



Guide to Outsourcing and Admission Agreements in the LGPS

September 2020

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1. Introduction

This guide has been written for scheme employers who participate in the Local Government Pension Scheme (the “**LGPS**”) and who are involved in the outsourcing of services to the private sector. The guide also applies to internal departments within East Sussex County Council that are responsible for the outsourcing of services. We refer to such bodies collectively as “**Contracting Authorities**”.

The guide is also relevant for the private sector contractors (“**Contractors**”), who wish to provide the transferring employees with continued access to 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 publicly funded bodies.

This guide is intended to be a starting point for Contracting Authorities when considering their obligations with regards to pension protection as part of any outsourcing process and provides a high level explanation of the process of obtaining admitted body status in the East Sussex Pension Fund (the “**Fund**”).

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 the Fund which is administered by East Sussex County Council and in this capacity is referred to as 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 parts of the country.

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.

2. Best Value Direction and 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:

- the Council
- unitary councils
- district councils
- fire and rescue authorities

If a Contracting Authority is a best value authority then it must 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 imposes a legal obligation on best value authorities to ensure that pension protection is included 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.

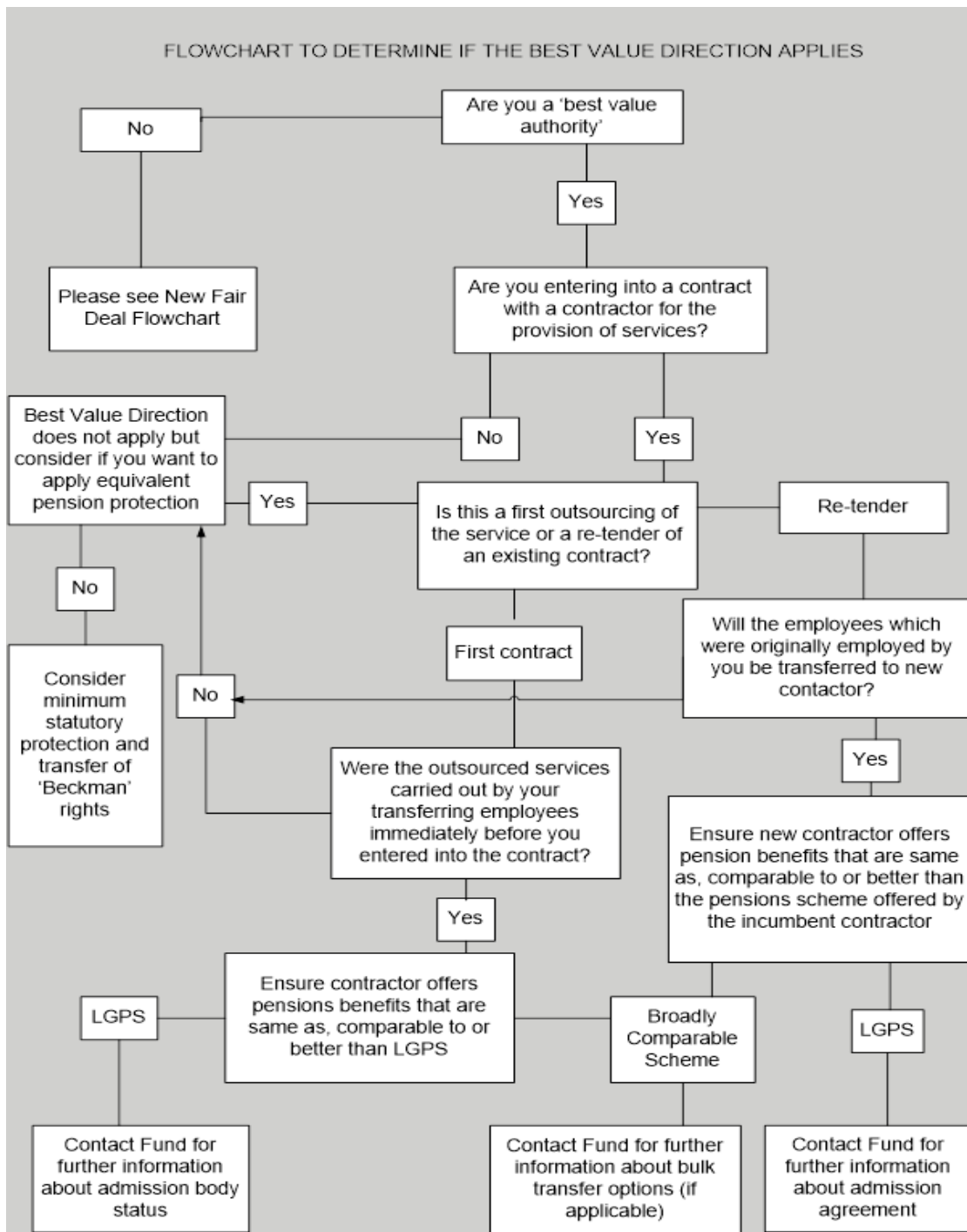
Where such former employees are members of a final salary broadly comparable scheme, the Contracting Authority may need to take further advice as to whether re-admitting the employees to the LGPS (which now provides benefits on a 'CARE' basis) would satisfy the Best Value Direction.

