The Impact of Salary Sacrifice for Shared Cost AVCs on your LGPS Benefits

Additional Voluntary Contributions (AVCs) allow you to build up extra savings for retirement. If you choose to pay AVCs, they are invested separately from your Local Government Pension Scheme (LGPS) benefits, and provide you with additional income upon your retirement.

The LGPS has a provision within its regulations to allow an employee to enter into an agreement in which the employer can decide to also contribute to their employee's AVC arrangement. This is known as a Shared Cost AVC (SCAVC). This could be done under a Salary Sacrifice arrangement.

If an employee enters into a SCAVC Salary Sacrifice arrangement with their employer, they would both stand to make savings.

For example, if an employee was earning £20,000, and agrees with their employer that they will give up £1,000 of their salary, which the employer will put directly into a AVC fund, then as long as the employee also puts in a minimum of £1, they will enter into a Shared Cost AVC. The employee will make savings on tax and National Insurance (NI) contributions, and the employer will save on NI contributions.

This employee could well have made the same tax savings themselves, by simply paying the £1,001 in directly into the AVC pot, without involving their employer or Salary Sacrifice at all, but via Salary Sacrifice they would get the bonus on saving on their National Insurance contributions too.

Would there be a reduction to my LGPS benefits as a result of a SCAVC Salary Sacrifice scheme?

The worry that you may have is that the reduced wage post Salary Sacrifice may have a detrimental impact to the value of your LGPS pension account, and the investment in an AVC provides uncertain returns, as they are based on the stock market, rather than a defined benefit scheme such as the LGPS.

However, the Shared Cost AVC Salary Sacrifice scheme does not affect your LGPS benefits, provided your employer specifies in your contract of employment that the contribution the employer makes to the SCAVC will be a pensionable emolument. Therefore there is no detrimental impact to the calculation of pension benefits as a result of joining a SCAVC Salary Sacrifice scheme.

The specification or amendment to your statement of particulars is **essential**, or you could be left with a significant reduction in your LGPS benefits, as the post sacrifice salary figure will be used in the calculation of benefits for both pension built up to 31st March 2014 (Final Salary and Membership), and from 1st April 2014 (Career Average Revalued Earnings).

Would I pay less contributions towards my LGPS pension, as a result of my pay going down?

No, because the portion of pay sacrificed and paid into a SCAVC is classed as a 'pensionable emolument', which means that any payment made in respect of the Salary Sacrifice will still be used to calculate your pension benefits with. Therefore, the contributions are based on the pre Salary Sacrifice figure, and the amount is based on the applicable pay bands for the relevant scheme year.

LGPS Employee Contribution Rates

Both you and your employer pay contributions to pay for your LGPS pension. How much you pay depends on how much you earn. You will pay between 5.5% and 12.5% of your pensionable pay.

Every April your employer will decide your contribution rate. If you have more than one job, your employer will set your contribution rate separately for each job.

You can find the latest LGPS Employee Contribution Rates here:

https://www.lgpsmember.org/2024/02/21/new-contribution-bands-2024/

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What if I'm already paying into an AVC fund?

If you already have an active AVC arrangement in place, and wish to enter into a SCAVC with your employer, this would have to be a new arrangement for the purposes of the LGPS Regulations. You would need to cease paying into your current AVC arrangement, and could then elect to either:

a) Leave your previous AVC fund as a separate pot (this may be something you wish to do if you want your original AVC to remain governed under the terms and conditions that you agreed to when beginning that AVC), or

b) Transfer your previous AVC fund into your new SCAVC fund, in which case the whole of the pot would be governed by the regulations in force at the time the SCAVC was entered into

Annual & Lifetime Allowance

Please note that any increase to your pension account could have an impact on your annual and/or lifetime allowance. If you are worried that you may exceed either of your allowances, we recommend you seek advice from an independent financial advisor.

How do I set up a Shared Cost AVC Plan?

Speak to your employer's HR/Payroll Dept to see if they offer a Shared Cost AVC scheme. They will be able to advise you further and refer you to their chosen provider.

Please contact us: Dorset County Pension Fund, County Hall, Dorchester, Dorset. DT1 1XJ

Telephone: 01305 224845

Website: www.dorsetpensionfund.org

Email: pensionshelpline@dorsetcouncil.gov.uk

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Example of Shared Cost AVC

The Current AVC Scheme

Under the current AVC arrangements Richard would decide to put £1,000 into an AVC fund by regular monthly deductions from his pay and he would get tax relief on his AVC payments, but his National Insurance (NI) contributions would be calculated based on his gross earnings of £20,000.

So for tax deduction purposes his salary would be £19,000, but for NI contributions, his salary would still be £20,000.

The New Shared Cost Salary Sacrifice AVC Scheme

If Richard joined a Salary Sacrifice SCAVC scheme, and agreed to his salary being reduced to £19,000, with his employer paying £1,000 into the AVC fund on his behalf, he would get the same tax relief but also pay less NI contributions.

So for tax deduction purposes his salary would be £19,000, and for NI contributions, his salary would also be £19,000. Richard's employer would also make a saving on their own NI contributions, as they would be based on his reduced pay.

As the AVC fund is required to be set up in a 'shared cost' format, this means that both Richard and his employer must pay in. Richard's employer has agreed to put in the £1,000 sacrificed from his salary, so this is effectively the employer's contribution, and a further contribution is required from Richard. As long as Richard pays in at least £1 a month into the AVC fund via a payroll deduction, the requirements of a Salary Sacrifice SCAVC scheme have been met.

Please see below an examples of the affect on take home pay:

The Current AVC scheme – based on pay of £20,000		**The Salary Sacrifice SCAVC scheme – based on post Salary Sacrifice pay of £19,000**	
Monthly Pay	£1666.67	Monthly Pay	£1583.33
LGPS Contributions	£96.67	LGPS contributions	£96.67
AVC Contribution	£83.33	AVC Contribution	£1.00
Monthly pay after contributions	£1486.67	Monthly pay after contributions	£1485.66
Tax Paid	£114.00	Tax Paid	£114.00
NI contributions Paid	£108.00	NI contributions paid	£98.00
Total Take Home Pay	£1264.67	Total Take Home Pay	£1273.66

As you can see from the comparison above, Richard's take home pay has risen from £1,264.67, to £1,273.66 per month, an increase of £8.99 per month, or £107.88 per annum. He has £84.33 (£1,000 ÷ 12 + £1) paid into his AVC fund for that month and his LGPS contribution is the same.
In this circumstance, Richard's employer would also stand to save £138 per annum in National Insurance contributions, which makes it an attractive arrangement for both parties.