Public Sector Pensions Authority

Consultation - Isle of Man Government Unified Scheme (Amendment) Scheme 2017

This fact sheet is designed to help Practitioner members in Sections 1, 2, 4 or 5 understand the proposed changes to the Isle of Man Government Unified Scheme 2011 (the Scheme) and to illustrate the impact of these changes on the future pension benefits.

In order to achieve the savings which will make the Scheme more sustainable in the future it is proposed to:

For Active Members on 31 March 2017

1. Reduce the pension benefits built up on or **after** 1 April 2017 by 6%; and
2. Increase member contributions by 2.5% being phased in from 1 April 2018

For New Members on or after 1 April 2017

3. Reduced benefit accrual by 6%
4. Membership of a New Standard Section with a contribution rate of 7.5%
5. For Fire-fighters Membership of Section 7 with a contribution rate of 13.5%

The fact sheet uses terms that you may not be familiar with and a Jargon Buster is included on page 6.

For Active Members on 31 March 2017:

1. Reduction to Pensions for Active Members in the Scheme on or before 31 March 2017

How the 6% reduction is calculated

To understand how this will impact on your future pension, you first need to understand how your practitioner pension is calculated. Your pension is based on the years and days of service you build up, the current value of your total earnings and the growth rate appropriate to your age and is calculated as follows:

(Total Revalued Earnings / Pensionable Service) x Pensionable Service x Growth Rate = Pension

In order to apply a 6% reduction to the pension that is built up on or after the 1 April 2017, the Pensionable Service calculation will need to be split into two parts and the pension calculated separately.

The 6% reduction will be applied to the pension that is built up from your pensionable service on or after 1 April 2017.

For older members, with less time until retirement age, this change will have minimal impact to their overall expected retirement benefits as they will be building up a lower pension for a shorter period of time. The higher pension they have built up before 1 April 2017 will not change.

For younger members, the impact to expected retirement benefits will be greater. This is because younger members will be building up a pension at a 6% lower rate in the future and for longer than an older member.

The new formula incorporating the 6% reduction will look like this:

> **Part 1**: (Total Revalued Earnings/ Pensionable Service) x Pensionable Service from Date of joining to 31 March 2017 x Growth Rate = Pension
>
> plus
>
> **Part 2**: (Total Revalued Earnings / Pensionable Service) x Pensionable Service from 1 April 2017 to date of leaving x Growth Rate x 94% = Pension

- Part 2 of the pension will be multiplied by the 94% to represent a 6% reduction.

Illustrative Examples of how the 6% reduction will impact on future pensions

Example 1

Using an example of a member in Scheme Section 5, who retires at age 60 with 40 year's scheme service and total revalued earnings of £3,000,000 the expected pension will currently be:

(3,000,000/40) x 40 x 1.63% = £48,900 a year

After introducing the proposed reduction of a 6% deduction to the pension (shown as x 94%) built up from service on or **after 1 April 2017** this formula will change.

As the reduction is applied to only the future pension built up after the date of change the scheme service or "pensionable service" as it is referred to in the Scheme will need to be split into two parts. Part 1 will be the service built up before the 1 April 2017 and Part 2 will be the service built up on or after the 1 April 2017. The 6% reduction will be applied to the pension built up from the service built up on or after 1 April 2017.

The following examples illustrate the impact of the 6% reduction to the pension built up on or after 1 April 2017 across a range of ages. As the 6% reduction is only applied to pension built up in the future, the biggest impact to pensions will be for younger members who have longer to work and build up a pension to retirement. Those closer to retirement who have already built up most of their pension will see the least impact to their expected pensions when compared to recent projections.

Example 2 - Assumes a member is aged 58 on 1 April 2017.

Using the same pension as Example 1 and assumed joined the Scheme aged 20 and has 40 years expected service to retirement at age 60. 38 years were built up before the 1 April 2017 and 2 years will be built up after 1 April 2017.

To illustrate how the pension is impacted, the calculation needs to be split into 2 parts and then added together to get the total pension:

Part 1 - the pension that equates to the 38 years service built up before the 1 April 2017 the pension at age 60 is:

(3,000,000/40) x 38 x 1.63% = £46,455

Part 2 – the pension that equates to the 2 years service to be built up after the 1 April 2017 to age 60 and reduced by 6% is:

(3,000,000/40) 2 x 1.63% = £2,445 x 94% = £2,298

Total Pension - £46,455 + £2,298 = <u>£48,753 a year</u>

The expected pension at age 60 in Example 1 was £48,900 and after the reduction is applied the pension reduced to £48,753.

Therefore the impact of the 6% reduction to future service built up after 1 April 2017 for a 58 year old member retiring at age 60 is £147 (i.e. 6% of £2,445) reduction in the expected pension.

Example 3 – Assume Member is Aged 40 on 1 April 2017

Using the same pension as Example 1 and 2, but assuming the member is younger at the time of change, with 20 years built up to the time of change plus an expected 20 years service to retirement age 60.