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.

Broadly Comparable Schemes

As noted above, instead of offering continued access to the LGPS, Contractors may 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 instead of the LGPS then it should contact the Administering Authority to discuss this further as different considerations (such as bulk transfer arrangements from the LGPS to the broadly comparable scheme) will apply.



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 pension 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 under the Best Value Direction for the Contractor to provide a broadly comparable pension scheme can only be used under New Fair Deal in very limited circumstances. This is one of the differences between the Best Value Direction and New Fair Deal.

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. Such employees 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.

Basic TUPE and Pension Protection Regulations

Where no special pension protection is to be applied then minimum statutory protection will apply as a matter of law 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).

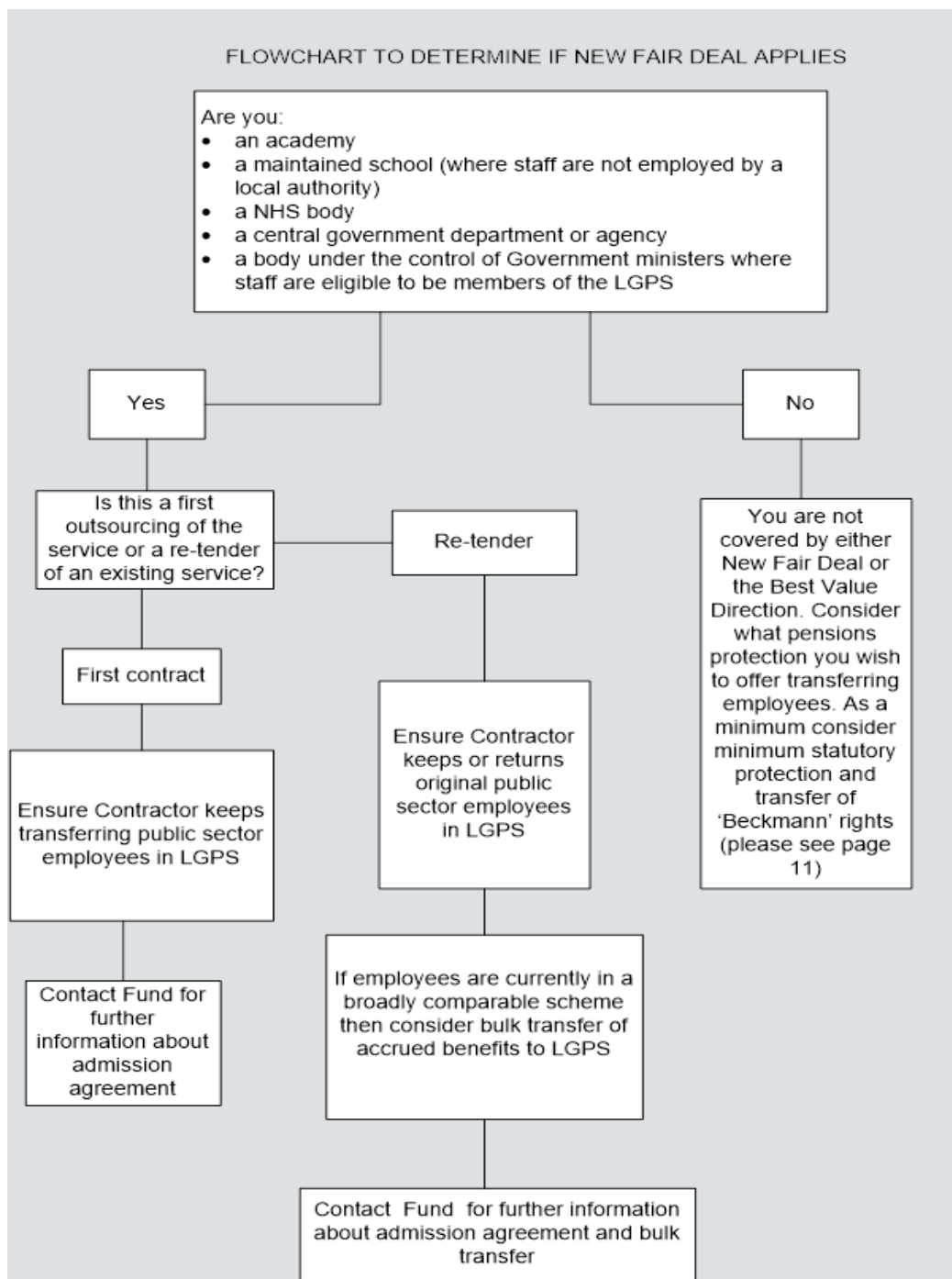
However, in the case of the LGPS, this statutory protection is far less than that provided by the Best Value Direction or New Fair Deal and would allow LGPS to be replaced by a defined contribution pension scheme where the Contractor only has to match employee contributions up to 6% of basic pay.

