Local Government Association

Pensions guide for councils moving to a new model of service delivery

Guide

Background

1. Local government is facing unprecedented financial challenges and is therefore seeking innovative ways to deliver services within new funding constraints. Councils[1] are increasingly exploring potential outsourcing of services to the private and third sectors plus implementation of service delivery via joint vehicles, mutuals or wholly owned companies. All of these models will have pensions implications which must be considered at the beginning of the process or there will be unforeseen and potentially material impacts on the financial viability of the options being explored.

The Local Government Pension Scheme (LGPS)

2. Under the Local Government Pension Scheme Regulations 2013 (as amended) local councils are scheme employers within Part 1 of Schedule 2[2]. This means that by law they are obliged to offer access to the LGPS to all existing and new employees who are eligible for the scheme. Employees may choose to opt out of the scheme (they can also choose to opt back into the scheme). In addition scheme members can, since 1 April 2014, elect to pay half their normal pension contributions and in return build up half their normal pension by choosing the 50/50 section of the scheme.
3. Councils pay an employer's contribution rate in respect of the LGPS made up of a Future Service Rate (FSR) designed to cover the cost of future accrual of benefits in the scheme and a Deficit Contribution Rate (DCR) in order to make up the shortfall against past service benefits.
4. These rates are determined using experience and assumptions at the local level, through the triennial valuation process, leading to a wide variety of employer rates both across and within the 90 LGPS Pension Fund Administering Authorities in England and Wales. Therefore each employer (both councils and other types of employers) will have its employer contribution rate determined separately.

Other Public Service Pension Schemes (PSPS)

5. For a variety of historical and policy reasons councils also have employees with access to other PSPSs, for example the Teachers' Pension Scheme and the NHS Pension Scheme. Employees who are eligible for these schemes are granted access either due to their profession (teachers) or as a result of, for example, a statutory Transfer Scheme (eg public health staff). Unlike the LGPS these schemes have employer contribution rates set centrally and have no funds behind them with all expenditure being met from contributions and taxation.

1 The guide is directed at local councils; if this is being read by another type of body (for example higher or further education body, relevant information should be sought from your Pension Fund Administering Authority.)
2 http://www.lgpsregs.org/index.php/schedule-2

Issues for models of service delivery

6. Creating a new model of service delivery and moving staff who currently have access to the LGPS or another PSPS will have both financial and industrial relations issues which need to be considered early in the process. These issues stem from Fair Deal (or its equivalent in LGPS) and regulations covering the funding and recovery of LGPS deficits.

Fair Deal

7. HM Treasury published revised Fair Deal guidance[3] in October 2013. This provides for the continued access to PSPS for employees subject to an involuntary change of employer whether or not TUPE applies. This access to the PSPS continues on subsequent movements of employer (eg re tenders of the service).

8. For employees with access to the LGPS 'Fair Deal' type arrangements have been in place for some time. The Best Value Authorities Staff Transfers (Pensions) Direction 2007[4] places on councils and police authorities in Wales (best value authorities) a requirement to either provide continued access to the pension scheme the employee is provided with through their employment with the council (which, in the case of the LGPS would be via an admission agreement) or to insist that the new employer provides a 'broadly comparable' pension scheme.

9. LGPS regulations will be amended (anticipate in late 2015) to incorporate the Fair Deal equivalent principles which will enable all local council transferring staff to remain within the LGPS rather than being offered access to a broadly comparable pension scheme.

10. For outsourcing arrangements these regulations will provide for the new employer having an admission agreement and a funding objective that means that pension liabilities accrued prior to the start of the contract will not, normally, be charged to the new employer. This is to enable a level playing field between those bidding for contracts.

11. Fair Deal and its LGPS equivalent are designed to smooth the transition to new models of delivery by reducing the impact on existing benefits and therefore avoiding industrial relations issues.

Employer contributions

12. DCR payments in the LGPS are based on outstanding liabilities and assets but also take into account the 'active life' of the employer. FSR amounts take into account the current and anticipated profile of the membership. Any move to a new model of service delivery which impacts on either the active life or profile of the council will have a resulting impact on either DCR or FSR amounts.

