

SURREY COUNTY COUNCIL

PENSION FUND BOARD

DATE: 14 FEBRUARY 2014

LEAD OFFICER: SHEILA LITTLE, CHIEF FINANCE OFFICER

SUBJECT: REVIEW OF PENSION ABATEMENT POLICY



SUMMARY OF ISSUE:

The introduction of the new Local Government Pension Scheme (LGPS) from 1 April 2014 requires the pension fund administering authority (AA) to review its discretionary pension policy on the abatement of retirement pensions when a scheme member in receipt of a LGPS pension is re-employed in local government employment.

The regulations also require the AA to make policy decisions in relation to other pension matters that do not require a formal written policy statement. One such policy decision that requires review is whether or not to require medical clearance of scheme members before they are permitted to purchase an additional pension.

RECOMMENDATIONS:

It is recommended that the Board :

1. adopt a policy that continues with the existing practice of not abating the pension of a scheme member that is re-employed by a local government pension scheme employer as outlined in paragraphs 1-18.
2. adopt a policy that continues with the existing practice requiring a scheme member to receive medical clearance before being permitted to purchase an additional pension as outlined in paragraphs 19-25.

REASON FOR RECOMMENDATIONS:

Adopting a policy that does not abate pension upon re-employment will simplify pension administration and will be more compatible with modern day working practices such as working for longer, part time working and flexible retirement.

Adopting a policy that requires scheme members to be medically cleared before being permitted to purchase an additional pension will reduce the risk of employers incurring significant costs if a member is retired on permanent ill-health grounds.

DETAILS:

Background

Pension Abatement

1. The Local Government Pension Scheme Regulations require that each pension fund administering authority must formulate and keep under review a policy on pension abatement. Pension abatement is the extent, if any, to which a scheme member's pension in payment is reduced or suspended where the member has entered a new employment that entitles them to re-join the Local Government Pension Scheme (LGPS).
2. If an administering authority's policy is to abate pensions on re-employment it means that any amount by which the annual pension in payment, plus the annual pay from the new employment, exceeds the indexed annual pay from the former employer, results in a reduction in pension on a pound for pound basis during the period of re-employment. The indexed annual pay means that CPI (consumer price index) increases are applied to bring the member's pay from the former employer up to today's value to ensure a fair comparison.
3. The following example illustrates how abatement works in practice:

EXAMPLE

Indexed rate of pay of former employment	£37,000
Annual pension in payment	£ 6,000

Therefore, in this example, the member can earn up to £31,000 a year before the pension would have to be abated, because the pension (£6,000) plus the new salary (£31,000) does not exceed the former pay of £37,000.

If however the member earned say £35,000 a year in the new employment, the pension would have to be abated by £4,000 a year because the pension (£6,000) plus the new salary (£35,000), exceeds the former pay (£37,000) by £4,000.

Therefore, if the member earned in excess of £37,000 in the new employment, the pension in payment would be completely abated.

4. When formulating an abatement policy, the pension regulations require that the administering authority has regard:
 - a) to the level of potential financial gain at which it wishes abatement to apply;
 - b) to the administrative costs which are likely to be incurred as a result of abatement in the different circumstances in which it may occur; and
 - c) to the extent to which a policy not to apply abatement could lead to a serious loss of confidence in the public service.

5. The abatement of pensions has been a feature of most public sector schemes since the 1950s. Until 1998 it was compulsory for local government administering authorities to apply the abatement provisions in full. However, in 1998 the government changed the pension regulations to provide administering authorities with the discretion to decide, after consultation with the fund scheme employers, to what extent, if at all, the abatement provisions should apply.
6. The general principle of applying the abatement provisions to public sector pensions is to ensure that a member in receipt of a public sector pension should not be financially better off if they became re-employed in the public sector. This can only ever be partially achieved because the abatement provisions are scheme specific. This means that the member's pension is only subject to abatement if the re-employment occurs with an employer with access to the same pension scheme as the pension is being paid from.
7. For example, if a local government pensioner takes up employment with a NHS Primary Care Trust the pension would not be affected and vice versa, because local government and NHS employees are eligible for membership of different schemes.
8. If however, for example, a retired library assistant applied for an administrative job with a local government employer, because a library assistant post and administrator post would both come under the local government pension scheme the pension would be subject to abatement. However, if a retired Teacher applied for the same administrator post the teacher's pension would not be subject to abatement because the teacher's pension would be paid from the Teachers Pension Scheme, even though the retired teacher and retired library assistant may have been employed by the same employer.
9. The pension regulations governing abatement are not particularly robust in that it is relatively easy to circumvent the abatement provisions with the help of the pensioner's new employer. For example, as the assessment of the pensioner's salary in the new employment is based on contractual entitlement, it is possible for an employee to be contracted for a lower number of hours but then work non-contractual additional hours that cannot be taken into account for abatement purposes. It is also possible to avoid the abatement provisions by becoming employed on a number of fixed-term contracts or to work as a consultant.
10. Many local authorities now consider that pension abatement is no longer compatible and, in some cases, conflicts with modern day working practices. For example, it is acknowledged that people will need to work for longer and pension abatement is considered a barrier for some employees to do this. Pension abatement can also conflict with the LGPS flexible retirement provisions which allow eligible employees, with their employers consent, to draw their pension and continue working on a reduced hours basis without the abatement provisions applying.

