer. The negotiations on the "cost sharing mechanism" are on-going at a national level and as things develop in this area we will advise scheme members accordingly.

Further details of the 2014 Scheme can be found at:-
http://www.lgps2014.org/

Possible Changes to the LGPS AVC Arrangement – Lump Sum Options

Not currently part of the new 2014 scheme rules, but the Treasury in their overall supervisory role of all public sector pension schemes have questioned the options on use of scheme AVC's contained within the LGPS which can in many cases allow a person retiring to take all or the majority of their AVC fund as a tax free lump sum (in addition to any other scheme lump sum, but subject to certain limits imposed by HMRC). This option is allowable under current tax legislation as long as the scheme rules permit it i.e. a person may take 25% of the value of their overall pension benefits within the scheme as a tax free lump sum. However the other major public service schemes do not allow this option and Treasury are insisting that the LGPS falls into line with the other public service schemes which means that for lump sum purposes under the new "2014" scheme AVC's and main LGPS benefits would be regarded as two separate entities. This would allow a person to take 25% of the main scheme rights as lump sum tax free cash plus 25% of any AVC pot. The AVC investment in excess of 25% would have to be taken as an additional pension. Our current understanding is that current AVC contributors will be protected and retain the lump sum option. We do not however have details of this protection in writing and we will keep scheme members informed of developments in this area as they come to our attention.

Survivor Pensions Nominations

When a scheme member dies, in service, on pension, or whilst entitled to a deferred pension, a survivor pension can be paid to:

- **their spouse, including a civil registered same sex partner,**
- **an unmarried partner, who has been nominated to receive a pension upon the death of the scheme member, who meets the qualifying conditions,**

A formal nomination in favour of the unmarried partner **must** be in place before a pension can be paid, if it is not then **in no circumstances** will a pension be awarded. (Unmarried partners include same sex partners who have not entered into a civil registered partnership),

Please don't get confused with the provision which allows a member to nominate a person to receive any lump sum due on their death. Partner nominations and lump sum nominations are two entirely different things. If you live with an unmarried partner and you want them to receive a pension on your death you must make a partners pension nomination in their favour. If you also want them to receive any lump sum due on your death you should also completed a lump sum nomination i.e. you will need to make **two separate nominations.**

Lump Sum Nominations – All scheme members are entitled to complete a nomination setting out who they would wish to receive any lump sum payable on their death i.e. were a person dies in service a lump sum of 3 time annual pensionable pay is due. This lump sum is in addition to any spouse's, partner's or dependant children's pension payable – please see the main scheme guide as regards age restrictions etc. which apply to the payment of children's pensions – normally a child must be dependant and under age18 or under 23 and have remained continually in full-time education.

Pension Scheme Tax Changes – These changes apply to all pension schemes from April 2014

There are a number of changes taking place to the tax advantages available from being a member of a pension scheme. These changes are taking place from 6th April 2014.

Such changes are a personal tax matter and people affected may need to personally register with HMRC to get the Lifetime Allowance protections available.

What changes are being made?

Basically two changes are being made

- 1) the Lifetime allowance is being reduced and
- 2) the Annual Allowance is being reduced, both with effect from 6th April 2014.

The majority of employees will not be affected by these changes which are aimed at limiting the “tax breaks” high earners can obtain from pension scheme membership. These changes will however impact upon some employees who are at the higher end of the earnings scale or are paying significant amounts of extra contributions or AVC’s into their pension plan.

Changes to the Lifetime Allowance

From 6th April 2014 the Lifetime Allowance, the total amount or value which a person can have in all pension schemes before they suffer a tax penalty at retirement, is reducing from £1.5 million to £1.25 million. Clearly these are large sums and this change will only impact upon a limited number of employees. In a defined benefit scheme, such as the LGPS, where we do not hold individual fund values for employees, HMRC determine the overall value of a person’s pension by multiplying it by 20 and adding any lump sum to that amount.

Example - a person who is entitled to an annual pension of £60,000 a year and a lump sum of £180,000 would have a total fund value of :-
£60,000 x 20 = £1,200,000 + £180,000 = £1,380,000. In this case they would exceed the new reduced Lifetime Allowance limit of £1,250,000 and would be liable for an additional tax change, a “Lifetime Allowance Charge”.

Protections Available

HMRC have announced that there will be 2 protections available to people who may be impacted on by this change to the Lifetime Allowance.

Fixed Protection "2014"

To access Fixed Protection "2014" an **employee must personally** make an application to HMRC ***before 6th April 2014.*** This is a personal taxation matter and the Pension Section cannot assist with this or advise individuals.

If you apply for Fixed Protection this would mean that you would still be able to have pension rights with an overall value of £1.5 million before you would suffer a Lifetime Allowance charge at retirement.

You cannot have the new "Fixed Protection 2014" if you have obtained from HMRC Primary, Enhanced or Fixed Protections at the time of one of the previous changes to the pension tax regime.

