Cambridgeshire Pension Fund

Northamptonshire Pension Fund

LGSS Pensions
One Angel Square
4 Angel Street
Northampton
NN1 1ED

LGF Reform and Pensions Team
Ministry of Housing, Communities and Local Government
2nd Floor, Fry Building
2 Marsham Street
London
SW1P 4DF

Dear Sirs,

Local Government Pension Scheme (LGPS): Fair Deal – Strengthening pension protection policy consultation

I am writing to you on behalf of the Cambridgeshire and Northamptonshire Pension Funds to provide our response to the matters covered in the consultation. We have answered each question in turn.

General comments
The Cambridgeshire and Northamptonshire Funds (the Funds) are supportive of the general principles of Fair Deal and its application to the LGPS to provide continued access to the Scheme for individuals who are compulsorily transferred out of public sector employment. We feel strongly that it is important to provide continued eligibility, in these circumstances, for all those who are already eligible for membership of the LGPS prior to such a transfer.

Question 1: Do you agree with this definition (points 7-18 "protected transferee")
Regulation 3B(7) provides that:

"An employee of a service provider who is working wholly or mainly on the delivery of the service or function transferred from a Fair Deal employer other than by a compulsory transfer under sub-paragraph (1) may be treated as a protected transferee with the written agreement of the Fair Deal employer and the service provider."

This could result in current members of the LGPS who accepted employment with a service provider with the expectation of eligibility for membership of the LGPS, after the service or function had been transferred, losing their eligibility.

The consultation does provide that such individuals ***can*** be treated as "protected transferees" if both the awarding authority and new contractor agree to do so. This provision is no different to the current provision under the Best Value Staff Transfers (Pensions) Direction 2007 but the Funds feel that this is a missed opportunity to provide pension protection to all eligible individuals, with an expectation of access to the LGPS, regardless of where there employment started, thus avoiding the creation of a two tier workforce.

LGSS

The Funds also note that the written agreement by both parties to provide protection to such individuals can be terminated unilaterally. This provides the opportunity for "gaming" by service providers when bidding for public contracts. A prospective provider could, in theory, agree to offer to protect such members in order to win a contract and then terminate the protection shortly after to reduce the costs of service provision. If agreement is required from both the awarding authority and service provider to provide protection, agreement of both parties should be required to terminate such protection.

Sub paragraph 3B(8) could be amended to say that the agreement *"may be terminated with the agreement of both the Fair Deal employer and the service provider, at any time."*

We also note that these provisions appear to be contradicted by sub paragraph 3B(11). The regulation should either be removed or amended so that it is *"subject to regulation 3B(7)"*

Sub paragraph 3B(5) provides that a person remains a protected transferee for as long as they are "wholly or mainly" employed in relation to the provision of the transferred service or function. The Funds are of the opinion that it would be useful for the term "wholly or mainly" be defined or clarified to ensure a consistent approach across all employers and administering authorities. The word "mainly" could be subject to differing interpretations.

The regulations are also silent on what happens if the person returns to being "wholly or mainly" employed in connection with the provision of the transferred service or function. The Funds are of the view that the regulations should be amended to clarify whether protected transferee status would be reinstated or if it is removed permanently.

Question 2: Do you agree with this definition of a Fair Deal employer (Points 19-23)

The Funds broadly agree with this definition of a Fair Deal employer and the principle that these provisions should cover all public sector bodies and not extend to non-public sector bodies.

However, the Funds do note that this will increase the likelihood of these types of employers ceasing participation within the Fund, crystallising potentially large funding deficits. This is of particular concern in relation to further and higher education institutions, which typically have large legacy liabilities, given the financial instability of that sector and the lack of protection for Pension Funds in cases of the insolvency of such an institution.

The Funds also note that employers listed under Schedule 2, Part 4 of the 2014 LGPS regulations are not included in this definition. The consequence of this is that employees of Foundation, Voluntary aided and Federated schools, for whom the Local Education Authority is the deemed employer for pension purposes but for whom the school is the legal employer, are not classed as "protected transferees". The definition of a Fair Deal employer should be extended to include employers listed under Schedule 2, Part 4 of the LGPS regulations.

Question 3: Do you agree with these transitional measures? (points 24-25)
The Funds broadly agree with the principles of the transitional measures. It is important that all former public sector employees are provided with the same protection. The proposed measures, however, may result in unintended consequences:

- Individuals that were transferred to a broadly comparable scheme, prior to 1 April 2014, will have been transferred to a Scheme that is broadly comparable to the LGPS as a final salary scheme rather than a career average scheme. This could mean that under the proposed regulations, some individuals could be forced to leave a scheme that may be better for them than the current version of the LGPS and losing a link to final salary benefits.