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 Contractor.

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



3. Terms of 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.

It is therefore essential that the Contracting Authority ensures that the service contract with the Contractor contains suitable provisions to contractually require the Contractor to provide the required level of pension protection i.e. membership of the LGPS (or a broadly comparable scheme - where applicable).

Model clauses for the LGPS can be found in the Cabinet Office's Model Services Contract.

The drafting may also need to cover bespoke risk sharing arrangements that the Contracting Authority is prepared to offer the Contractor. This may include referencing any risk sharing provisions contained in the admission agreement (see **Section 7** and the Fund's default pass through policy) and/or documenting other risk sharing provisions that sit outside of the admission agreement.

Contracting Authorities should seek specialist legal advice on the drafting of such pension terms for the service contract to ensure the drafting is fully compliant.

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 require equivalent protection on a voluntary basis.

4. Procurement and the Tender Process

Pensions and Procurement

Pensions will be a key issue on any public sector procurement involving a transfer of staff and it will be vital to ensure that bidders are provided with as much pensions information as early as possible in the procurement process.

This will help to identify pension issues early and will allow for a much smoother procurement process and contract implementation.

Clarity over the required level of pension protection and issues such as the allocation of pension risk will help to ensure that all bidders are fully informed of the pension requirements of the contract and have sufficient information to properly assess and price their bids. This will avoid bidders submitting unclear or heavily caveated bids.

Raising the pension issues early in the procurement process will also help to avoid unidentified pension issues arising late in the process, resulting in potential delays or, in the worst case, abandonment of the procurement.

Early engagement with the Fund

Whatever procurement route the Contracting Authority is using, it is vital that the Contracting Authority discusses the pension implications of any proposed procurement with the Administering Authority as early as possible and certainly before any Invitation to Tender (or equivalent document) is issued.

The Administering Authority will need to ask the Fund actuary to prepare actuarial assessments and ask its lawyers to prepare the necessary draft admission agreement and bond documentation to give to bidders.

