

The Local Government Pension Scheme



lgps Increasing Scheme Benefits

A guide to increasing your benefits in the Local Government Pension Scheme

Increasing Your Pension Benefits

Background

Since 6 April 2001 members of the Local Government Pension Scheme (LGPS) have had the following choices to consider when deciding how to increase their benefits via a pension arrangement:

- purchasing extra years of membership (commonly known as 'added years') in the LGPS
- paying additional voluntary contributions (AVCs) via the LGPS to the scheme's AVC plan (commonly known as scheme AVCs or in-house AVCs)
- paying free-standing additional voluntary contributions (FSAVCs) to a FSAVC provider of your personal choice
- paying contributions to a concurrent stakeholder pension scheme
- paying contributions to a concurrent personal pension scheme
- repaying contributions previously refunded under the LGPS

Not all of the above alternatives will apply to every individual.

This booklet sets out to provide you with basic information on each of the above options. The meaning of words in **bold type** in the text of the booklet are explained in the glossary at the front of this booklet. A useful table comparing the main options is also included.

Why should I consider increasing my pension benefits?

Most of us look forward to a happy and comfortable retirement and in order to have that little bit extra during your retirement years it is worth considering paying extra contributions, which are a tax efficient way of topping up your income in retirement.

It should be noted that extra contributions can also be paid to increase the level of a spouse's or civil partner's pension payable, or to increase the amount of the lump sum payable, if you die in service.

Are there any limits on how much I can contribute to increase my pension benefits?

There is no limit on the amount of contributions you can pay, although there is a limit on the number of added years you can buy in the Scheme. However, you can only receive tax relief on contributions up to 100% of your taxable earnings. Additionally, unless you have enhanced protection, there will be a tax charge if in any year, other than the year in which all your pension benefits have become payable, the value of your pension savings has increased in excess of the annual allowance. There will also be a tax charge if, when you draw your benefits, the value of all your pension savings exceeds the lifetime allowance (or, if you have opted for it, the primary lifetime allowance protection or enhanced protection). Tax will be payable on any excess amount.

As your normal LGPS contributions are either 6% or 5% this leaves a significant proportion of your taxable earnings that you can invest in additional contributions or AVCs, although from 6 April 2006 the additional years of membership in the LGPS you may opt to purchase is limited to 6 years 243 days.

The following sections provide you with details on the various options available.



The Options Explained

Pay additional contributions to purchase extra years of membership in the LGPS.

This option allows you to purchase additional years of membership in the LGPS.

From 6 April 2006, the maximum number of additional years you may opt to purchase is 6 years 243 days. Contributions to purchase additional years of membership in the LGPS are deducted direct from your pay and the tax relief (at your highest rate) is automatically given through the payroll. This means that tax is calculated on your pay after your pension contributions have been deducted.

If you elect to pay additional contributions to purchase extra

membership in the LGPS, you will start paying the additional contributions from your next birthday. The contributions would be due to cease on the day before your 65th birthday (or, in some cases, on an earlier date where the contract to pay additional contributions was taken out before 1 October 2006).

The amount of contributions you pay will depend on your age when you start paying the additional contributions and the number of additional years of membership you wish to purchase. A quote can be obtained by writing to the Pensions Section (see address on page 27). You should note that, before an election to pay additional contributions can be accepted, you may be required to produce, at your own expense, a medical report from a registered medical practitioner to show that you are in reasonably good health.





If, whilst paying additional contributions, you go on sick leave with reduced or no pay, your contributions will be deemed to have been paid in full. However, during any other period of absence you will be required to continue paying the additional contributions in full.

The additional years of membership will count towards any minimum period of membership you are required to have under the LGPS to be entitled to a benefit and will count in working out the amount of your benefits when you leave or retire.

So, if you decide to purchase additional years of membership in the LGPS you will not only know what percentage of your **pay** it will cost you each month, but you will also know what proportion of your **final pay** you will receive in return for the additional contributions.

