

Bedfordshire Pension Fund

Guide to outsourcing staff in the LGPS

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1. Introduction

This guide has been written for authorities outsourcing services to the private sector ("**Contracting Authorities**") as well as for the private sector contractors ("**Contractors**"), who wish to provide the transferring employees with continued access to the Local Government Pension Scheme (the "**LGPS**").

This guide may also be helpful to other types of bodies seeking admission to the LGPS, such as not-for-profit bodies and other public funded bodies.

This guide is intended to be a high level explanation of the main aspects of becoming an admission body in the LGPS and is intended to be a starting point for Contracting Authorities considering their obligations with regards to pension protection as part of any outsourcing process.

The LGPS

The LGPS is a funded defined benefit occupational pension scheme provided for the benefit of those employed or working in local government. The LGPS is split into separate regional funds. These funds are administered and invested by a local "administering authority". The relevant fund for your area is Bedfordshire Pension Fund (the "**Fund**") which is administered by Bedford Borough Council (the "**Administering Authority**").

Contractors may be admitted to other funds in the LGPS where they have been appointed to provide outsourced services to other Contracting Authorities in other areas.

The detailed provisions relating to the benefits and administration of the LGPS can be found in the Local Government Pension Scheme Regulations 2013 (the "**Regulations**") (as amended from time to time). The Regulations include provisions relating to admission bodies.

It should be noted that this guide does not constitute legal or actuarial advice and should not be relied upon by any Contracting Authorities or Contractors, who should take their own independent legal (and if necessary actuarial) advice before proceeding down the admission body route.

Broadly Comparable Schemes

It is important to note that under the Best Value Direction (see section 3 below) Contractors may instead choose to provide a pension scheme that has been independently certified as being “broadly comparable” to the LGPS. However, this guide only concerns those Contractors who wish to offer the LGPS.

Where a Contracting Authority has bidding Contractors wishing to provide a broadly comparable scheme then it should contact the Administering Authority to discuss this further as different considerations (such as bulk transfer arrangements from the LGPS) will apply.

2. The Procurement Process

Basis for admission

Whether or not a Contractor is able to participate in the LGPS depends on whether the Contractor meets the admission body criteria requirements specified in the Regulations.

The most common ground for admission is as a body that is providing or who will be providing a service (or assets) in connection with the function of a Contracting Authority as a result of a transfer or services (or assets) by means of a contract or other arrangement i.e. an outsourcing contract.

Typically contracts awarded as part of local authority outsourcing exercises will satisfy the above criteria. However, this will depend upon individual facts and should always be checked.

Early engagement with the Fund

Whatever the situation, it is important that a Contracting Authority discusses the pensions implications of any proposed procurement with the Administering Authority as early as possible in the process.

The Administering Authority will need to ask the Fund actuary and lawyers to prepare the necessary information and draft admission agreement and bond documentation to give to bidders. Contracting Authorities should allow 4-6 weeks as a minimum for this to be prepared. There will be a charge for this work payable by the Contracting Authority.

A tailored version of the draft admission agreement and bond will ultimately be signed once the successful bidder has been identified.

It is important to ensure that all bidders are fully informed of the pension requirements of the contract as part of the procurement process and are given sufficient information to properly assess and price their bids. This in turn will help Contracting Authorities to avoid exposing themselves to unnecessary risks during the procurement process such as heavily caveated bids.

Failure to engage with the Administering Authority at an early stage is likely to lead to problems and delays during the procurement process.

Contact details at the Administering Authority can be found at section 7 of this guide.

3. Principles of Pension Protection

Providing transferring employees (or former employees on a retender) with continued access to the LGPS will usually be a legal requirement for many Contracting Authorities. In particular, where a Contracting Authority is a 'best value authority' then the Best Value Authority Staff Transfers (Pensions) Direction 2007 (the "**Best Value Direction**") is likely to apply to the contract.

Best Value Authorities

In order to determine what level of pension protection will apply to the contract, the Contracting Authority will firstly need to establish whether it is a 'best value authority' or not. Best value authorities are those authorities that are listed in section 1 of the Local Government Act 1999 and include:

- unitary authorities
- town councils
- parish councils
- fire and rescue authorities

If a Contracting Authority is one of the above then it will need to comply with the Best Value Direction when entering into a new outsourcing contract (or re-tendering an existing contract where original transferred employees are still employed by the incumbent contractor).

Best Value Direction

The Best Value Direction is a statutory direction that sets out the pension protection that a best value authority must require as part of the outsourcing contract.

