Scottish Public Pensions Agency
Buidheann Peinnseanan Poblach na h-Alba

Discretion for administering authorities to determine the amount of exit credit - Local Government Pension Scheme (LGPS)

Scottish Government response to the consultation
January 2025

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The Local Government Pension Scheme (Scotland) (Amendment) (No. 2) Regulations 2024 – Consultation Response

1. Introduction

1.1 In May 2024, the Scottish Government consulted proposals to amend the Local Government Pension Scheme (Scotland) Regulations 2018 (the 2018 regulations) to create a discretion for administering authorities to determine an amount that may be payable to an employer exiting the Local Government Pension Scheme (LGPS). The amount of this payment is described as an “exit credit”.

1.2 The intention of the proposals is to revise the current arrangements and provide administering authorities sufficient flexibility to take into account all relevant factors when determining the amount of exit credit payable.

1.3 This document sets out Scottish Ministers’ response to the views received in that consultation.

2. Policy aims for the proposed regulation changes

2.1 Regulations 60 to 61B of the 2018 regulations provide for actuarial valuations of pension fund, and special circumstances where revised actuarial valuations and certificates must be obtained. Under Regulation 61, where a scheme employer exits the scheme, or otherwise ceases to have any active members (and no prospect of enrolling new members) an actuarial valuation is carried out. Prior to 2018, scheme employers were responsible for any estimated shortfall against their liabilities at the point of exit but were not entitled to receive any surplus. Changes were introduced in 2018 to allow risk to be shared more fairly between employers and administering authorities, and since that date an exit credit is due if the employer’s pension liabilities are calculated to be less than the associated assets held at the date of exit.

2.2 These changes mirrored similar provision in the equivalent scheme in England and Wales, where it soon became clear that they could have an undesirable affect. For example, where a local authority had outsourced services to a contractor, the contractor may have to become an admission body within the LGPS for the duration of that contract in order to continue to provide employees access to the LGPS pension scheme. At the end of that contract, the contractor will cease to participate in the scheme and an exit valuation will be completed. An exit credit payment is due to that contractor if the fund is in surplus at that time.

2.3 Within these arrangements, the contractor’s liabilities to the pension fund and the pensions risk remains with the local authority throughout the life of the contract. This is commonly known as ‘pass-through arrangement’ and can mean that any exit credit payment when a contractor leaves the fund, is disproportionate to the risk they have taken on.

2.4 These ‘pass-through arrangements’ are common in England and Wales and in considering this risk to the scheme, the UK Government amended the scheme regulations in 2020 to provide administering authorities with a discretion to determine the amount of exit credit which should be payable to an employer upon exit.

2.5 In Scotland, ‘pass-through arrangements’ are rare and fund authorities at that time did not see the need for a similar change to the regulations here. According to the 2023 valuations, the funding position of the Scottish LGPS has improved significantly indicating an overall funding position of 147% for 7 of the 11 funds. Scottish Ministers are aware that the resulting increase in pension exit credits, which funds are required to pay when an employer leaves a fund, may have a negative impact on cash flow and result in any subsequent risk being passed on to the remaining employers of the funds.

2.6 After consulting with stakeholders and reviewing the experience of funds and employer exits in England and Wales, Scottish Ministers are bringing forward amendments to the regulations in Scotland that broadly align to those made in England and Wales in 2020. A brief summary of consultation responses is included in paragraphs 3.1 to 3.15 below.

2.7 These new regulations will amend the 2018 regulations to create a discretion for administering authorities to determine the amount of exit credit which should be payable to an employer on leaving the LGPS.

2.8 The amendments will apply retrospectively from 1 June 2018 and are expected to come into force on 2 April 2025. However, we propose to make a transitional provision so that any exit credits paid between 1 June 2018 and the date these provisions come into force are not affected.

2.9 This means that any amount already paid as an exit credit is an authorised payment for the purposes of the Finance Act 2004 under section 176 of that Act (payments by public service pension schemes). Any payments which have been made will be treated as if the administering authority had exercised its discretion to pay that amount. The administering authority may not seek to change the amount due, or exercise discretion retrospectively.

2.10 In cases where an administering authority has not yet paid an exit credit, it may now exercise its discretion in determining the amount of exit credit that is due. Administering authorities should exercise that discretion within six months of the employer exiting the scheme, or within a longer time as agreed between the administering authority and the exiting employer.

3. Consultation summary

3.1 A short technical consultation was carried out between 9 May and 30 May 2024. There were twelve responses to the consultation, some in agreement with the proposed changes and others, primarily those representing charitable 'Third Sector' employers, were not.

