Consultation on Public Sector Exit Payment Recovery Regulations,
Workforce, Pay and Pensions Team
HM Treasury
1 Horse Guards Road
London SW1A 2HQ

Ask for: Alan South
Telephone: 01225 395283
Email: alan_south@bathnes.gov.uk
Our ref.: Pens/AGS
Date: 25 January 2016

Dear Sir

Consultation: Exit Payments

With reference to the current consultation regarding exit payments and the introduction of a clawback provision on re-employment, this is the response from Bath and North East Somerset Council as the administering authority for Avon Pension Fund which represents 36,370 actives, 40,050 deferred beneficiaries and 28,000 pensioners [incl. dependants].

This is the second consultation regarding exit payments to have been issued in the last few months, the other being the introduction of the cap of £95k. The response in this paper is in respect exit cap provisions from both consultations as they are connected.

It is of major concern to the Fund that there is an apparent rush to introduce these provisions. The exit cap consultation was conducted over a reduced period during the holiday season last August and the government's reply to the responses was issued within about three weeks which is such an exceptionally short time .If the current consultation has the same effect it could certainly give the impression that the outcomes have already been decided, regardless of any input from stakeholders.

The key areas to consider actions are as follows:

1. Complexity of Administration
2. Creation of Inequality

Administration

The exit cap proposals now in draft regulations are a clear indication of the continued financial pressures under which the public sector is being placed.

The introduction of career average into the new scheme in 2014 brought many administrative changes especially from a scheme employer viewpoint and the proposed changes will add even more complexities to an already complex scheme. Many of these requirements are to be implemented with relatively short timescales, need to be communicated to scheme members and will undoubtedly add to continuing member confusion.

The following table outlines some areas of increased complexity that have been introduced or are being proposed

1	End of year	Additional information required as two types of benefits Final Salary / Career Average
2	information	
a	Annual Benefit Statements	Tighter timescales for supplying information deadline recently changed and must be now be provided each year by end of August [previously September]
b	Government Actuary Department	Requiring information for Model Funds earlier
3	HMRC	
a	Lifetime Allowance	Ever reducing level bringing more members within the scope
b	Annual Allowance	further complex changes imminent in an already complicated area
4	Exit Payments	
a	£95k Cap	Operational complications for employers to understand members may not come forward voluntarily as previously Complex issue for members and employers to understand
b	Clawback	Two employers in each case need to be aware of issues and their responsibilities
5	Scrutiny	
a	The Pensions Regulator	Ensuring that administration conforms with the Code of Practice in meeting legislative requirements Compliance proven but producing evidence
b	Local Pension Board	Overviewing governance of Funds

In all these cases it is for the administrators of the Pension Arrangements to oversee matters and educate employers and members with more and more complicated information. There is a serious and growing challenge for administrators in explaining the complexities of the scheme in plain English. This is at a time when scheme members are being told by independent financial advisers that they themselves do not fully understand the public sector schemes particularly with all the different changes in recent years?

There has been a clear aspiration from successive governments that people should now be able to plan for their future retirement and its funding. These changes will make this more difficult for individuals.

Employers will need to be satisfied that they fully understand the impact the proposed legislation will have on a scheme member’s benefits and decisions that may be made in connection with any redundancy exercise.

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Creation of Inequality

Employer inequalities

Public sector bodies were set up to provide services and are not intended for profit or gain but their staff are having an increasing number of restrictions applied to their pay and benefits, whilst other publically owned employers [e.g. banks and media companies] are excluded and yet these seem to be the organisations that generate the very payments that government is trying to curtail.

There now appears to be a three tier system proposed for LGPS employers;

Public sector included

Public Sector exempted

Private Sector [including contractors within public sector pension schemes]

With contracts moving from public to private sector and vice versa there could also be an additional sub- category as employers involved in these transfers will be uncertain of their position in redundancy situations.

It is also difficult to understand why Housing Associations that were originally set up from the housing departments of local authorities are to be reclassified as private sector.

One key area that could be challenged is which employers are considered to be "public sector". There appears to be a deliberate intention to operate a two tier system within the public sector where some employers from a public sector scheme are included in the proposed legislation whereas other are excluded. For instance Universities are exempt but University training colleges are included. The Local Government Pension Scheme will have some of the employers within their Fund subject to the conditions and others who are not.

An inequitable scenario also occurs where a local authority puts a service up for tender. If it is retained in-house then any scheme member subsequently made redundant will be subject to the exit payment restrictions, whereas if the contract is outsourced to a private contractor there could possibly be no restrictions imposed on any exit payments made even though the payments could be the same. On contracts brought back in-house do employees retain protection if the original transfer out was before the new conditions?

Clearly there is the likelihood that two employees in the same service within an organisation could be treated very differently on redundancy which would be difficult to explain and could result in a legal challenge.