If you apply to HMRC for Fixed Protection 2014 you would lose it if you:-

- Have a contribution paid to any money purchase pension scheme (i.e. a scheme where the pension is ultimately determined by the value of the invested fund rather than by reference to your pay and length of service).
- Build up further benefits in a defined benefit scheme (such as the LGPS or other public sector scheme) above certain limits.
- Join a new pension scheme.
- Start saving in a new pension pot either under your current pension scheme or a new arrangement (e.g. start an AVC arrangement).

Fixed Protection "2014"

As well as "Fixed Protection 2014" the Government have also announced that Individual Protection 2014 will be available from April 2014 when the Lifetime Allowance reduces to £1.25 million. Full details of how Individual Protection will work are not yet available but it is expected that:-

- It will give you a Lifetime Allowance equal to the value of your pension rights on 5th April 2014 up to a maximum of £1.5 million e.g. if the value of your pension rights on the 5th April 2014 were £1.4 million that would be your individual Lifetime Allowance should you obtain this protection.

- You would **not** however lose your Individual Protection by making further savings or contributions to your pension scheme. However, if as in the previous example, the person had pension rights worth £1.4 million on the 5th April 2014 at retirement they would suffer an Annual Allowance Charge in respect of any further pension right they had earned in excess of £1.4 million.

Our understanding is that any individual who wishes to avail themself of Individual Protection 2014 will be able to apply to HMRC for it with effect from 6th April 2014 and the final date for such applications will be 5th April 2017. This is a personal taxation matter and the Pension Section cannot assist with this or advise individuals.

Further information regarding these changes is available on the HMRC web site http://www.hmrc.gov.uk/pensionschemes/news.htm

Annual Allowance Tax Charges

The Annual Allowance is the amount by which the value of a person's pension rights can grow in **one year** before they incur an additional tax charge. The Annual Allowance is currently £50,000 but will reduce to £40,000 from 6th April 2014.

This is an example of how the Annual Allowance works for a person in a defined benefit pension scheme such as the LGPS:-

A person has 25 years in the LGPS. At the year ended 31st March 2014 their accrued annual pension was £14,000 and their lump sum £40,000. During the year ended 31st March 2015 the person gets a large pay increase and their accrued annual pension at 31st March 2015 is now £19,000 plus an accrued lump sum of £54,000.

In this case the value of the accrued pension benefits for the purposes of the annual allowance limit has increased as follows:-

£19,000 - £14,000 = £5,000 x 16	**= £80,000**
Plus the increase in the lump sum (£54,000 less £40,000)	**= £14,000**
Increase in the value of the LGPS pension rights	**= £94,000**

As the increase exceeds the current annual allowance for 2014/15 of £40,000 by £54,000 this employee could possibly be looking at a tax charge on the £54,000 increase in the overall value of their LGPS pension rights.

Please Note - this is a simplified example, in practice inflation is taken into account when comparing the value of accrued pensions in one year with the next and the person would have been able to carry forward any unused annual allowances from the previous 3 years to offset their tax bill.

The Lifetime Allowance – Protection

We understand that where scheme members have pension pots worth or close to £1.25m they may have the option to apply to the tax authority and have their current entitlement protected subject to them only accruing further pension rights with prescribed limits e.g. pension rights not to rise by more than CPI inflation. The terms for such protections are yet to be announced by HMRC.

To put the £1.25M limit into context a person would have to have a right to an LGPS pension of over £50,000 a year to have any chance of breaching this limit.

Pension Liberation Schemes

There are certain organisations which are advertising services which claim to enable people with pension rights to transfer the capital value of their pension pot to a scheme overseas. They then claim that this gives the person access to the pension earlier than would be available under UK law or to take a lump sum from the pension pot which would be in excess of that allowable under UK tax law. These schemes are potentially illegal and both the UK tax authorities and the Pension Regulator are investigating such transactions.

There are also potentially considerable risks involved when transferring funds outside of UK jurisdiction in this way and persons effecting such transfers could be leaving themselves open to the risk of criminal and fraudulent activity.

We would recommend that any person contemplating such a transfer should consider taking independent financial advice from a legitimate UK financial advisor.

Pension Auto Enrolment

As you may be aware from recent correspondence, press and the media, employers will have to start automatically bringing employees into a pension scheme. This is being phased in over a number of years starting from 1st October 2012. The LGPS is a “qualifying scheme” for the purposes of auto enrolment and therefore auto enrolment will have no impact upon your membership of the LGPS.

Customer Service Excellence Award

The Northumberland Pension Team has undergone a review of their Customer Service Excellence Award accreditation and retained the award. The Customer Service Excellence Award is a central government initiative which recognises excellence in the delivery of a public service.

Application of the Scheme Regulations

This leaflet is intended to give general information only and it does not confer any rights upon the reader. In all cases pension rights earned in the Local Government Pension Scheme will be determined in accordance with the statutory regulations governing the Local Government Pension Scheme.

Contacting The Pensions Team

The Pensions Team are there to help you with any matter relating to your LGPS pension entitlement. You can contact them by phone, letter and online. Contact details are as follows: -

Mr Alan Whittle
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Northumberland County Council

CUSTOMER SERVICE EXCELLENCE

lgps look forward with confidence

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