3.2 Some respondents raised concerns about the existing provisions and the negative impact of exit credits on a fund's cashflow. However, an employer exit is a known event and is usually planned for well in advance of leaving the fund, often as a result of successive valuation results. The 2018 regulations also provide that the valuation amount is fixed for 90 days after the valuation of the exit credit (or debit) to allow for an employer to discuss the exit payment with the fund authority and any relevant partners.

3.3 Other respondents suggested that exit credits/debits are not usually material in the context of the cashflow position of the fund. The six-month deadline for payment of an exit credit or debit ensures that employers are paid (or pay) the balance within a reasonable time, but there is flexibility for a longer timescale to be agreed by both parties, as necessary.

3.4 In response to concerns expressed by some respondents regarding the effect of the proposed changes on small businesses, the Scottish Public Pensions Agency commissioned an assessment by the Government Actuary Department (GAD). This was designed to measure the effects of the proposed changes and assess possible risks to employers, including those in the Third Sector.

3.5 In their assessment GAD concluded that Third Sector employers may be impacted by the regulation changes from both perspectives, i.e. as an 'exiting' employer, but also as an employer remaining in the fund when other employers exit the scheme. The considerations are similar to those of other types of scheme employer in that, should there be a scheme deficit, the employers who remain in the LGPS, will share the cost of those resulting liabilities.

3.6 Employers in the LGPS include many different bodies, such as housing associations, leisure centres, women's aid organisations and providers of mental health services. These non-profit organisations provide a service to local communities, providing support to those in need by reason of age, ill-health, disability and financial hardship. Respondents suggested that as a result of this amendment, a reduction in an employer's exit credit could have a negative consequence on that employer's ability to provide these services.

3.7 Some trade union representatives were concerned that if the regulations were not changed, the current surplus could lead to an increase in employers leaving the scheme, due to a reduction in grant funding or other financial challenges, to access excessive exit credits and offer alternative pension provisions to members,

3.7(contd.) resulting in those members receiving inferior pension benefits on retirement. This could be particularly relevant in the LGPS, where 75% of the members are female.
As the members most likely to take maternity leave, carer's leave, look after pre-school children and ageing parents, this places clear limitations the amount of pension they will accrue during their working lives. 'The Gender Pensions Gap', research paper published by the UK Government in August 2024 concludes that women, on average, will have to work an extra 19 years to retire with the same pensions savings as men.

3.8 Some representatives of Third Sector employers raised concerns that introducing this discretion might allow administering authorities to pay little or no exit credit to an employer leaving the fund. In response to this, we propose that changes should be made to the requirements in the Funding Strategy Statement of each fund (FSS) to ensure that administering authorities set out their published strategy on how exit payments will be calculated.

3.9 To deliver this SPPA proposes that Scottish administering authorities adopt the approach set out in the 'Guidance for Preparing and Maintaining a Funding Strategy Statement' (FSS) recently published by the Local Government Pension Scheme Advisory Board in England and Wales on their website. This guidance is intended to assist employers and funds when agreeing 'an exit strategy'.

3.10 The guidance was written in partnership between the LGPS SAB (E&W) the Chartered Institute of Public Finance and Accountancy (CIPFA) the Ministry of Housing, Communities and Local Government (MHCLG) in consultation with funds, industry experts and other interested stakeholders, including representatives of the Scottish Local Government Scheme Advisory Board, which has endorsed this guidance for use by Scottish administering authorities.

3.11 This guidance provides that the FSS should also set out in general terms, the termination assumptions basis on which surpluses or deficits will be calculated. Where the fund has a discretion in decisions on the level of exit payment to be paid, the FSS should set out the factors that may be considered and the process to be followed in exercising that discretion.

3.12 Adhering to the guidance will ensure that funds set out how their discretion will be applied, to ensure a consistent approach to all employer exits, whilst taking into account all pertinent facts when calculating the correct amount of exit credit when an employer leaves the fund.

3.13 Although approaches to exit credits may vary by employer type and factors specific to any particular circumstances, the FSS should be clear on how and when exiting employers will be able to make representations, the timescales for making decisions, and any rights or options to have decisions reconsidered.

3.14 Having considered the responses to the consultation and reviewing the draft amendments, the Scottish Ministers are of the view that making these changes to provide funds with the discretion to determine the amount of exit credit to be paid to an employer leaving the LGPS. The proposed changes, combined with the supporting guidance, are the right course of action and provide a balanced approach to risk for fund employers and administering authorities.

3.15 SPPA would like to thank all respondents for taking the time to send us a response setting out your views on the proposed changes. Also thanks go to colleagues from the Scottish Local Government Pension Scheme Advisory Board, the Ministry for Housing, Communities and Local Government, the Local Government Association and the Government Actuary's Department for giving their time and support.

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