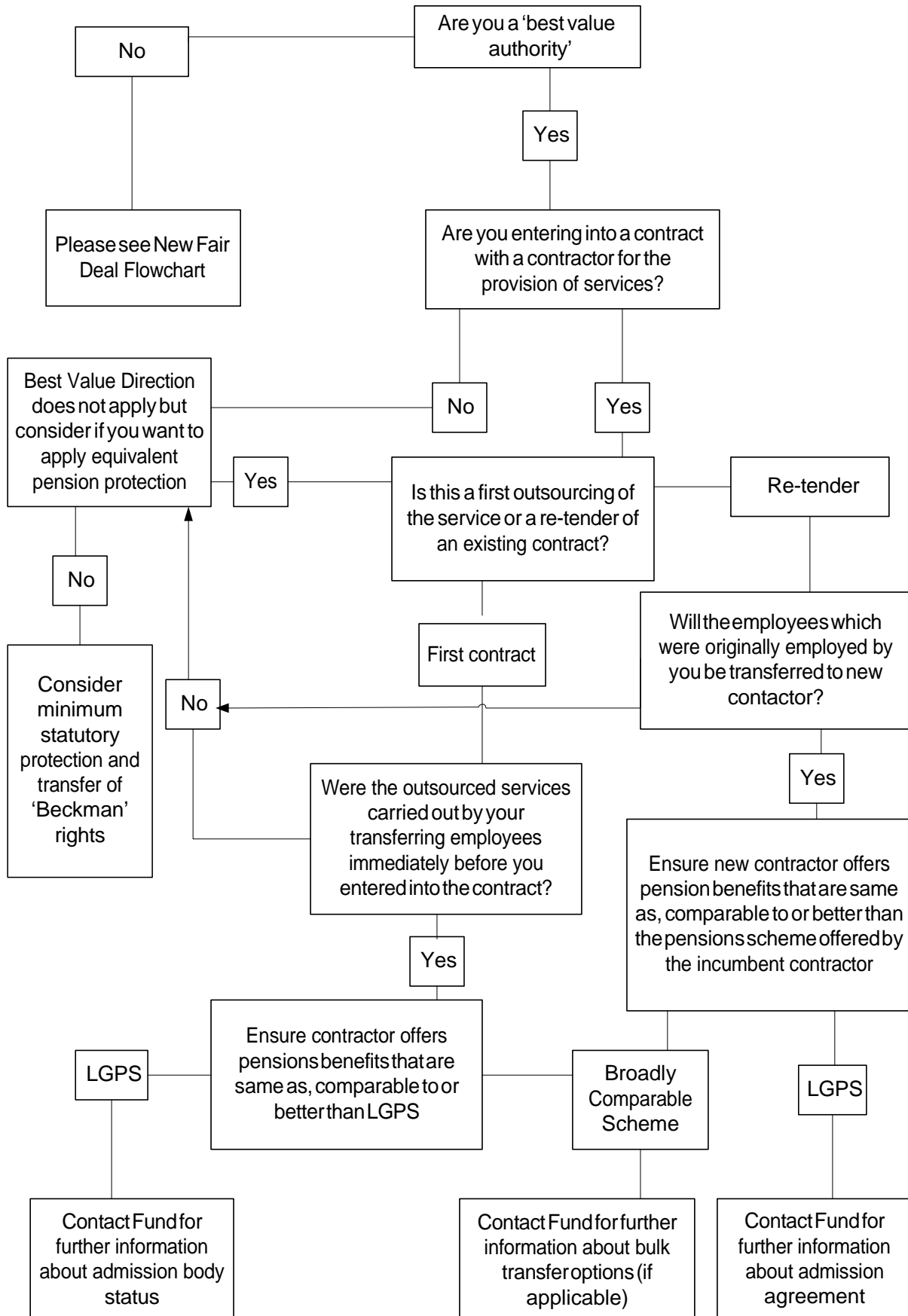
Broadly speaking, the transferring protected employees must be offered pension benefits which are the same as, broadly comparable to or better than the benefits they had in the LGPS as employees of the Contracting Authority. This means that the Contractor must either keep transferring employees in the LGPS under an admission agreement or provide the employees with membership of an occupational pension scheme that has been independently certified as being broadly comparable to the LGPS.

On a retender of an existing contract, the protection is by reference to the pension scheme that former employees of the Contracting Authority were entitled to immediately prior to the subsequent transfer, which may be the LGPS, a broadly comparable scheme or some other form of pension scheme.