Another concern is which employers have been exempted, as there does appear to be a very definite objective to put restrictions on the more basic public sector staff whereas other publically owned bodies such as banks and media companies are excluded. There is no valid reason to exclude these employers from austerity measures.

It does appear that employers are also being restricted in how they manage their workforce. There can no longer be a recruitment package which can include the pension arrangements as a benefit that can be relied on in the future, if it is subject to constant future changes.

Managing downsizing will be affected with the process of redundancies taking on a different slant in that employers must be aware of the implications of these new proposals for employees. It is more than likely that there will be fewer volunteers to take severance on redundancy as a result, leading to more compulsory redundancies and adding to already difficult downsizing challenges.

Scheme Member inequalities

Following Lord Hutton's review of public sector pensions in 2011, there was a Heads of Agreement made in December 2011. As a result all the respective public sector departments went into discussions with relevant employers and trade unions to produce an appropriate pension scheme within its cost ceiling for each workforce.

Each element of the scheme was costed so that the specific package agreed was within the cost ceiling.

All the public sector pension schemes were each separately negotiated and agreed between Departments, Employers and Unions and then submitted for HM Treasury approval, and yet within 18 months of the new LGPS becoming operational, new restrictions are now to be imposed changing the scheme structure which is certainly at odds with the previous comments of the Chief Secretary to the Treasury that the schemes would be around for 25 years.

Under the existing pension scheme at that time the LGPS had a provision that on leaving on grounds of redundancy /efficiency over the age of 55 any pension benefits accrued would be payable immediately.

Other public sector schemes such as Teachers and NHS had the provision that the member had to elect to receive benefits and suffer any reduction for early payment. It was expected that for the new scheme arrangement in 2014 that the same condition would be introduced within the LGPS but no such change was forthcoming. As a result, it can only be presumed that all parties were in agreement with this decision.

As stated above there is a difference between certain public sector pension schemes as regards being entitled to immediate benefits if reason for leaving is redundancy.

As those schemes that do not allow immediate benefits give the member the right to decide whether to take a reduced benefit, will other schemes like the LGPS, be changed to allow the member to receive redundancy and severance payments but defer receiving their pension benefits until the total exit payment cost is below the cap level? If so will the benefits still be unreduced from this point?

There are several points that need to be considered here as the retirement conditions of these schemes were not exactly the same and it would be unfair to disadvantage members of the LGPS. [LGPS abolished its early retirement rule of 85 with some limited protection whereas the other schemes kept retirement at 60 for existing members.]

There needs to be some clear understanding as to how the cap will be operated as the draft regulations do not give any indications on which to respond. Areas that need to be address are as follows:

1. The LGPS does not allow an individual to defer. All the draft regulations provide is that a payment can be made which does seem to imply that delaying is not an option. There is no detail as to how the payment is to be made or calculated so an employer could decide to recover from the pension over a period.

2. If actuarial guidance is to be provided there may be no way to respond to the basis of this calculation until after the regulations are passed.

3. By setting an exit cap of £95,000 automatically introduces inequality as members of the LGPS will in some circumstances have higher strain on fund costs because of the way public schemes dealt with protections for early retirement. The LGPS uses actuarial reductions to age 65 whereas others only to age 60.

The major reason given for the change to introduce an exit cap is to curb exit payments for high profile retirements particularly those scheme members with high salaries, it would seem from the consultations that employees earning above £80,000 are deemed high earners. The cap suggested of £95,000 can be shown to be flawed in that other members who have been in the scheme for a substantial period would only have to be on a salary of around £40,000 to be affected by the intended exit cap provisions.

An example showing this is attached as Annex 1. This member over the past 30 plus years has seen their pension expectations reduce over this time. The abolition of the rule of 85 has meant that part of the benefits will now be reduced if retirement is before age 65 and for some part age 66.

On entering the scheme part of the benefit package was that if made redundant immediate benefits would be paid if redundancy occurred after age 50. This age was then increased to age 55 which is the current age but instead of getting full accrued benefits on redundancy it is now intended that the benefits are either reduced or delayed. This member has served local government for over 30 years with increasing pressures being applied to local authorities in recent years with financial restrictions and staff cuts or pay restrictions and would now be penalised further. The restrictions on pay also affects their pension growth so there is a multiple impact on that member's pension value As mentioned earlier there is no explanation of how the excess of £14,000 in the example is to be recovered from the member..

During the period of this membership not only did members receive full immediate benefits on redundancy after age 50 but a significant number were even given additional service up to a further 10 years to compensate loss of potential pension. No action has ever been proposed to get these individuals to pay towards this.

There is no indication of an intention to phase in the cap but merely come straight in with the proposed cliff edge approach. Any scheme member within 10 years of age 60 will find it difficult to make provision to compensate any potential reductions in benefits should redundancy occur

Managers who have been downsizing their departments over the past few years will find themselves caught by these restrictions if they happen to be last out the door. It would appear that despite their efforts in the process they will have their benefits reduced just because they leave after these restrictions take effect.

