EXPLANATORY NOTE

PUBLIC SECTOR COMPENSATION SCHEME 2013

Background

Public Servants are excluded from Statutory Redundancy provisions by an Order made in 1996 under the Redundancy Payments Act 1990. Because of this exclusion the majority of public servants have separate redundancy provisions under specific schemes which compensate them for 'loss of office'

The Public Sector Pensions Authority is now seeking to introduce, via The Public Sector Compensation Scheme 2013, new compensation benefits for a number of Public Sector employment groups in respect of the compulsory or voluntary 'loss of office' (including termination of employment by way of redundancy).

The Scheme seeks to replace the various arrangements that are currently in place which, with their differing eligibility and calculation criteria, are considered to be difficult to understand and complex to administer. Furthermore, some existing provisions having remained relatively unchanged since their introduction in the late 1980's, and provide for early retirement, in some cases from as early as 50 years of age. It is considered that provisions such as this may encourage those who are eligible to become economically inactive by removing themselves from the labour market which given the current public sector landscape, as well as employment trends, is now no longer appropriate.

In addition, life expectancy has increased significantly since the 1980-90's and statistics, released by the UK's Office for National Statistics, show that in 1989 the life expectancy for a man was 72.63 years, and 78.24 years for a woman compared to 78.66 years and 82.64 years in 2011. Because life expectancy is increasing, pensions are in payment for longer eg for a person who takes early retirement at age 50, their pension could be in payment for over 30 years, which for some could be a longer period than the time they were in work.

It is therefore considered that it is no longer appropriate to structure benefits based broadly upon and supporting early retirement, and that benefits should, instead, be based upon paying a fair level of compensation for 'loss of office'. There may however be circumstances in which an employer is content to support early retirement and for members of the Isle of Man Government Unified Scheme (GUS) there are provisions for early retirement within GUS that are, specifically, covered by the Augmentation provisions. By introducing the Public Sector Compensation Scheme the PSPA is seeking to end the historic and automatic link between redundancy and early retirement.

The Public Sector Compensation Scheme has therefore been drafted with the key aims of seeking to harmonise and simplify the provisions, provide a fair level of compensation for those that experience compulsory or voluntary redundancy and to break the automatic link with early retirement.

The Scheme

The Public Sector Compensation Scheme 2013 has been drafted under the powers of the Public Sector Pensions Act 2011, and in particular Section 6 (1) (c) which requires the PSPA to make schemes for the superannuation of public sector employees. Under the Act superannuation includes not only pensions, but also compensation for those who suffer 'loss of office'.

Ideally the PSPA would like to introduce this Scheme with effect from 1 January 2014. However, these proposed new provisions can only be introduced once consultation with affected employees, their representative organisations and other key stakeholders has been completed, the results considered and any necessary changes to the draft Scheme made.

Who the Scheme Covers

The Scheme seeks to cover broadly the following Employment Groups:

a) Civil Servants as defined in the Civil Service Act 1990, as amended;

b) Officers or Employees appointed to or by the following Departments, Boards and Offices of Government:
   - Department of Community, Culture and Leisure
   - Department of Economic Development
   - Department of Education and Children
   - Department of Environment, Food and Agriculture
   - Department of Health:
   - Department of Home Affairs
   - Department of Infrastructure
   - Department of Social Care
   - Department of the Treasury
   - Communications Commission
   - Financial Supervision Commission
   - Gambling Supervision Commission
   - Insurance and Pensions Authority
   - Isle of Man Office of Fair Trading
   - Isle of Man Water and Sewerage Authority
   - Manx Electricity Authority
   - Manx National Heritage
   - Public Sector Pensions Authority
   - The Isle of Man Data Protection Supervisor
   - The Isle of Man Industrial Relations Officer
   - Staff of the Office of the Isle of Man Data Protection Supervisor
   - Staff of the Isle of Man Industrial Relations Office
   - The Clerk of Tynwald
   - Staff of the Clerk of Tynwald's Office

However, for all employees, in order to receive benefits an employee must have two years service which is in line with statutory redundancy qualification criteria.

There are, however, some groups that are not covered by these arrangements. These include:

- Members of the Isle of Man Constabulary;
- Firefighters employed by the Department of Home Affairs
- Teaching staff in schools and lecturing staff in colleges in the Isle of Man;
- General practitioners and the staff employed by GPs surgeries;
- Private dental practitioners and their staff:
- Members of the Judiciary;
- Members of Tynwald;
- Manx Radio;
- Those employed by Hospice.

Whilst this provides a summary of those covered, or not, by the Scheme, full lists can be found at Schedule I and Schedule II of the Scheme.