- Where an incumbent service provider is awarded a contract following a retender of services there is a risk that the proposed provisions would create a cessation event, within the broadly comparable scheme, if the provider no longer has any active members in that broadly comparable scheme. This could impact the employer covenant of that provider and increase the risk to LGPS Funds, if the provider is required to pay a materially significant exit payment.

- If the contract for services has been in place for some time, it may be difficult to enforce this provision. Under the current data protection act, employers are only required to hold personnel data for 6 years and are likely to have destroyed data, relating to individuals subject to a compulsory transfer, at the expiry of that retention period. If this is the case, it would be difficult to establish who should be enrolled back into the LGPS following a subsequent transfer. The ability to enforce this provision would rely on the service provider holding information that can identify those employees that were part of the original compulsory transfer.

Where an incumbent service provider is successful in a retender process and currently provides a broadly comparable scheme, it is the Funds view that this should be allowed to continue but care should be taken to ensure that this does not provide an unfair advantage during any tender process.

The Funds do agree that individuals transferring back to the LGPS, from a broadly comparable scheme, should have the right to transfer these benefits into the LGPS but that this should be subject to is the same limits imposed on new members of the LGPS.

Question 4: Do you agree with our proposals regarding the calculation of inward transfer values (point 26)
The Funds broadly agree with the proposals. In line with our concerns under question 3, if the member was compulsorily transferred out of public sector employment and transferred to a broadly comparable scheme prior to 1 April 2014, the transfer of benefits into the LGPS should purchase final salary benefits, on the condition that the member has deferred final salary benefits remaining in the LGPS, as a result of the original compulsory transfer and that the benefits should be aggregated on re-joining the LGPS. This would ensure that members were not forced into a worse position than they currently enjoy, through no fault of their own.

Question 5: Do you agree with our proposals on deemed employer status? (points 29-39)

The Funds agree with the principle of allowing "deemed employer" status as an alternative to admission agreements but believe this should be an agreed additional option, not a default position out of the administering authorities' control. The deemed employer approach should be permissible only with the agreement of both the Fair Deal employer and the administering authority. This is based on our view that deemed employer status, if introduced as a default position could create both funding and administrative issues for administering authorities.

Funding - The Funds believe that it is important to allow administering authorities to formally and directly recognise risk sharing arrangements between awarding authorities and service providers. So called "pass-through" agreements can have a number of benefits, in the correct circumstances. If the deemed employer approach was the default position, however, the Funds would be concerned where a current admission body retains a contract following a retender process and is allowed to automatically convert to the deemed employer approach with a material deficit automatically being subsumed by the "deemed employer". It is the Funds view that material deficits should not be subsumed by the "deemed employer" in all circumstances and that the regulations should be drafted to allow administering authorities the discretion to require the repayment of any deficit, as a condition of the conversion to the deemed employer approach. Not allowing administering authorities discretion over this matter could lead to negative impacts on a Fund's cash flow.

Further, where the deemed employer route is used, the proposed regulations continue to require the service provider to meet the costs of any decisions taken by them, that result in a strain cost arising. The proposed regulations, however, do not provide the option for an awarding authority to require a bond be put in place by the service provider to cover these potential strain costs, in cases of insolvency. This could create additional funding risks, if these strain costs cannot be recovered from the service provider.

Administration - The Funds note that one of the intended benefits of the proposed deemed employer status is to limit or reduce the number and variety of scheme employers in the LGPS. It is the view of the Funds that the deemed employer approach would not tackle the underlying issues and potentially increase the complexity of administering the scheme. Under such arrangements, administering authorities would, in reality, need to manage both the service provider and deemed employer, in relation to data and contribution collection as well as communication, training and engagement.

The proposals would increase the difficulty in addressing poor employer performance, not make it easier. Administering authorities would be completely reliant on the strength of service contracts between the deemed employer and the service provider to manage poor performance by the service provider. It is our experience that commercial contracts are usually inadequate in dealing with pension matters completely.

Question 6: What should advice from the scheme advisory board contain to ensure that deemed employer status works effectively? (points 38-39)
The Funds have doubts over how effective any scheme advisory board advice would be in resolving the key issues that could arise from the deemed employer approach. In order to have any opportunity to have a real impact, any guidance from the scheme advisory board should be statutory guidance and should therefore be issued by the Secretary of State, not the scheme advisory board.