Where such former employees are members of a final salary broadly comparable scheme, the Contracting Authority may need to take further advice as to whether re-admitting the employees to the LGPS (which now provides benefits on a 'CARE' basis) would satisfy the Best Value Direction.

The flow chart below provides further information on the application of the Best Value Direction and the required level of pension protection that the Contractor needs to provide.

FLOWCHART TO DETERMINE IF THE BEST VALUE DIRECTION APPLIES



New Fair Deal

If a Contracting Authority is not a best value authority then the Best Value Direction will not apply. However, the Contracting Authority may still be subject to non-statutory guidance that requires similar levels of protection.

HM Treasury guidance "Fair Deal for staff pensions: staff transfer from central government" ("New Fair Deal") issued in October 2013 applies to:

- academies
- maintained schools (where staff are not employed by a local authority)
- NHS bodies
- central government departments and agencies,
- other parts of the public sector under the control of Government ministers where staff are eligible to be members of a public service pension scheme.

New Fair Deal will therefore apply to some employers in the LGPS. New Fair Deal replaced previous HM Treasury Fair Deal guidance that applied from 2000-2013.

New Fair Deal guidance requires that when employees who are members of a public service pension scheme, such as the LGPS, move from the public sector to an independent contractor by way of a TUPE transfer, the employees must remain eligible to be members of their public service pension scheme. The option for the Contractor to provide a broadly comparable pension scheme can only be used in very limited circumstances.

On a retender of an existing contract, the protected former public sector employees should be returned to the appropriate public service pension scheme even if they are currently members of the incumbent contractor's broadly comparable scheme. They should also be given the option to transfer any accrued benefits in a broadly comparable scheme to the public service pension scheme on day for day (or equivalent) terms. Again, the option under New Fair Deal for the Contractor to provide continued access to a broadly comparable pension scheme can only be used in very limited circumstances.

The flow chart below provides further information on the application of New Fair Deal and the required level of pension protection that the Contractor needs to provide.

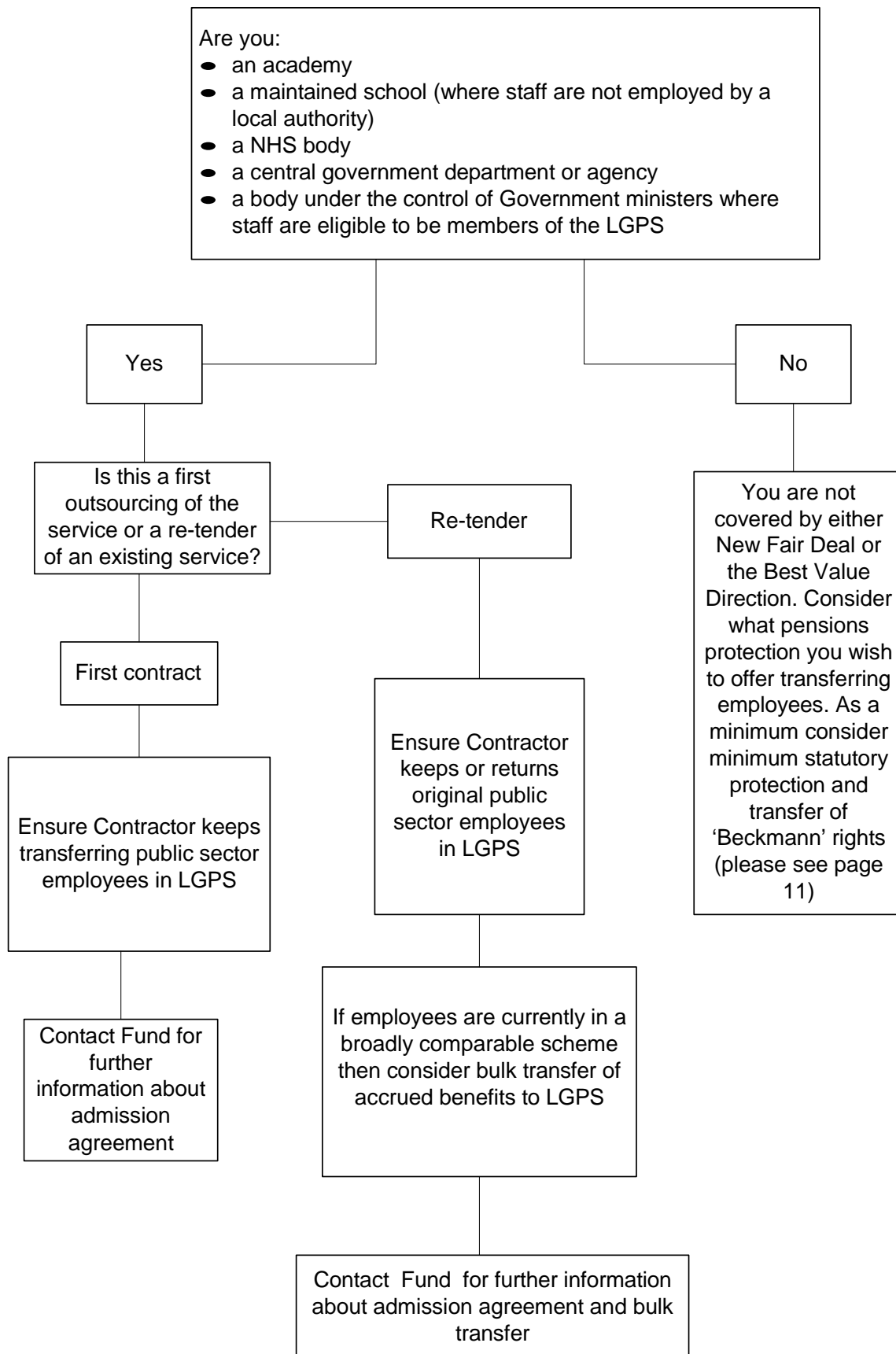
If a Contracting Authority has any doubt about whether it is subject to the Best Value Direction or New Fair Deal then it should take its own legal advice.