3 http://www.lgpsregs.org/images/OtherGuidance/FairDealOct2013

4 http://webarchive.nationalarchives.gov.uk/20120919132719/www.communities.gov.uk/documents/localgovernment/pdf/pensions-direction-2007.pdf

13. For example an outsourcing in which the transferring staff are younger than the average may impact on the council's membership profile which in turn may increase the FSR at a future valuation.
14. Alternatively if a significant majority of staff are moved to a wholly owned company and no new entrants of that company are given access to the LGPS its 'active life' as a scheme employer could be significantly shortened. This may lead to an increase in DCR amounts for that new organisation due to a shortening of the recovery period.
15. In extreme cases a wholesale transferring of staff from the council (apart from any statutory positions) could potentially result in an exit payment (ie a demand for any deficit to be paid in full immediately) due to the impact on the 'active status' of the council as a scheme employer. These amounts can be in the millions and could completely negate the business case for the move to the new model of service delivery.
16. Councils should contact their LGPS administering authority to ensure they are fully aware of the potential impact on employer contributions or the possibility of an exit payment.

New employer types

17. The type of new employer and the process used to determine the identity of that employer will have a bearing on the pension arrangements available or required.
18. If a procurement process is used then either the Fair Deal or Best Value Authorities Staff Transfers (Pensions) Direction 2007 will apply and access will be granted for transferring staff but not necessarily for new staff employed on the contract following transfer. If new staff are to be offered access to the LGPS then an open admission agreement will need to be entered into with the new employer rather than the closed agreement.
19. If the staff are transferred using the TECKEL exemption to procurement (eg to a company controlled by the council) then the new employer will be a Part 2 of Schedule 2 of the LGPS Regulations 2013 scheme employer which means it is up to the new employer to determine access to the LGPS for both existing and new employees (eg whether or not TUPE applies as, if it does, transferring employees will have the right of access to the LGPS or to a broadly comparable scheme under the Best Value Authorities Staff Transfers (Pensions) Direction 2007). However, future changes to include Fair Deal provisions into LGPS regulations may, in all cases, require access to the LGPS for at least the staff transferring to such bodies.
20. Transfers to other models such as a mutual will depend on the exact legal definition of the new employer. If the new employer is connected with the council (with "connected with" meaning that according to proper practices in force at that time, financial information about the new employer must be included in the local authority's statement of accounts for the financial year in which that time falls) then paragraph 19 above may apply. If not then the council should take legal advice as to whether a procurement process should be undertaken in which case paragraph 18 will apply.
21. Councils should contact their LGPS administering authority to ensure they are fully aware of the potential impact on employer contributions or the possibility of an exit payment.