You may choose to cease paying additional contributions at any time by giving written notice of your wish to do so to both the authority administering the pension fund and to your employer. You would be credited with the proportion purchased to the date of cessation.

(Please note: If you then wished to re-commence payment you would be required to take out a new contract which could not start until your next birthday and the contribution rate for which would be higher (as it is linked to your age on taking out the contract).

If you leave (other than on the grounds of permanent ill health) before completion of the contract to purchase additional years of membership you will be credited with the proportion purchased to the date of cessation. However, if within 12 months of leaving you move to another employer that participates in the

LGPS you will be able to continue paying the additional contributions provided you aggregate your pension rights and, within 3 months of rejoining the LGPS, you pay the additional contributions that would have been due in respect of the period of any break between the employments.

However, if you are retired on grounds of permanent ill health or you die in service while paying additional contributions to increase your membership, the contributions will be deemed to be fully paid. This means that the full amount of additional membership being purchased will be used in the calculation of the benefits due.

Should you be made redundant or retire on grounds of efficiency at least 12 months after you elected to pay additional contributions, you will be given the opportunity to pay the remaining contributions due in a lump sum. If you

choose not to do so, you will be credited with the proportion purchased to the date of redundancy or retirement on the grounds of efficiency.

If you draw benefits on flexible retirement you will, unless you opt to stop paying before you take flexible retirement, continue to pay for any additional membership you are purchasing. The benefits from the additional membership will not be paid until you finally retire, unless you have opted to stop paying the additional contributions before you take flexible retirement.

To pay additional voluntary contributions (AVCs) via the LGPS to the scheme's AVC plan (commonly known as scheme AVCs or in-house AVCs)

If you choose to pay AVCs under the LGPS, the AVCs are invested separately in funds

managed by an insurance company or building society. You have your own personal account that, over time, builds up with your contributions and the returns on your investment which are free of capital gains tax.

You may be offered a range of AVC investment routes. For example, you may be able to invest your contributions in a 'with-profits' fund, a 'unit-linked' fund, a 'deposit' fund, an 'ethical' fund, a 'lifestyle' fund, an index 'tracker' fund etc. or a combination of funds. It is for you to choose which fund, or combination of funds, you wish to have your contributions invested in. Your decision is likely to be influenced by factors such as your attitude to investment risk and how close you are to retirement.

An election to pay AVCs must be made in writing. Payments commence from

the next available pay day after your election has been accepted and you may vary or cease payment at any time whilst you are contributing to the LGPS. The authority administering the pension fund may specify a minimum contribution that must be paid.

AVCs are deducted direct from your pay and the tax relief (at your highest rate) is automatically given through the payroll. This means that tax is calculated on your pay after your pension and AVC contributions have been deducted.

You may be able to transfer any previously accrued FSAVCs and in house AVC funds in another scheme to an LGPS in house AVC scheme while you are a contributing member of the LGPS.

At retirement the accumulated fund in your account is used to buy you an





annuity from an insurance company, bank or building society (but you can defer purchasing an annuity until the eve of your 75th birthday at the latest). If you work beyond age 65 you will not be able to purchase an annuity until you stop working and retire, or you reach the eve of your 75th birthday, whichever occurs first.

The annuity can be bought from the insurance company or building society with whom the AVCs were invested. Alternatively, it can be purchased from another annuity provider so that you can benefit from the best annuity rates available at the time.

An annuity is an amount of additional pension benefit. When you buy an annuity you can choose the type of pension that best suits your circumstances. For example, you could buy a flat rate annuity (i.e. one that

never increases), one that is increased each year by a fixed rate, or one that increases in line with the Retail Prices Index. You can choose whether to include a prospective widow's / widower's / **civil partner's** pension (should you predecease your spouse / **civil partner**). Clearly, the level of the annuity will, in part, depend on which of the above elements you wish to include.

