



LOCAL GOVERNMENT PENSION SCHEME

Overview of Pensions Strain

The Local Government Pension Scheme (LGPS) is a final salary scheme whose benefits are defined in regulation.

The benefits are paid for from the pension fund held by the administering authority (Nottinghamshire County Council).

The Pension Fund is paid for by its participating employers and employees largely in the form a % pension contribution and the investment income derived from it.

The Pension Fund's actuary reviews the fund every 3 years and makes adjustments to the employer rates based on current shortfall of funding level and expected income and expenditure.

The actuary makes a number of assumptions amongst which are anticipated levels of early retirements. Prior to 1998 it was those assumptions that were relied upon for the funding of early retirements and that combined with a then 5yr valuation period led to difficulties in accurately budgeting for the employers rates.

In 1998 following the Audit Commissions report 'retiring nature' the LGPS imposed employer costs for employer related early retirements.

Fund costs relating to redundancy and efficiency retirements, which were seen to be largely in the control of the employer, were then recharged directly to the employer using the term 'pensions strain'. Ill health retirements were not charged for in this manner unless there were exceptional circumstances where the actuary's assumptions were far exceeded.

The critical retirement age (CRA) which is a combination of different normal retirement date protections including the 85yr rule (based on service plus age) is used to determine whether a benefit is to be reduced, if it is paid before the age of 65.

Members who voluntarily leave after 60 may claim early payment of benefits. If they have met their CRA there will be no reduction, but if they have a reduction they may defer receiving payment until there is no reduction.

In redundancy and efficiency cases if the member is over 50, the LGPS must release the benefits immediately and unreduced irrespective of whether the CRA has been met.

Pension strains occur on redundancy and efficiency where the member leaves before age 60 (relating to the early payment of the pension, and where the CRA has not been met, the payment of an unreduced pension). Also where the member leaves after age 60 where the CRA has not been met (based on the payment of an unreduced pension).

Pension strains may also occur where the employer allows voluntary retirement with the early release of pension (Reg 31). This is similar to redundancy and efficiency cases but as the payment of a reduced pension is allowed (where the CRA is not met) for certain cases the reduction is sufficient to offset any strain costs.

Information regarding strain is distributed from time to time to all our participating employers.

Strain was introduced in 1998 and at that time a spreadsheet was made available for employers to perform their own estimated costs. The spreadsheet was withdrawn in 2002 (and not replaced) following a change in the method of calculation of strain costs. In 2005 the strain costs were increased by 25% at the recommendation of the Funds actuary.

Currently (2007) we calculate strain through our Pensions member records software (AXISe). The basis of the calculation AXIS performs is described in the Actuary's 2002 'Report on Early Retirement Costs' which can be found in the employers section of the Nottinghamshire Pension Funds Website at www.nottinghamshirepensionfunds.org.uk

If an employer wishes to know what costs they may incur in respect of the retirement of an employee they should contact Nottinghamshire's Pensions Office for an estimate. Employers should of course seek information on all areas of potential cost before making financial decisions and pensions should be a part of that process.

Payment of strain incurred should be made at the time of the members retirement. Payment options are either as a single sum or, at the discretion of the Pensions Office, by 3 instalments over 2 years. Payment by instalments incurs a slightly higher cost to take into account the payback period.

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