Definitions

The Scheme sets out in Section 4 certain definitions used within the Scheme. Some of these are technical in nature, and define some of the language used within the Scheme. As the proposed benefits are calculated upon pay and length of service, attention is drawn to the definition of "pay" at rule 4.3, "service" at rule 4.4 and "reckonable service" at rule 4.5.

Pay - In summary the pay definition provides for basic pay and permanent additions or allowances, which have been paid in the 12 months prior to the end of employment, to be included when calculating a compensation payment.

The rule goes on to define what happens in certain circumstances such as when the employee is on maternity leave, secondment or sick leave.

It should also be noted that the Scheme seeks to provide a minimum level of pay upon which benefits will be calculated, and it is proposed this is initially set at £25,000. Therefore if an employee's full-time pay is £20,000, for the purposes of compensation benefits it will be deemed that they earn £25,000. It is proposed that this figure will be adjusted each year by reference to the change in public sector average earnings for full-time employees, as identified by the Isle of Man Earnings Survey.

Service - In relation to service, it will be the length of continuous service with in the public sector, which may not necessarily be with the same employer. For example, if a person starts their career as a nurse but moves to a job in the Civil Service, for the purposes of calculating any benefits, these will be based upon service that commenced when they became a nurse. This, of course, is as long as there was no break of greater than 28 days between the two jobs, except in certain circumstances such as maternity leave or service within the reserve forces.

The definition of service determines eligibility to receive benefits under the Scheme, however, the calculation of benefits is based upon reckonable service.

Reckonable Service - In simple terms reckonable service is the amount of time an employee is at work in the Public Sector with a relevant employing authority in terms of years, months and days whilst being employed. So periods of unpaid leave, or unpaid sick leave, do not count towards the period to be used when calculating benefits, but they do not break the continuity of service. The definition of reckonable service also sets out how part-time service is calculated on a pro rata basis.

Benefits

Sections 5, 6 and & 7 of the Scheme set out to whom and what benefits are applied. In terms of the benefits provided by the Scheme, these provide for circumstances covered by voluntary and compulsory redundancy. The provisions are also dependent upon whether an employee was in post at the time of the scheme is introduced or whether they are new members of staff appointed after the scheme is introduced.

In summary, for all employees the benefits are based upon a formula of pay and length of service made up of one month's pay for each year of reckonable service. However under each scenario there are caps upon the amounts of service that can be used ranging from 12 months to 24 months. In addition, for those who are approaching contractual retirement age (age 65 for the purposes of the scheme), the amount of benefits are also capped under a tapering mechanism. This mechanism provides that the amount of benefits that can be paid out on redundancy is proportionately reduced as an employee approaches contractual retirement age, so that at age 65 the employee receives no more than 6 months' pay. The detail of the tapering mechanism is set out at rule 4.10.

In relation to the benefits that are paid, for those who opt for voluntary redundancy, their benefits will be calculated as follows:

- For current employees, the calculation will be one month's pay for each year of service up to a maximum of 24 months pay.
- For new employees, the calculation will be the same but up to a maximum of 18 months pay.

For those who experience compulsory redundancy, their benefits are calculated as follows:

- For current employees, aged 45 years or over at the time the Scheme is introduced the calculation will be based upon one month's pay for each year of service up to a maximum of 24 months pay.
- For those current employees aged under 45 years at the time the Scheme is introduced, the maximum will be up to 18 months pay, again based upon one month's pay for each year of service.
- For new employees the maximum is 12 months pay.

For any employee who departs on a voluntary or compulsory basis and is over contractual retirement age, they will receive a lump sum payment equivalent to 6 months' pay.

Those members who have applied for voluntary redundancy but had their applications declined and who are subsequently made compulsorily redundant arising from the same redundancy consultation, will be entitled to the same compensation terms offered to those made voluntarily redundant.

It should also be noted that following the calculation of redundancy benefits under the Scheme, if the benefits that would have been payable to an employee under statutory redundancy provisions, had they applied, are greater than those under this Scheme then the lump sum payment must be equal to the level of the statutory payment.

Increasing Pension

Sections 6 and 7 also include details of how any lump sum payments may be used to enhance an employee's pension provision. For those employees who depart on a voluntary or compulsory basis, who are 50 or over and under contractual retirement age, they will be offered the opportunity to exchange their lump sum to buy additional service in order to enhance their pension. Employees will be able to buy as much or as little additional service as they wish, up to the maximum available through the use of the compensation lump sum, but capped at the maximum they would have otherwise been able to accrue at the contractual retirement age of 65.

However, whilst those employees who are made redundant after having attained the age of 50, but before attaining the age of 55, will be able to buy additional service, it is important to note that the pension will not be able to be brought into payment before the age of 55. The factor at which the service is bought will be determined at the date of the termination of employment, preserved until the date it is brought into payment.