To illustrate how the pension is impacted, the calculation needs to be split into 2 parts:

Part 1 - the pension that equates to the 20 years service built up before the 1 April 2017 the pension at age 60 is:

(3,000,000/40) x 20 x 1.63% = £24,450

Part 2 – the pension that equates to the 20 years service to be built up on or after the 1 April 2017 to age 60 and reduced by 6% is:

(3,000,000/40) x 20 x 1.63% = £24,450 x 94% = £22,983

£ 24,450+ £22,983= <u>£47,433 a year</u>

The expected pension at age 60 was £48,900 a year and after the reforms are applied from 1 April 2017 the reduction reduces the expected pension to £47,433 a year.

When compared to Example 1 the impact of the 6% reduction to future service built up on or after 1 April 2017 for a 40 year old member planning to retire at age 60 is £1,467 a year (i.e. 6% of £24,450) reduction in the expected pension.

Example 4 – Assume Member is Aged 30 on 1 April 2017 – using the same pension as Example 1, but assuming the member is younger at the time of change, with only 10 years built up to the time of change plus an expected 30 years service to retirement age 60.

To illustrate how the pension is impacted, the calculation needs to be split into 2 parts:

Part 1 - the pension that equates to the 10 years service built up before the 1 April 2017 the pension at age 60 is:

(3,000,000/40) x 10 x 1.63% = £12,225

Part 2 – the pension that equates to the 30 years service to be built up on or after the 1 April 2017 to age 60 and reduced by 6% is:

(3,000,000/40) x 30 x 1.63% = £36,675 x 94% = £34,475

£ 12,225 + £34,475 = £46,700 a year

The expected pension at age 60 was £48,900 a year and after the reforms are applied from 1 April 2017 the reduction reduces the expected pension to £46,700 a year.

When compared to Example 1 the impact of the 6% reduction to future service built up after 1 April 2017 for a 30 year old member planning to retire at age 60 is £2,200 a year (i.e. 6% of £36,675) reduction in the expected pension.

2. Increase member contributions by 2.5% from 1 April 2018

For all practitioner members who are active in the Scheme on the 1 April 2017 pension contributions will increase by 2.5%. However, these new contribution rates will be phased in by a maximum of 1% each year from April 2018 over a period of **three** years, so that members do not face a change in contributions of more than 1% of pensionable pay in any year. New members to the Scheme on or after 1 April 2017 will join Standard Section and will contribute 7.50%.

Section	**Contribution Rate Transition**		
	1 April 2018	**1 April 2019**	**1 April 2020**
1 (Standard)	6%	7%	7.5%
2 (Ex members Civil Service Classic)	8.5%	9.5%	10.25%
2 (other schemes)	8.75%	9.75%	10.25%
3	10.50%	11.50%	12.25%
4	7.60%	8.60%	9.10%
5	10.50%	11.50%	12.00%
6	9.40%	10.40%	10.90%
7	12.00%	13.00%	13.50%
Protected Hospital Doctor Member	10.60%	11.60%	12.10%

Active members who received support against increased contribution rates

If you were age 53 or over when the Unified Scheme was introduced in April 2012 and you were able to join your Protected Section without paying more than your rate of contribution at that time or the Standard rate of contribution (5%), you contribution rate will increase from 1 April 2018 to reach the rate shown above for your particular section. Your contribution increase will be limited to a maximum 1% a year.

Employer Contributions

Treasury have informed the PSPA that employer contributions will remain at 15% from April 2016.

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Jargon Buster

Growth rate (or accrual rate)

This is the rate by which an employee earns pension benefits. For example, if your growth rate is 1.63% then for each year of service you earn 1.63% of your Final Pensionable Pay. So a person retiring after 40 years with a Final Pensionable Pay of £75,000 will therefore receive a pension of 40 x 1.63% x £75,000 = £48,900.

Contribution rates

This is the annual percentage you pay to be a member of the scheme (as a proportion of your Pensionable Pay). The contribution rates described in this guide are those that will apply in Scheme. However, the Scheme includes a cost-sharing mechanism and these rates could change in the future.

CARE Final Pensionable Pay

The pay used to work out your benefits. This is known as your Final Pensionable Pay. This is the total revalued earnings throughout your practitioner service divided by your Pensionable Service.

Normal Pension Age

Under the Scheme you can choose when you want to retire (generally between 55 and 75 but subject to the agreement of your employer) and your benefits will be adjusted accordingly.

Pensionable Service

The total number of years and days which count towards your scheme benefits. Your Pensionable Service may be different to the length of time you have worked and contributed to the scheme (e.g. if you have worked part time or had periods of unpaid leave). Pensionable Service includes any service transferred in from previous pension arrangements and any added years of pension you may have purchased and built up.

Total Revalued Earnings

The pay used to work out your benefits and is referred to your final "career average revalued earnings"(CARE). Where benefits are based on CARE, they will be based on the average of total pensionable earnings whilst you are/were a member of the pension scheme (as a Practitioner), and revalued to the date you leave service or retire. This is achieved by recording your pensionable Practitioner earnings for each year of membership in the Scheme and applying a revaluation factor. The revaluation factor used is 1.5% above the amount of the annual increase due under the Pensions Increase Act. The resulting figure is known as your Revalued Earnings. An example of how we calculate this is shown on page 5 of the Isle of Man Government Unified Scheme Guide –

Supplementary guide for Practitioners which can be found on the resources page of the PSPA website at www.pspa.im