Annuities are subject to annuity rates which in turn are affected by interest rates. When interest rates rise, the organisation selling annuities is able to obtain a greater income from each pound in your AVC fund, and therefore can provide a higher pension. Conversely a fall in interest rates reduces the pension which can be purchased.

Alternatively, upon leaving the LGPS with an immediate payment of pension benefits you will be able to use the

accumulated fund in your AVC account to buy a top-up pension from the LGPS. This will provide an inflation proofed pension and dependants' benefits.

You can use part of your accumulated fund to buy a top-up pension from the LGPS and the balance of your fund to purchase an annuity.

In certain circumstances, such as retirement on ill health grounds or cessation of payment of AVCs before retirement, the LGPS currently makes provision for members to opt to convert AVCs into LGPS membership provided you commenced payment of the AVCs prior to 13 November 2001. You can even take your AVC fund as cash. At retirement, you can take all or part of the accumulated fund in your in house AVC as a tax free lump sum if you draw it at the same time as your LGPS pension benefits, provided when added to the LGPS lump sum it

does not exceed 25% of the overall value of your LGPS benefits (including your AVC fund) or, if less, 25% of the lifetime allowance less an adjustment for the value of any other pension benefits you are already drawing. If you defer drawing your AVC, you can draw up to 25% of the value of your AVC fund as a tax free lump sum at the time you decide to take benefits from your AVC fund.

If you draw your main LGPS benefits on flexible retirement you will not normally be able to take your AVC benefits. The benefits from the AVCs will not normally be paid until you finally retire.

Whilst you are in the LGPS you can also pay AVCs to increase your death in service lump sum cover over and above the two times **final pay** provided by the LGPS, or to provide additional dependants' benefits.

If you take out an AVC for additional

death benefits you may be asked to complete a medical questionnaire and you may be asked to undergo a medical examination at your own expense before your election is accepted.

More information on AVCs, including an application form, is available from the Pensions Section (see details at the end of this document).

There will be a tax charge if in any year, other than the year in which all your pension benefits have become payable, the value of all your pension savings has increased in excess of the **annual allowance** or if, when you draw your benefits, the value of all your pension savings exceeds the **lifetime allowance** or any **primary lifetime allowance protection** or **enhanced protection** you may have. Tax will be payable on any excess amount.

Under the LGPS your employer may

establish a shared cost AVC arrangement (SCAVC) to which, at your option, both you and your employer contribute. The establishment of such an arrangement is at the employer's discretion and your employer's policy with regard to it must be included in their Policy Statement (a copy of which you can ask for).

To pay free-standing additional voluntary contributions (FSAVCs) to a FSAVC provider of your personal choice

FSAVCs work in much the same way as AVCs under the LGPS. However, there are some important differences. These are:

- You must choose (and monitor) the financial institution to invest your FSAVCs. The main features for consideration would include contract charges (policy fees,





annual management charges, bid / offer spreads, location rates), the types of investment routes on offer, historical investment performance, the financial strength of the provider, and the provider's long term commitment to the FSAVC market. You would also wish to ascertain whether there is a minimum payment, how often you can choose to vary the amount of your FSAVC and whether there are any charges for doing so, whether there are any penalties for stopping payment of FSAVCs or for transferring to another scheme, and whether there are any penalties for purchasing an annuity on the open market rather than with the organisation to whom you had paid the FSAVCs.

- You must make the necessary arrangements. Contributions will not be deducted from your pay. Instead,

you will need to make arrangements to pay contributions to the FSAVC provider e.g. by a standing order or direct debit mandate from your bank or building society account. The FSAVC provider will claim the basic rate tax relief from HM Revenue and Customs and credit it to your FSAVC contract. If you are a higher rate tax payer you will need to claim the higher rate tax relief on your annual tax return.