Questions to ask when considering service delivery options

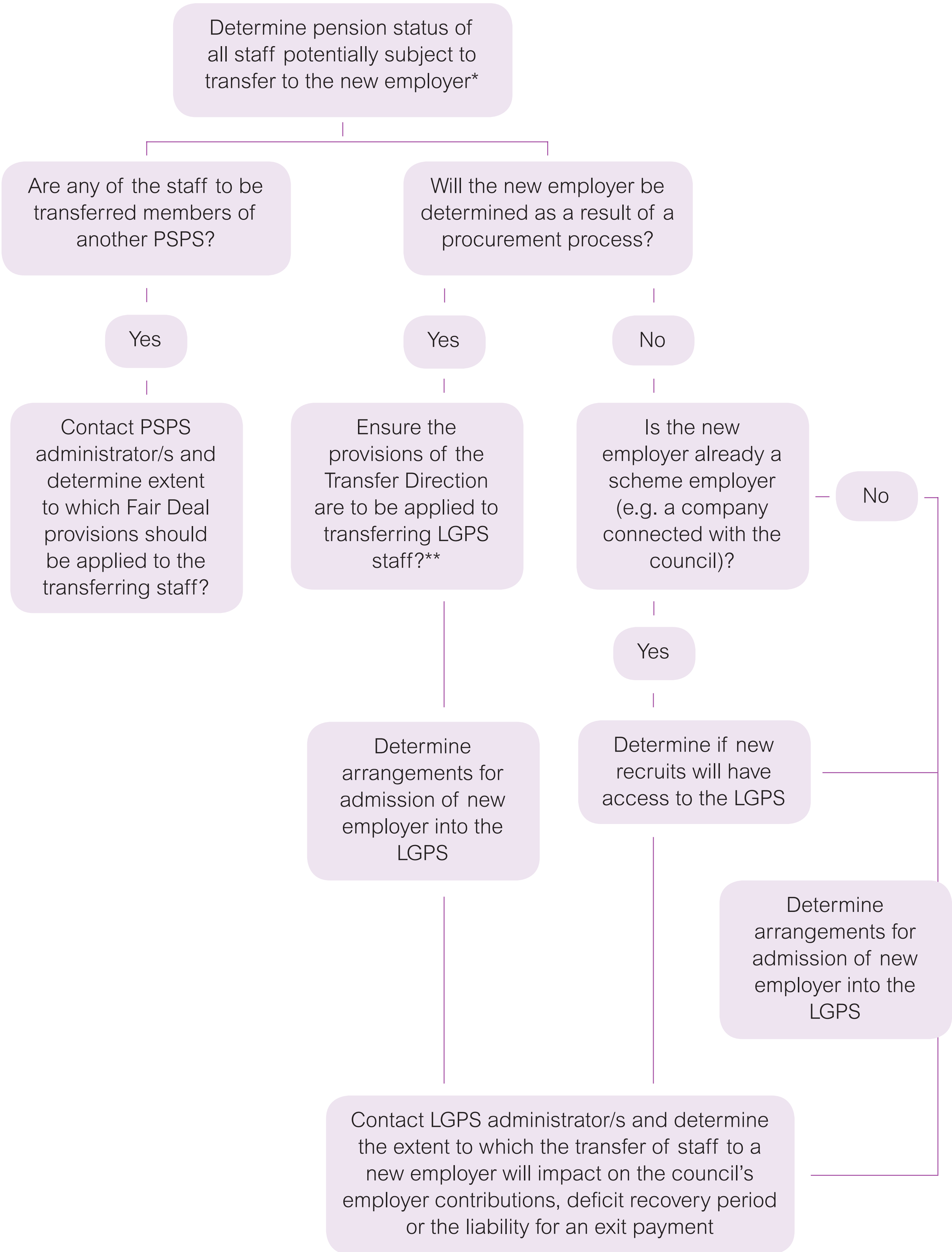
22. In order to properly prepare the financial and industrial relations impact of any move to a new model of service delivery councils should ensure they know the answers to the following questions:

    - Of the staff affected by the transfer which are members or have access to the LGPS?
    - Of the staff affected by the transfer which are members or have access to another PSPS and on what terms?
    - For PSPS staff how will Fair Deal guidance apply to their pension? For example, will the new employer have to seek admission to the TPS or NHSPS?
    - For LGPS staff does the Best Value Authorities Staff Transfers (Pensions) Direction 2007 apply and, if so, will the new employer have to seek admission to the LGPS.
    - What will be the position of new employees to the new employer with regard to access to the LGPS or another other PSPS (where eligible)?
    - For the LGPS what will be the impact of the transfer on the projected membership profile and/or active life of the council and what impact could this have on FSR or DCR amounts?
    - For the LGPS is there a possibility of an exit payment being required and if so when and how much?

Summary

23. Before considering new models of service delivery councils should ensure they know the pensions position of transferring staff and the likely financial impact of each option. Failure to do so could result in significant delays, unexpected costs and industrial relations issues.
24. Councils should contact their LGPS Pension Fund Administering Authority to ensure they are fully aware of the potential impact on employer contributions or the possibility of an exit payment.

Pensions implications – a flowchart



* Complete this process prior to the submission of the business case.

** Following the introduction of Fair Deal type provisions in the LGPS regulations all changes of employer not just outsourcing arrangements will need to be checked for the protections to be offered to transferring staff.

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