Pension Drafting in the Service Contract

It should be noted that neither the Best Value Direction nor New Fair Deal automatically override the terms of the service contract. Therefore, the Contracting Authority needs to ensure that the service contract contains suitable provisions to contractually enforce the Contractor to provide the required level of pension protection.

Contracting Authorities should seek legal advice on such drafting to ensure it is fully compliant. Without such drafting the pension protection may not be enforceable and may expose the Contracting Authority to claims from former employees for not protecting their pension rights.

FLOWCHART TO DETERMINE IF NEW FAIR DEAL APPLIES



TUPE and Pension Protection Regulations

Where a Contracting Authority is not subject to the Best Value Direction or New Fair Deal (for example further and higher education corporations), they may still decide to provide equivalent protection on a voluntary basis.

Where no special pension protection is to be applied then certain minimum statutory protection will apply under either TUPE (in respect of membership of a personal pension scheme) or under The Transfer of Employment (Pension Protection) Regulations 2005 (in respect of membership of an occupational pension scheme such as the LGPS). However, in the case of the LGPS, this statutory protection is far less than that provided by the Best Value Direction or New Fair Deal and would allow LGPS to be replaced by a defined contribution pension scheme where the Contractor only has to match employee contributions up to 6% of basic pay.

Beckmann Rights

Whilst rights to old age, invalidity and survivors' benefits under an occupational pension scheme do not transfer under TUPE, certain early retirement benefits have been held by the courts as being capable of transferring under TUPE. Such benefits are commonly known as 'Beckmann' rights (named after one of the lead legal cases).