- FSAVCs can be drawn at any time from age 50 up to the eve of your 75th birthday regardless of whether or not you have retired and are drawing your LGPS pension. The accumulated fund in your FSAVC account is usually used to buy you an annuity from an insurance company, bank or building society but, if the scheme rules permit, you can opt for an **unsecured pension** if you defer

the purchase of an annuity.

(Please note: Schemes are required to increase the earliest age that benefits can be drawn from age 50 to age 55 by 2010. Benefits can be drawn from an earlier age on the grounds of incapacity i.e. physical or mental impairment).

- FSAVCs cannot be transferred directly into the LGPS to purchase membership whereas, in certain circumstances, AVCs can.
- AVCs cease on leaving the LGPS (but the value of your AVCs can be transferred to another scheme if you transfer your LGPS benefits) but FSAVCs can carry on being paid into the same contract provided you rejoin another occupational pension scheme.

- Only 25% of the value of the FSAVC fund can be taken as a tax free lump sum at the time you decide to take benefits from your FSAVC fund.

To contribute to a concurrent personal pension plan or stakeholder pension scheme

You may, if you wish, be a member of the LGPS and make your own arrangements to pay contributions from the same earnings to a personal pension plan or stakeholder pension scheme.

If you choose to also pay into a stakeholder or personal pension scheme, the contributions you make to it are invested in funds managed by an insurance company. You have your own personal account that, over time, builds up with your contributions and the returns on your investment.

Stakeholder pension schemes will have to satisfy minimum standards relating to the maximum charge that can be made and there should be no penalties on discontinuing membership. This does not apply to personal pension schemes.

If you choose to contribute to a stakeholder or personal pension scheme you must make the necessary arrangements. Contributions will not be deducted from your pay (unless your employer voluntarily agrees to do so). Instead, you will need to make arrangements to pay contributions to the provider e.g. by a standing order or direct debit mandate from your bank or building society account. The provider will claim the basic rate tax relief from HM Revenue and Customs and credit it to your personal fund. If you are a higher rate tax payer you will need to claim the higher rate tax relief on your annual tax return.

Benefits from a Stakeholder or personal pension scheme can be drawn at any time from age 50 (please see note on previous page regarding the earliest age that benefits can be drawn) up to the eve of your 75th birthday regardless of whether or not you have retired and are drawing your LGPS pension. The accumulated fund in your stakeholder or personal pension account is usually used to buy you an annuity from an insurance company, bank or building society but, if the scheme rules permit, you can opt for an **unsecured pension** if you defer the purchase of an annuity. The annuity can be bought from the insurance company with whom you invested your contributions. Alternatively, it can be purchased from another annuity provider so that you can benefit from the best annuity rates available at the time. It should be noted that up to 25% of your accumulated fund may be taken as a tax





free lump sum on retirement or, if less, 25% of the **lifetime allowance** less an adjustment for the value of any other pension benefits you are already drawing. An annuity is an amount of additional pension benefit. When you buy an annuity you can choose the type of pension that best suits your circumstances. For example, you could buy a flat rate annuity (i.e. one that never increases), one that is increased each year by a fixed rate, or one that increases in line with the Retail Prices Index. You can choose whether to include a prospective widow's / widower's / **civil partner's** pension (should you predecease your spouse / **civil partner**). Clearly, the level of the annuity will, in part, depend on which of the above elements you wish to include.

Annuities are subject to annuity rates which in turn are affected by interest rates. When interest rates rise, the organisation selling annuities is able to

obtain a greater income from each pound in your personal fund, and therefore can provide a higher pension. Conversely a fall in interest rates reduces the pension which can be purchased.

To repay a previous refund of LGPS contributions.

If you ceased Local Government employment between 1 April 1974 and 31 December 1979 with less than five years membership in the LGPS and you claimed a refund of contributions, you may repay the refund plus interest. The repayment must be made within six months of re-joining the LGPS, or such longer period as your current and former administering authority may allow. This is an administering authority discretion; you can ask your current and former administering authorities what their policies are on this matter. Once the repayment has been made, the period of

membership will again count for pension purposes.