11. Pension abatement is a difficult process to administer. All pensioners need to be clearly informed in writing that they are required to inform Pension Services if they are re-employed in local government employment. Unfortunately, past experience has shown that many pensioners still failed to advise Pension Services when they were re-employed and this may only be detected either when Pension Services specifically writes to all pensioners or through the National Fraud Initiative run by the Audit Commission every two years.
12. Although several pensioners do get re-employed in local government employment, past experience has shown that a very small proportion, around 4%, actually required abatement of their pensions. However, all cases of re-employment have to be investigated even though the outcome rarely requires the pension to be abated. This involves writing to the new employer to confirm the level of the pensioner's pay and then carrying out the calculation and informing the pensioner of the outcome. In the event that the pensioner has a contractual change in pay then the whole procedure has to be repeated. The whole abatement process takes up a considerable amount of administrative resources.
13. The process is likely to be even more complex under the new LGPS because the new scheme regulations do not allow the part of a member's pension that accrues from 1 April 2014 to be taken into account when considering abatement.
14. The fund's abatement policy was last reviewed in June 2010 when it was decided that in future, pensions should not be abated when a pensioner takes up further local government employment and, in cases where pensions were currently being abated, that they should be reinstated in full. This decision had the overwhelming support of the fund employers.
15. At the time this decision was made the fund had 14,837 pensions in payment at an annual cost of £74.5 million. The number of pensions that were being abated in part or full amounted to 21 at a total abatement of £86,000 a year.
16. The reasons that led to the council resolving in June 2010 to no longer apply the abatement provisions as outlined in the above paragraphs, are still valid today. In addition, the change in the pension regulations that only enables the pension that has accrued to 31 March 2014 to be abated together with the uncertainty surrounding how we would treat the pensioners that have been re-employed since abatement of pensions ceased in 2010, makes it even more impracticable to change the existing policy.
17. It is therefore recommended that there is no change to the existing policy in that pensions are not abated when a LGPS pensioner is re-employed in local government employment.
18. The pension abatement policy will be kept under review and will be brought for approval to future Board meetings when any material revision is required.

Purchase of Additional Pension – Medical Clearance

19. The pension scheme enables a scheme member to pay additional pension contributions or make a lump sum payment to purchase an additional pension. The maximum additional pension that a scheme member can purchase under the new scheme will increase from £5,000 to £6,500 a year.
20. In the event that a scheme member who is paying additional contributions is retired on permanent ill health grounds the additional contributions remaining are deemed to have been paid and the additional pension awarded in full from the date of early retirement.
21. In the event that a scheme member who has made a lump sum payment to purchase an additional pension is retired on permanent ill health grounds the full additional pension is also paid from the date of early retirement rather than the normal retirement age.
22. In both scenarios in paragraphs 20 and 21 above the resultant cost to the scheme employer would be substantial. For this reason the scheme regulations enable administering authorities to require that all scheme members who elect to purchase an additional pension must first be medically cleared before being allowed to do so.
23. The fund's current policy is that it requires all scheme members who elect to purchase an additional pension to receive medical clearance before being permitted to do so to ensure that there is no medical reason present that may cause the member to be retired early on permanent ill health grounds.
24. The medical clearance is obtained through the County Council's occupational health service at a cost to the scheme member of £40.00.
25. It is recommended that the fund should continue to require that medical clearance is obtained from the County Council's occupational health service before a member is permitted to purchase an additional pension.

CONSULTATION:

26. The Chairman of the Pension Fund has been consulted on the proposed document and has offered full support for the proposal.

RISK MANAGEMENT AND IMPLICATIONS:

27. Adopting a policy that requires scheme members to be medically cleared before being permitted to purchase an additional pension will reduce the risk of employers incurring significant costs if a member is subsequently retired on permanent ill-health grounds.

FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

28. Any amount of a scheme member's pension that could be abated would result in a saving to the fund. However, in relative terms, this saving would be an insignificant amount compared to the total value of pensions in payment and the benefits that would be derived from not having a policy to abate pensions.

CHIEF FINANCE OFFICER COMMENTARY

29. The administrative difficulties and incompatibility with modern working practices associated with the abatement of pensions far outweigh the financial benefit the fund would receive from abating a small number of pensions. Requiring medical clearance to be obtained before a member can purchase an additional pension is a sensible precaution to reduce the risk of additional costs being incurred by the fund if the member is retired on permanent ill health grounds. On this basis, Chief Finance Officer is satisfied that all material, financial and business issues and possibility of risks have been considered and addressed in this report.

LEGAL IMPLICATIONS – MONITORING OFFICER

30. There are no legal implications or legislative requirements associated with this report.

EQUALITIES AND DIVERSITY

31. The approval of these policies will not require an equality analysis, as the initiative is not a major policy, project or function being created or changed.

OTHER IMPLICATIONS

32. There are no potential implications for council priorities and policy areas.

WHAT HAPPENS NEXT

33. The following next steps are planned:
- The Board's decision regarding its proposed policy on abatement of pensions will be sent to the scheme employers for consultation.
 - A further report will be submitted on the outcome of the consultation at the next board meeting.

Contact Officer:

Paul Baker
Pensions Manager

Consulted:

Pension Fund Board Chairman

Annexes:

None

Sources/background papers:

None