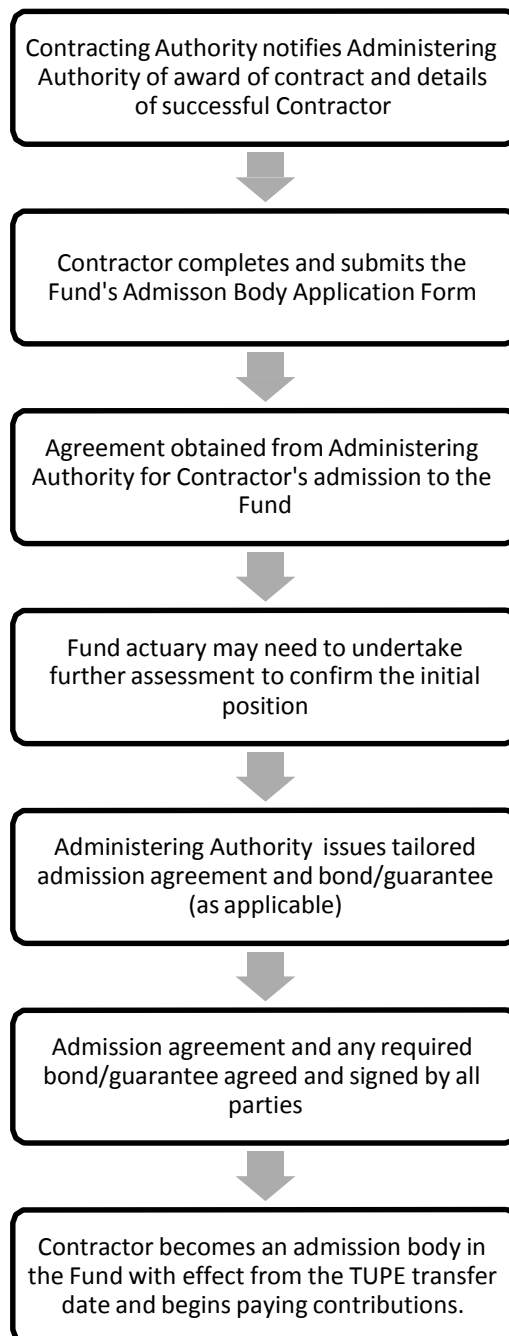
This means that if employees are only given minimum statutory pension protection on a TUPE transfer and are not kept in the LGPS (or a broadly comparable scheme) in their new employment then certain LGPS early retirement benefits, in particular redundancy triggered benefits, may transfer under TUPE to the new employer.

Contracting Authorities should be aware of this issue and take legal advice as necessary.

4. The Admission Agreement

Following the conclusion of the procurement process, arrangements will need to be made to formally admit the successful Contractor to participate in the LGPS.

The admission process following the award of the contract is set out below:



An agreement will be required to formally admit the protected employees to participate in the LGPS. This document is known as an admission agreement.

The Administering Authority has a template admission agreement and bond which can be adapted for the specific contract and provided to Contracting Authorities to supply to bidders during the procurement process (together with indicative employer contribution rates and the bond risk assessment provided by the Fund actuary). Contracting Authorities should allow 4-6 weeks as a minimum for this to be prepared. There will be a charge for this work payable by the Contracting Authority.

Copies of the Fund's template admission agreement and bond as well as the Fund's Admission Body Application Form can be found at http://www.bedspensionfund.org/employers/admitted_body_status.aspx

A tailored version of the draft admission agreement and bond will ultimately be signed once the successful bidder has been identified, has applied to the Administering Authority for admission and the application has been approved by the Administering Authority. There will be a charge for the production of the final documentation (and any further actuarial work that may be required) which will be payable by the Admission Body.

Key points to note in relation to an admission agreement are:

- Admission agreements are tri-partite documents and need to be signed by the Administering Authority, Contracting Authority and Contractor as the admission body. Any bond will also need to be signed by the bond provider and extra time should be allowed for this.
- The LGPS is a funded defined benefit pension scheme and the admission body is agreeing to pay all contributions due from it under the admission agreement and Regulations. These include ongoing employer contributions (which will be assessed at least every three years), early retirement strain costs and exit payments representing any funding deficit that exists when the admission agreement terminates.
- Unless an employee chooses not to aggregate their previous LGPS membership, aggregation will happen automatically so the admission body becomes liable for historic as well as future membership liabilities.
- The admission body will normally be credited within the Fund with assets equal to the value of the historic liabilities at the point of admission. This will normally be assessed by the Fund actuary using the ongoing actuarial basis at that time. The Contracting Authority will normally be responsible for making good any shortfall in the required funding.

- Where the admission agreement relates to a service contract the eligible employees must remain employed in connection with that contract to remain members of the LGPS.
- The admission agreement will terminate on the earlier of (i) the expiry or early termination of the service contract or (ii) when the admission body ceases to employ any active members of the LGPS.
- On termination of the admission agreement an actuarial valuation will be carried out by the Fund actuary using the appropriate actuarial basis at that time and if a funding deficit exists in relation to the admission body then an exit payment will be due equal to the deficit.
- The Contracting Authority will be the guarantor of last resort if the admission body defaults on its payments to the Fund.
- Before the admission body is admitted to the Fund, a risk assessment must be undertaken to assess whether a bond or guarantee is required. This will ultimately help to protect the Contracting Authority in the event the admission body defaults on its payments to the Fund. Please see section 5.
- The admission agreement must include a right for the Contracting Authority to deduct from any payments due from the Contracting Authority to the admission body under the service contract an amount equal to any unpaid contributions owing by the admission body to the Fund. Once deducted the Contracting Authority must pay the monies to the Fund.