Are there other alternative investments?

Individuals often have to consider whether they should top up their pension benefits or, in addition to their basic contributions to the LGPS, save for retirement through an alternative medium e.g. National Savings, Individual Savings Accounts (ISAs), Offshore investments, venture capital trusts, etc. which have some forms of in-built tax advantage. To some extent the decision will depend upon the objectives of each individual. The aforementioned list is by no means exhaustive and should not be seen in any way as an endorsement of the product. Individuals should seek their own independent financial advice.

Disclaimer

The information in this booklet is based on our understanding, at the date of printing, of current pensions and taxation legislation, and of HM Revenue and Customs practice, all of which are liable to change.

The Pensions Section is not authorised under the Financial Services Act to give scheme members individual advice. If you wish to receive individual and independent advice you may wish to talk to a registered independent financial adviser. You will personally need to meet the cost of any charges made for the advice.

Further Information

Further information about LGPS AVCs is available by contacting us on the details at the end of this guide. The Pensions

Section will also be pleased to provide an individual quotation on the purchase of additional years of membership in the LGPS.

You can obtain information on a wide range of financial topics, including how to go about finding a financial adviser, from the Financial Services Authority. Call the FSA Consumer Helpline on 0845 606 1234 or visit the FSA Consumer Help website at www.fsa.gov.uk/consumer

There is a DSS booklet entitled 'Stakeholder Pensions - Your Guide (PM8)' available by telephoning 0845 7 31 32 33 or on-line from www.pensionguide.gov.uk

General note: In certain circumstances people who left the LGPS between 1.4.74. and 31.12.79. with less than 5 years membership of the scheme, and who took a refund of contributions, may repay that refund in order to again count the

service. For further information see the main guide.



Glossary

Annual Allowance

This is the amount by which the value of your pension benefits may increase in any one year (disregarding the year that that all your benefits become payable) without having to pay income tax at 40% on the excess. The **annual allowance** is set by the Treasury and for

2007/2008 is £225,000. Most scheme members will not be affected by the **annual allowance**. For calculating the increase in value of your LGPS benefits, the first year ran from 6 April 2006 to 31 March 2007; subsequent years run from 1 April to 31 March. If you exceed the **annual allowance** in any year you are responsible for reporting this to HM Revenue and Customs on your Self-assessment tax return and for paying the annual allowance tax charge. Your **administering authority** will be able to give you the information you require on the increase in the value of your LGPS benefits including any additional voluntary contribution (AVC) arrangement you may have. The assessment covers any pension benefits you may have in all tax-registered pension arrangements – not just the LGPS. Please note, however, that the annual allowance tax charge will not apply if you have registered to have **enhanced protection** (but only if you



keep **enhanced protection** throughout the relevant tax year).

Civil partner

A civil partnership is a relationship between two people of the same sex ("civil partners") which is formed when they register as civil partners of each other.

Final Pay

This is the figure used to calculate most of your pension benefits and is normally your **pay** in the last year before you retire, or one of the previous two years' pay if that amount is higher. For a part-time employee, the figure used is normally the **pay** you would have received if you had worked whole-time. If your **pay** is reduced because of sickness, the **final pay** is taken to be the **pay** you

would have received if you had not been sick. During any period of maternity, paternity or adoption leave in respect of which you pay (or are deemed to have paid) pension contributions, **final pay** includes the **pay** you would have received had you not been on maternity, paternity or adoption leave.