If the intention is to prevent adverse publicity and public perception due to exit payments being made following ineffective work practises then it would seem more appropriate to review the conditions whereby pension benefits are forfeited. This could then be directed to cover all publically owned employers [including institutions like banks and media] as well as private employers working on public sector contracts. Most of the high profile payoffs in recent years have come within these areas and excessively greater amounts than within the classified employers.

Within the public sector, exit payments are used in the most sensitive cases but before such agreements are made the employer will have key decisions to make regarding an individual. Cost of the severance payment will have to be weighed against the potential other costs that may arise from a legal challenge including the legal costs themselves. So it would appear that the cases the government is determined to curtail may well be the very cases that in fact will still proceed.

Although there is a provision that a full council could provide an exemption to the cap applying this would not help the general long serving members as in most cases within local authorities where discretions are made it is usually only the high profile cases that are considered and usually this would already be with full council approval.

Exit Payment Clawback

The first area on clawback that needs consideration is whether the salary of £80,000 should only relate to the outgoing post or also be applied to the new employment or either. There could situations that appear to be quite inequitable.

The table below shows that if the salary is only restricted to the exiting employment there would appear to be anomalies:

Member	A	B
PAY ON EXITING	£79,950	£80,000
Service (yrs)	35	25
NEW PAY	£100,000	£25,000
Clawback	No?	Yes?

The strain costs here could be very similar but only one individual may be affected by the clawback. Consideration should therefore to given to the financial situation in each case and legislate a fairer system as to benefit gained by the subsequent re-employment.

Before April 1998 the LGPS had a provision that a pension would be abated on re-employment with a new LGPS employer if the new pay plus pension exceeded the pay at retirement. This compulsory provision was changed in 1998 so that administering authorities could decide whether to abate and whether this would be in all or specified cases. When flexible retirement was introduced abatement was specifically excluded in such cases.

This consultation intends to deal with members who have retired with exit costs to the employer having to repay these costs if they become reemployed within one year by a specified public sector employer. Why no clawback if outside the one year period? Such a short period could lead to manipulations.

The direction of legislation here seems at odds with the actual pension provisions, where decisions on abatement have gone from compulsion to discretion and now introducing a new threshold for compulsion.

As previously referred to the employers classified as being included seem to suggest that there are two distinct types of public controlled bodies and one type is always subject to restrictions for both pay and pensions while other more high profile get exempted. It seems inequitable that the private sector is not regulated in the same way.

Employer perspective

This report has been shown to the lead officer on employment matters for Bath and North Somerset Council and whilst agreeing to points raised by the administering authority here also wanted to add the following:

> *“My Council is in the process of setting its budgets for 2016/17 and has to be mindful of the proposed changes and the impact this may have upon its plans and implementation but is equally concerned to ensure that equitable and workable arrangements are put into place to reflect the value placed in this country on public services.”*

Conclusions

It is the opinion of Avon Pension Fund that these intended changes with regards earnings cap need to be considered against the following

Administration

Further level of complexity to go with many others whilst dealing with austerity

Communications: Requirement to explain this in simple terms to all members when independent financial advisors struggle to cope with the scheme complexity.

Explaining to members and employees

Supporting members in key decisions

Inequality

The selective classification of employers with so many different tiers with some employers being given preferential treatment

Unintended consequences: Effects on benefits on long serving non high profile members who get drawn in accidentally.

Scheme Member

Long term planning: constant changes to pension structures which counters the government's aim of enabling individuals to manage their finances in retirement

Understanding: additional complexities on top of Freedom or Choice, HMRC Allowances following on from scheme changes

Employer difficulties

Recruitment and redundancy processes: devaluing of pensions as part of the remuneration package. Potential reluctance of employees to volunteer for redundancy

Outsourcing issues: Further added complexities to an already complex area by not classifying employers the same way.

This legislation appears to show a direction of Government in respect of the public sector and its pension schemes which may be unintended. Classifications appear to show the break-up of services and the profitable ones will be reclassified as private sector like the Housing Associations.

Some public sector schemes such as police and fire have recently lost key legal battles in certain cases resulting in additional administration required to rectify matters. This could potentially happen with these proposed introductions if the inequalities are not addressed sufficiently.

When Lord Hutton set out to review public sector pensions there was a consensus that they should be regarded as a standard and that there should not be race to the bottom with regards pension provision. The review certainly set out the recommendation that the public sector schemes should be fair and transparent.

It is important therefore that before any of the proposed legislation becomes operative that full consideration is given to all points raised by all respondents as to whether it is currently able to deliver the objectives required in a manner that is fair and tranparent.

Also there are some issues still outstanding as to the mechanism of recovery of payment from scheme members that have not been released and therefore have not as yet been consulted on.

Yours sincerely

Alan South

Alan South
Technical and Compliance Manager
Avon Pension Fund

Annex 1 Example