5. Bonds and Guarantees

As noted in section 4 above, before an admission body is admitted to the Fund, an assessment must be undertaken, taking account of actuarial advice, of the level of risk arising on premature termination of the provision of service (or assets) by reason of insolvency, winding up, or liquidation of the admission body.

Whilst the assessment must technically be carried out by the admission body itself, this assessment must be done to the satisfaction of both the Administering Authority and the Contracting Authority. In practice, the assessment will be done by the Administering Authority on behalf of the admission body using the Fund actuary.

The Fund actuary will produce a report setting out indicative employer contribution rates and the risk assessment for the bond which can be provided by the Contracting Authority to bidders. This assessment will help to inform the level of bond that will be required in relation to the admission body. Contracting Authorities should allow 4-6 weeks as a minimum for this to be prepared. There will be a charge for this work payable by the Contracting Authority.

Further actuarial work may be required once the successful bidder has been identified. Any fees for this work will be payable by the Admission Body.

The provision of a bond by the Contractor will ultimately protect the Contracting Authority which acts as a guarantor of last resort to the Fund.

Bonds

In the event that the risk assessment indicates that a bond is required, the Contractor will need to arrange for a third party bank or insurance company (that meets to requirements of the Regulations) to provide this. There will normally be a fee or premium to provide the bond which will pay money up to the maximum level of the bond in the event of a relevant triggering event.

The Administering Authority has a template bond agreement it insists on which it can provide to Contracting Authorities to supply to bidders during the procurement process (together the bond risk assessment provided by the Fund actuary). As noted above, Contracting Authorities should allow 4-6 weeks as a minimum for this to be prepared.

The level of risk covered by the bond may vary over the term of the admission agreement and therefore regular risk assessments may need to be undertaken resulting in new or amended bonds to cover the revised level of risk.

The scope and frequency of these reviews will depend on the size of the admission body and its liabilities. A review may also be triggered on the occurrence of certain events, such as where the employer closes participation to new entrants, or where circumstances materially change.

Any actuarial fees for such risk assessments will be payable by the Admission Body.

Guarantees

Where it is deemed not desirable to enter into a bond, a guarantee will be required instead.

The Administering Authority reserves the right (after consulting with relevant parties) to decide whether a guarantee is acceptable in the place of a bond and to decide the terms of that guarantee. The Administering Authority also reserves the right to request further information on the financial covenant of the guarantor.

Like a bond, a guarantee is also a written agreement between the Administering Authority, the Contractor and the body chosen by the Contractor to act as the guarantor. The Administering Authority has a template guarantee agreement which it can provide to Contracting Authorities or Contractors on request.

A guarantee can only be provided by a body that meets the requirements of the Regulations and include:

- bodies which fund the admission body in whole or in part
- in the case of a Contractor, the Contracting Authority of that Contractor (i.e. the body you are providing services to)
- a person who owns, or controls the exercise of the functions of the admission body such as a parent company
- a Secretary of State where the admission body has been established by an enactment.

6. Risk Sharing

As noted above, when a body becomes an admission body it is agreeing to various financial obligations and risks that come with participating in a funded defined benefit pension scheme such as the LGPS.

These include obligations to pay ongoing employer contributions (which will be assessed at least every three years), early retirement strain costs and exit payments representing any funding deficit that exists when the admission agreement terminates.

In outsourcing contracts, Contracting Authorities and Contractors will often agree various mechanisms to share the risk of the Admission Body participating in the LGPS. There is a wide range of risk sharing mechanisms that can be agreed in the service contract such as 'cap and collar' and 'pass through' mechanisms. In the absence of such arrangements, the Contractor is directly liable to Fund to pay its obligations and the Contracting Authority will be the guarantor of last resort if the Contractor defaults on its payments to the Fund.

Any risk sharing arrangements are purely a contractual agreement between the Contracting Authority and the Contractor that need to be documented in the service contract. The Administering Authority will not agree to document this as part of the admission agreement (other than to confirm the initial funding position of the Contractor on the commencement of the admission agreement).

The Contracting Authorities should seek legal advice on the drafting of such risk sharing mechanisms. The Contracting Authority may also wish to speak to the Administering Authority about any proposed risk sharing mechanism to check that the Fund can provide any information the Contracting Authority may require for such mechanism to work in practice.

7. Contact Details

For further information on admission agreements or bonds or guarantees or to commission pensions information for procurement exercises then please contact:

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