Lifetime Allowance

This is the total capital value of all pension benefits you can have without triggering an excess benefits tax charge. If the value of your pension benefits when you draw them (not including any state retirement pension, state pension credit or any spouse's, civil partner's or dependant's pension you may be entitled to) is more than the **lifetime allowance**, or more than any **primary lifetime allowance protection** or **enhanced protection** you may have, you will have to pay tax on the excess

benefits. The **lifetime allowance** is set by the Treasury and for 2007/2008 is £1.6million. The **lifetime allowance** covers any pension benefits you may have in all tax-registered pension arrangements – not just the LGPS. Most scheme members' pension savings will be significantly less than the **lifetime allowance**. For pensions that start to be drawn on or after 6 April 2006, the capital value of those pension benefits is calculated by multiplying your pension by 20 and adding the lump sum – so, for example, an employee earning in excess of £130,000 per annum and with 40 years membership in the LGPS could be affected. For pensions already in payment prior to 6 April 2006, the capital value of these is calculated by multiplying the current annual rate, including any pensions increase, by 25. Any lump sum already paid is ignored in the valuation.

Pay

This is your normal salary or wages plus any shift allowance, bonuses, contractual overtime, Maternity Pay, Paternity Pay, Adoption Pay and any other taxable benefit specified in your contract as being pensionable. **Pay** does not include non-contractual overtime, travelling or subsistence allowances, pay in lieu of notice, pay in lieu of loss of holidays, school achievement awards, any payment as an inducement not to leave before the payment is made, nor (apart from some historical cases) the monetary value of a car or pay received in lieu of a car.

Primary lifetime allowance protection and enhanced protection

Primary protection is aimed at protecting benefits earned up to 5 April 2006 in respect of those high earners affected by the introduction of the

lifetime allowance from 6 April 2006. Under HM Revenue and Customs rules, if the value of your pension benefits at 5 April 2006 exceeded the 2006/2007 **lifetime allowance** of £1.5million, you can register for **primary protection** so that you have an **individual lifetime allowance** based on how much your benefits at 5 April 2006 exceeded the value of the 2006/2007 standard **lifetime allowance**. Your individual lifetime allowance increases at the same rate as the standard **lifetime allowance**. You can also register for **enhanced protection**, as well as **primary protection**, if the value of your pension benefits at 5 April 2006 exceeded the 2006/2007 **lifetime allowance** of £1.5million, or you can register for **enhanced protection** if you believe they may in the future exceed the standard **lifetime allowance**. Under **enhanced protection** you do not pay tax on benefits in excess of the **lifetime**

allowance provided your benefits at 5 April 2006 have not increased since then beyond certain limits (in general terms, by more than the greater of 5% per annum, the increase in the Retail Price Index or increases in your pensionable pay). If the limit is exceeded, you will pay tax on the excess. You will lose **enhanced protection** if you pay contributions into a money purchase pension arrangement (e.g. pay into the LGPS in house AVC facility) or if you start a new pension arrangement, or if you transfer your LGPS benefits to another defined benefit pension scheme. You can also voluntarily give up **enhanced protection** by giving notice that you no longer wish to keep it.

If you lose **enhanced protection** you must notify HM Revenue and Customs within 90 days. Failure to do so could result in a fine of up to £30,000.



You have to register with HM Revenue and Customs by 5 April 2009 if you wish to obtain **primary** or **enhanced protection**. The relevant forms are available at <http://www.hmrc.gov.uk/pensionschemes/protection.htm>

Please note: A provision in the Finance Act 2006 has ensured that those with enhanced protection will not lose it if they are paying AVCs at 5 April 2006 purely for extra life assurance cover and carry on doing so after that date provided the terms are not varied significantly from those that were applicable under the policy at 5 April 2006 so as to increase the level of life assurance cover or extend the period during which such benefits are payable e.g. the member does not adjust the premiums to purchase increased life assurance cover.

Unsecured pension

Rather than purchasing an annuity, you can opt to take an unsecured pension provided direct from a Free-Standing AVC, Stakeholder or Personal Pension fund (if the rules of the scheme permit this) as income withdrawals (previously called Income drawdown). If the income withdrawal option is taken, you must withdraw income from the fund during the whole of the period you defer purchasing an annuity (up to the eve of your 75th birthday at the latest).



Contact details

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Our offices are open from
8.30 am to 5 pm, Monday to Friday

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