SouthYorkshirePensionsAuthority

Briefing: Consultation on Changes to the Local Valuation Cycle and the Management of Employer Risk

Background

On 8 May 2019, the Government issued a 12 week consultation in which it is seeking views on the following areas:-

- A proposal to move to a four yearly valuation cycle from three years with more discretion for funds to carry out interim valuations if appropriate. This includes additional flexibility for funds to alter contribution rates mid valuation.
- Increased flexibilities with exit payments – including restricting these where risk sharing has been in place.
- Allowing certain educational bodies (Further Education Corporations, Sixth Form College Corporations and Higher Education Corporations) to decide whether to admit employees into the scheme in future.

In total, the consultation raises 19 different questions but the key issues for consideration have been highlighted below. The full consultation is available here:-

https://www.gov.uk/government/consultations/local-government-pension-scheme-changes-to-the-local-valuation-cycle-and-management-of-employer-risk

Move to Four Year Valuation Cycle

This is intended to bring individual fund valuations to in line with the full scheme valuation that the Government previously moved to a four year cycle. The Government suggests two options to transition to a four year cycle:-

1) The 2019 valuation would provide rates and adjustment certificates for the next **five** years rather than three;
2) The 2019 valuation would provide rates and adjustment certificates for the next three years as normal. The following valuation (2022) would then be a two year valuation.

In each case the new cycle would commence every four years from 2024. The Government's proposal is to adopt Option (2) to provide greater certainty.

To ensure that lengthening the valuation cycle does not materially increase the risks that pension funds and their employers face, the Government are proposing the following mitigation measures that will allow LGPS funds to act between valuations:-

A) Introduce the flexibility for funds to undertake interim valuations when circumstances change between valuations and undertake full or partial valuations where required.
B) Widen the ability for funds to amend an employers' contribution rate in between valuations – for example following the outcome of a covenant check or where liabilities are estimated to have reduced

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It is proposed to introduce certain protections so that decisions on whether to undertake an interim valuation should only be made by the administering authority having due regard to the views of their actuary and following consultation with the Local Pension Board.

Recommendation: Members are asked to support the move to a four year cycle via Option 2 above and to approve the increased flexibility for interim valuations and contributions assessments. Members may wish to comment on the proposed controls.

Flexibility on Exit payments

The current arrangements for employers exiting the scheme (i.e. when the last active member leaves) can potentially cause difficulties for employers in that they are required to pay any outstanding liabilities up-front and with those liabilities calculated on a full buy-out basis. Funds have reported that, for some employers who have no capital to pay the employer debt, they can find themselves effectively tied to the scheme to avoid triggering the exit payment.

The proposal is to grant funds more flexibility to manage an employer's liabilities in this situation by spreading exit payments over a period. It is only intended that this provision be adopted where it is in the best interest of the fund (and other employers). This proposal has been requested by a number of funds and SYPA has encountered situations where this flexibility would have been beneficial to all parties.

Recommendation: Members are asked to support the increased flexibility to manage employers exiting the fund, provided the necessary risk assessment has been undertaken. Members may wish to comment on whether or not a time limit for recovery should be considered.

Exit Credits

In May 2018, the Government introduced a provision to allow payment of an exit credit where an employer was in surplus when exiting the scheme (for example, at the end of an outsourced service contract).

One of the unintended consequences of this change relates to situations where employers who have outsourced a service have agreed an element of risk sharing (e.g. through a 'pass-through' arrangement) in relation to pensions liabilities with the service provider. As the legislation is currently worded, the exit credit may only be payable to the service provider, even though the contracting employer has borne the risk.

The Government intends to retrospectively amend the position so that service providers cannot receive the benefit of exit credits where they have not borne the pension costs and risks.

Recommendation: Members are asked to support this amendment to the legislation to provide that a service provider will not receive an exit credit if they have not borne the pensions risk.

LGPS membership for the Further and Higher Education sector

Currently, further education corporations, sixth form colleges and higher education corporations are required to offer membership of the LGPS to their non-teaching staff.

The Technical and Further Education Act 2017 provided for the introduction of a new statutory insolvency regime which means that it is now possible for further education and sixth form colleges to become legally insolvent.

Although the Government expects cases of insolvency to be rare, there is a risk within the LGPS of other employers in the fund having to meet the liabilities of a failed organisation in the event of insolvency.

Given the nature of the LGPS and the changes in the further education and higher education sector, the Government is proposing to remove the requirement for these bodies to offer new employees' access to the LGPS.

Existing members would be protected for so long as they remain in continuous employment and the further and higher education bodies would be able to choose to offer membership of the LGPS to new employees if they wished.

No specific recommendation is proposed as this may be considered a matter for the further and higher education sector but member's views are welcome.

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Head of Pensions Administration June 2019