

# Avon Pension Fund

## Local Government Pension Scheme

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### Re: Consultation on Exit Payment Cap

With reference to the recent consultation regarding the proposed exit payment cap, published on 10 April 2019, this is the response from Bath and North East Somerset Council as the administering authority for the Avon Pension Fund which represents 36,479 active members from 384 actively contributing employer bodies.

In addition to our response to the consultation questions, which follow below, we would like to start by bringing to your attention the following significant concerns and or recommendations we have in relation to this consultation that we feel must be strongly considered, and where necessary addressed, before any such cap is implemented:-

- **There must be a specified minimum level of earnings which triggers the cap and this should be set at a level high enough to ensure that lower earners with long service are not penalised.**
- **The cap should be index linked and subject to annual increases.**
- **A one size fits all approach is not appropriate when the make-up of the different public service pension schemes is so different.**
- **Introducing this cap will cause significant administrative burden for both employers and pension administrators inevitably leading to additional staffing costs.**
- **The LGPS regulations must be changed to allow a member to defer the payment of their pension in the event that they are made redundant over the age of 55 as is available in other Public Service Pension Schemes.**
- **There must be more guidance available to pension administrators in relation to the calculation of the partial reduction and also options available for members to make payment to buy out any such reduction.**

### Section 2 – Proposed scope of draft regulations

**Question 1 – Does draft schedule 1 to the regulations capture the bodies intended (described in section 2.1)? If not, please provide details.**

We believe that draft schedule 1 does capture the bodies intended.

**Question 2 - Do you agree with the current list of bodies in scope, for the first round of implementation? If not, please provide reasons.**

No, if this cap is introduced then we feel that the restriction should apply to all public sector bodies, with no exceptions, from day one. Although, the government expects public sector authorities, who are not

currently listed as being in scope, to apply commensurate arrangements voluntarily, there is no legally enforceable way of ensuring that this happens.

One key area that could be challenged is which employers are considered to be “public sector”. Some employers from public sector schemes are included in the proposed legislation whereas others are excluded, for instance, Universities & Housing Associations are exempt therefore the Local Government Pension Scheme will have the majority of their employers within their Fund subject to the conditions but also some 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. Clearly there is the possibility 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 appear to be excluded.

Many local government workers devote years of loyal service on low pay. The Government’s own pay comparisons across sectors show that many working in the public sector could earn higher salaries for the same jobs in the private sector. On grounds of inequality, should the same cap also apply to all private sector schemes as well?

**Question 3 - Do you agree with the exemptions outlined? If not, please provide evidence.**

Please see comments to question 2 above.

### **Section 3 – Guidance and directions**

**Question 4 - Does the guidance adequately support employers and individuals to apply the draft regulations as they stand? If not, please provide information on how the guidance could be enhanced.**

The guidance goes some way in supporting employers to apply the draft regulations, however, as the guidance states, it is the employer’s responsibility to ensure that a payment is not made in excess of the cap and this will inevitably place an additional responsibility and administrative burden on already strained employers. Managing downsizing will be affected with the process of redundancies taking on a different slant in that 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 which could result in costs materially higher than the level of the cap. 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. Managers who have been downsizing their departments over the past few years may 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.

Where there is flexibility, such as the priority between cash payments and pension strain costs, these will have to be clearly communicated to the employee to allow the required decisions to be taken.

Engagement between pension funds, their employers and the individual members who are involved will be required at a much earlier stage in the process to facilitate this and this will involve much more work for all involved with the numerous options available and especially with regards to partial buyouts.

Although it is the assumption that employers will, where possible, cap the redundancy lump sum and allow individuals to receive their pension top up in full, this is not a requirement under the regulations meaning that employers will be able to opt for the pension to be reduced instead, this should be for the employee to decide as their pension could be significantly reduced due to an employer decision. As the guidance suggests, it is the governments expectation that pension schemes will provide members with options to use their own monies to make up any shortfall or to take a partially reduced pension where the pension strain cost is to be capped, which places massive additional administrative burden on to administrators. In addition, it should not be assumed, as seems to be the case, that all members will be in a position to make up the shortfall in full.

There is also no indication of an intention to phase in the cap but merely come straight in with the proposed cliff edge approach. Any scheme member over the age 55 will find it difficult to make provision to compensate any potential reductions in benefits should redundancy occur.

Has there been any engagement with pension administration software providers? Significant work is likely to be required to implement any changes required to calculations and systems will need to be ready for such a significant change in calculation methodology such as partial reductions. Most pension administrators encourage members to self-service, for example, carrying out their own pension estimates to ease the administrative burden, how will this work with the additional options available to members in relation to their redundancy benefits and how will they even begin to understand this without significant support from pension administrators. Another exercise often carried out is the running of bulk redundancy calculations for employers who are carrying out mass redundancy exercises to provide them with strain costs and figures for their members, how will this be possible with the multitude of options that may be available with regards to the strain cost. A costing exercise should be carried out to determine whether the savings gained by the cap would significantly outweigh the cost of the extra administration involved.

