

## The Pensions Line Special

Keeping you on track with all the LGPS news



### The End of “Contracting Out”

“Contracting out” will be abolished from 6 April 2016.

#### The history

Contracting out was introduced in April 1978 to relieve members of approved pension schemes of the burden of paying for both an occupational pension and the State Earnings Related Pension Scheme (SERPS). Reduced National Insurance contributions (NICs) are payable; currently the reductions are 1.4% for employees and 3.4% for employers on earnings between £111 and £805 per week.

#### What’s happening?

The Pensions Act 2014 introduced a new ‘single tier’ State pension payable to those reaching State pension age (SPA) from 6 April 2016. The current State pension system, which is comprised of the basic state pension, the additional “earnings linked” state pension (commonly known as S2P, and formerly SERPS) and the pension credit, will be abolished. This move means that contracting-out for defined benefit schemes (such as the LGPS) will also be abolished from 6 April 2016.

#### The financial impact

##### Employer costs

The abolition of contracting out will see the payroll bill of LGPS employers increase by 3.4% of relevant earnings and employees’ net pay reduce by 1.4% of relevant earnings. This reduction could increase the take-up of the 50/50 option and encourage opt-outs.

##### ‘Recycling’

The Pensions Act 2014 contains a ‘statutory override’ for private sector employers who can increase employee contributions or reduce future pension accrual to offset the increase in NICs, but this is not an option that is open to LGPS employers. However we understand that the LGA and DCLG may agree a method by which “recycling” of these extra costs takes place within the LGPS. It also worth noting that any agreed recycling would only apply within the LGPS and not for employees in other public sector schemes (e.g. the Teacher’s scheme in the case of academies) where separate arrangements would have to be put in place.

#### Getting ready for April 2016

With no chance of reversing the Government’s decision to end contracting out, it would appear that LGPS employers can only prepare for the change and take appropriate action such as:

- Determine what the additional employer payroll cost will be;
- Determine the fund cash flow impact in the event that 50:50 and opting out numbers increase;
- Communicate with pension fund members on the implications for them

## Conclusion

The removal of contracting out is going to have financial implications for all LGPS employers and employees. Employers will now have to make further savings to already hard hit budgets to fund the expected additional payroll costs. Some hope is on the horizon if the additional cost can be 'recycled' into LGPS funds but this is likely to be complicated and not available to the many non-local authority employers. The increase in employee NI contributions is likely to lead to an increase in opt-outs and higher take up of the 50/50 option although this would help reduce employer costs.

Peninsula Pensions  
Great Moor House  
Bittern Road  
Sowton Industrial Estate  
Exeter EX2 7NL

Email: [pensions@devon.gov.uk](mailto:pensions@devon.gov.uk)  
Web: <http://www.peninsulapensions.org.uk/>



Devon  
County Council