In summary, in order to buy added service the employee's pension scheme requires the payment of a lump sum calculated by multiplying a factor relating to their age next birthday by their salary at the point of departure and dividing the result by £100. This gives the cost of buying one additional year of service. The factors used for purchasing added service are set out at Schedule II of the Scheme.

During a transitional period the amount of service that can be purchased will be enhanced, and it is proposed that:

- For those made redundant in the first year following the introduction of the Scheme, the service purchased will be adjusted by a factor of 1.75.
- For those made redundant in the second year following the introduction of the Scheme the service purchased will be adjusted by a factor of 1.50.
- For those made redundant in the third year following the introduction of the Scheme the service purchased will be adjusted by a factor of 1.25.
- From the fourth year following the introduction of the Scheme, service will be purchased in accordance with the published factors.

An example of how this works in practice is attached at **Annex A**.

<u>Re-Employment</u>

Finally, Section 8 of the Scheme sets out how any employee who receives a payment under the scheme or any former arrangements, (such as the Interim Compensation Scheme) will be required to repay some or all of their compensation payment if they are re-employed by one of the employing authorities covered by this scheme, and within a time frame that the compensation payment covers.

For example, if an employee receives a compensation payment equivalent to 12 months pay, and are re-employed six months later, they will be required to re-pay an amount equal to 6 months pay. This re-payment will be based on the pay that was used to calculate the lump sum payment and not the equivalent of six months' pay in their new job.

<u>Schedules</u>

There are three Schedules to the draft Scheme. Schedule I sets out which employment groups are covered by the Scheme, Schedule II sets out which employment groups are not covered by the Scheme and Schedule III sets out a table of factors to be used for purchasing additional service under the Scheme if over age 50.

<u>Consultation</u>

The PSPA is conducting a three month period of consultation on the draft Scheme. As well as the draft Scheme and supporting written material it is anticipated there will be joint presentations to affected employees by the PSPA and the Office of Human Resources to explain the proposals and answer questions.

It should be noted that as redundancy provisions are identified in the majority of employment groups' terms and conditions of employment/service, the proposed changes will need to be discussed in each of the relevant joint negotiation fora, with a view to gaining agreement to their implementation.

At the end of the consultation period the PSPA will prepare a final Scheme, having considered both the responses received and the outcome of the negotiations with representatives of the various employment groups, before formally making the Scheme and submitting it to Tynwald for its consideration and approval.

The PSPA would therefore be grateful if any comments you may wish to make in relation to the draft scheme could be forwarded to the PSPA in writing by **midday Friday 4 October 2013**, at the latest to the following Address:

Compensation Consultation
Public Sector Pensions Authority
Goldie House
1-4 Goldie Terrace
Douglas
IM1 1EB

Alternatively any comments can be forwarded by e-mail to:

consultations@pspa.im

Ian T Murray
Chief Executive
Public Sector Pensions Authority

4 July 2013

Annex A

Example:

1. **Salary** £ 30,000

   Age 56 years

   Service 30 Years

   Pension Section Section 2 Member

   Current pension is (£30,000 x 30) x 1.2% = £10,800

   Redundancy

   - This member will receive a redundancy lump sum equivalent to 24 months pay, £60,000.
   - Their age next Birthday will be 57.

   The Member can choose to use some or all of their redundancy lump sum to buy added service under this scheme requires the payment of a lump sum calculated by multiplying the appropriate factor which relates to their age next birthday by salary and then divided by £100.

   Therefore in this example the cost of an extra year of service will be salary divided by £100 multiplied by the age 57 factor:

   (£30,000/100) x £32.26 = £9,678 per year

   Therefore in this example the individual can purchase a maximum of 6.2 years (£60,000)/£9,306) of service if they so choose.

   So pension becomes (£30,000 x 36.45) x 1.2% = 13,032 per annum.

   Pension increased by £2,232 per annum.

Transition

2. If the employee were made redundant on 1 January 2014 the cost of each added year of service remains the same i.e. £9,306, but it buys 1.75 years service.

   Service is capped at 65. So the maximum service the member can buy is 9 years.

   So to achieve 9 years service member needs to purchase 5.14 years. (9/1.75)

   Therefore they need to pay £9,678 x 5.14 = £49,745

   Pension is now (£30,000 x 39) x 1.2% = £14,040 per annum.

   Remaining lump sum = £10,255

3. The factors used to calculate the cost of every year of additional service for each applicable section of the Unified Scheme and the Manual Workers No. 1 Scheme are shown in Schedule III of the draft scheme.