**Question 5 - Is the guidance sufficiently clear on how to apply the mandatory and discretionary relaxation of the regulations, especially in the case of whistleblowers?**

Whilst we feel that the guidance on the application of the relaxation is sufficiently clear, there is no indication as to the expected timescales involved for cases where the consent of HM Treasury is required which we feel would be useful for employers.

**Question 6 – Is there further information or explanation of how the regulations should be applied which you consider should be included in the guidance? If so, please provide details.**

The guidance for pension scheme administrators is severely lacking, for us as administrators of the LGPS it provides no assurance that the proposed amendments to the regulations to allow for partial reduction of a member's pension benefits, where otherwise the exit payment cap would be breached, and the option for a scheme member to pay a charge to buy out some or all of that reduction will come into force at the same time as the cap.

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

1. The LGPS does not allow an individual to defer the payment of their benefits in the event of them being made redundant etc over the age of 55. The option to do so in other public service pension schemes already exists.
2. There is no detail as to how the payment that a member is able to make to cover any shortfall in pension is to be made or even calculated and whether this can be recovered from their lump sum retirement grant etc. 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. The LGPS regulations state that a pension strain cost is to be calculated by an actuary appointed by the administering authority. Due to the differences in demographic make-up across the country these factors can often differ from one administering authority to another meaning that the strain cost will also differ. We feel that a standard method of calculating pension strain across the LGPS should therefore be introduced to give consistency across the scheme.
4. By setting an exit cap of £95,000 this automatically introduces inequality as members of the LGPS will in some circumstances have higher strain on fund costs because of the way public sector schemes dealt with previous protections for early retirement. The LGPS uses actuarial reductions for the period from a member's retirement date to their State Pension Age, subject to a minimum of age 65.

#### **Section 4 – Devolution summary and equalities impacts**

##### **Question 7 – Are there other impacts not covered above which you would highlight in relation to the proposals in this consultation document?**

1. The original reason given for the change to introduce an exit cap was to curb exit payments for high profile retirements particularly those scheme members with high salaries, but what about the effects on benefits of long serving low salaried members who get drawn in as a consequence of the way our scheme is structured. We have carried out some analysis on exit payments that occurred following redundancy retirements from our scheme over the last 3 years which show that only 5% of the cases that would have been caught by the cap, had it been introduced, earned more than £80,000 with more than 41% of the cases earning less than £40,000. The lowest earner that would have been caught by the cap earned just £29,706 per annum on leaving after dedicating more than 37 years of service to Local Government. Therefore, the suggested cap of £95,000 seems to be flawed in that members who have been in the scheme for a substantial period could be on a salary of less than £30,000 and be affected by the intended exit cap provisions. We therefore feel that the cap should only apply when a person's salary on leaving exceeds a set amount so that it captures the higher earners that it was originally intended to.
2. Some public sector schemes have, over recent years, 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. The cost of

the exit payment will have to be weighed against the potential other costs that may arise from a legal challenge including the legal costs themselves.

3. The proposals will add a further level of complexity, for scheme members, employers and administrators to go with many others whilst also dealing with austerity. Communication and the requirement to explain this in simple terms to all members to support them in making informed decisions when even independent financial advisors struggle to cope with the complexity of regularly changing Local Government Pension Scheme.
4. There is an inability for scheme members to plan for the future caused by constant changes to pension structures which seemingly counteract the government's aim of enabling individuals to manage their finances in retirement and instead is in danger of creating a climate of increased poverty in retirement.
5. It does appear that employers are also being restricted in how they manage their workforce, further destabilising it through increased uncertainty over pension payments. 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.
6. Not to mention that this is directly disadvantaging individuals who lose their jobs due to government austerity cuts.

**Question 8 – Are you able to provide information and data in relation to the impacts set out above?**

1. An example of the analysis of data carried out is attached as Annex 1.
2. An example of some of these key legal battles that have brought about retrospective change, including ongoing cases that are expected to cause retrospective change are:
  - i) Milne v GAD case
  - ii) Norman v Cheshire FRS
  - iii) Brewster v NILGOS
  - iv) Walker v Innospec Ltd
  - v) Sargeant and others v London Fire and Emergency Planning Authority
  - vi) McCloud and others v Ministry of Justice

**Further Comments:-**

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.

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 just 5 years of the 2014 LGPS becoming operational, there have already been many changes implemented and yet more 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.

We hope our response is useful in taking the proposals forward and that full consideration is given to all points raised as to whether it is currently able to deliver the objectives required in a manner that is fair and transparent. We look forward to being updated in due course.

Kind Regards,

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