Where such guidance is issued, this should focus on the relationship between administering authorities, Fair Deal employers and service providers within the deemed employer approach, allowing administering authorities to enforce employer responsibilities directly with service providers, effectively delegating employer responsibilities to the service provider. Such guidance should also include a requirement for pension matters, relating to administration, discretions and risk sharing, to be addressed within the commercial contract with appropriate default positions, where deemed necessary, if matters are not covered by the contract. Such matters to be considered should include but not be limited to the following:

- Basis for setting the pension contributions expected from the service provider including a default position, if the matter is not covered by the commercial contract.
- Process for exercising employer discretions
- Arrangements for financial reporting
- Obligations at the end of the contract
- Roles and responsibilities for practical day to day activities such as:
    - Payment of pension contributions
    - Provision of monthly/annual pension data
    - Provision of new starter and leaver information
    - Arrangements for dealing with ill health retirements

Question 7: Should the LGPS Regulations 2013 specify other costs and responsibilities for the service provider where deemed employer status is used? (points 40-41)
In addition to costs arising from any decision made by the service provider, the Funds are of the view that service providers should also be required to pay any additional costs incurred by administering authorities as a result of poor performance in providing data to the administering authority, where de facto responsibility to do so belongs to the service provider.

The Funds would also reiterate the point that, if responsibility for pension strain costs, arising from an employer decision, are to be the responsibility of the service provider, it would also be wise to allow the Fair Deal employer to specify that the service provider take out a bond to cover these payments, in cases of insolvency. Failure to do so would create additional funding risks.

Question 8: Is this the right approach? (retaining the admitted body option) (points 42-43)

For the reasons discussed above, the Funds are of the view that the admitted body option should continue to be the default option with the deemed employer approach being an additional option available to administering authorities. It is the Funds view that risk sharing options should be explicitly allowed for and reflected in admission agreements, in the future.

Question 9: What further steps can be taken to encourage pensions issues to be given full and timely consideration by Fair Deal employers when services or function are outsourced? (points 44-46)
The Funds are not convinced that any legislation or guidance produced solely in the pension environment are guaranteed to have a positive impact on this issue. It is our experience that problems occur during outsourcing initiatives because awarding authorities and particularly contracting managers are either ignorant of or do not give due consideration of pensions legislation. Any further steps to encourage pension issues to be given full and timely consideration will need to be made outside of the pension environment and affect procurement and finance activities more directly. An example of such a measure would be to require the section 151 officer of the Fair Deal employer to certify that consideration of pension implications have been taken before any procurement exercise can be finalised.

Question 10: Are you aware of any other equalities impacts or any particular groups with protected characteristics who would be disadvantaged by our Fair Deal proposals?
No

Question 11: Is this the right approach? (Transferring pension assets and liabilities – points 48-53)
The Funds would be concerned about any prescriptive provisions, in relation to mergers or takeovers that impose one solution for all cases. The Funds would be concerned about cases where assets and liabilities are automatically transferred from a secure and stable employer to a less stable and secure employer. The Funds would also have concerns over a new employer being automatically entitled to participation within a Fund, without being subject to the admissions policy of that Fund, e.g. if the employer is usually of a type for which a bond or guarantee would be required, these provisions should apply to the new employer before allowing them to participate in a Fund.

The Funds would be comfortable with a position where the proposed arrangements are treated as the default option as long as administering authorities are able to prevent the automatic transfer of assets and liabilities, if this is, not unreasonably, deemed inappropriate given the individual circumstances of the case and that the administering authority can insist on triggering a cessation event. This would allow administering authorities to protect the Fund against any materially negative impacts resulting from a merger or takeover. We also believe that the regulations should be drafted as to require any new employer, entering a Fund as a result of such a merger or takeover, should be required to meet the same requirements as any similar new employer entering the Fund other than as a result of a merger or takeover.

Where such an event involves more than one Fund, the direction of movement should not be prescribed by law but should be decided on the circumstances of the case and allow the Funds to not unreasonably protect their own interests and those of its participating employers.

Question 12: Do the draft regulations achieve our aims?
Yes but please see our comments to the previous question. The Funds are of the view that the regulations should be drafted with those concerns in mind.

Question13: What should guidance issue by the Secretary of State regarding the terms of asset and liability transfers?
The Funds are of the view that any guidance should only be focussed on the key process of agreeing the transfer of assets and liabilities with enough scope for the Fund Actuaries to agree an appropriate methodology and assumptions to be used for calculating the transfer amounts.

In addition the guidance should allow the receiving administering authority to assess the covenant of the incoming employer and request additional security, if appropriate, and revise contribution rates accordingly and allow the Fund to require the payment of a lump sum payment, if the funding position of the employer in the receiving Fund will be materially reduced.

Yours faithfully

Mark Whitby
Head of Pensions
LGSS
On behalf of the Cambridgeshire Pension Fund and Northamptonshire Pension Fund