Contracting Authorities should allow six weeks as a minimum for this to be prepared.

There will be a charge for this work payable by the Contracting Authority.

A final version of the admission agreement and bond will ultimately need to be signed once the successful bidder has been identified and appointed.

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 8](#) of this guide.

The Fund's admission process is set out at [Appendix 1](#) of this guide.

5. The Admission Agreement

Basis for admission

Whether or not a Contractor is able to participate in the Fund under an admission agreement will firstly depend 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 of services (or assets) by means of a contract or other arrangement i.e. an outsourcing contract.

Typically most 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 with the Fund.

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

The admission process is set out at [Appendix 1](#) of this guide.

The Admission Agreement

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 if required) 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 four weeks as a minimum for this to be prepared. There will be a charge for this work payable by the Contracting Authority.

A final version of the admission agreement (and bond if required) 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 may be a further 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.

Please note that the Administering Authority will not accept amendments to its template admission agreement other than amendments to confirm which of the various alternative provisions are to be used, factual changes relating to the details of the parties or the contract and minor factual changes such as the correct execution block for the parties.

Any other provisions which are not covered by the admission agreement would need to be agreed between the Contracting Authority and the Contractor and documented separately in the service contract or a side agreement (see [Section 3](#) above). The Administering Authority would not be a party to that separate arrangement or be bound by those provisions.

Key Points About Admission Agreements

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. This should be signed before the contract goes live and the staff transfer under TUPE to the Contractor
- any bond required to accompany the admission agreement 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. Subject to any risk sharing arrangements (see **Section 7** and the Fund's default 'pass through' policy below), 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 of previous LGPS membership 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 (subject to any risk sharing arrangements) an exit payment will be due equal to the deficit. If a surplus exists then an exit credit may be payable to the Contractor
- 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 6** below
- 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

Timing of the Admission Agreement

It is the Administering Authority's strong preference that, wherever possible, the admission agreement (and bond where required) should be signed by the Administering Authority, Contracting Authority and Contractor before or at the point the contract goes live and the staff transfer under TUPE to the Contractor.

Whilst an admission agreement can be signed after the TUPE transfer and be backdated, this is not ideal for a number of reasons, including:

- the employees that are the subject of the admission agreement will not be active members of the LGPS until the agreement is signed
- the employees will be classed as deferred members of the LGPS in respect of their former employment
- as deferred members, the employees are not accruing benefits under the LGPS and are not entitled to the same death benefits and other ancillary benefits such as ill-health as active members
- the Contractor may be in technical breach of its automatic enrolment duties
- the deduction of employee contributions from pay whilst the employees are not active members of the LGPS may amount to an unlawful deduction

Early engagement with the Administering Authority should ensure that the admission agreement (and bond) is signed on time which will avoid all of these issues.

Ultimately if the admission agreement is not signed, the Contractor will not be an admission body and will not participate in the Fund. This is likely to result in a breach of a properly drafted service contract and may even trigger a right for the Contracting Authority to terminate the contract.

Discretionary Policy Statement

Once a Contractor becomes an admission body in the LGPS it must put in place a written policy in relation to the exercise of certain of its discretionary functions under the Regulations such as the funding of additional pension, flexible retirement, the waiving of actuarial reductions and the award of additional pension.

It must provide a copy of the statement to the Administering Authority and keep this statement under review from time to time.

The Administering Authority can provide a template discretionary policy statement on request.

6. Bonds and Guarantees

As noted in **Section 5** 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 then be provided by the Contracting Authority to bidders.

This risk assessment will help to inform the level of bond that will be required in relation to the admission body. Contracting Authorities should allow six 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. The requirement for a bond will therefore generally be a decision for the Contracting Authority.

Where the Fund's default pass through policy is used in relation to the admission agreement (see **Section 7** below), the risk assessment for the bond will normally be limited to redundancy risks only.

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 the bond. 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 six weeks as a minimum for this risk assessment 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 during the term of the service contract resulting in new or amended bonds to cover the revised level of risk.

If the term of the bond is shorter than the term of the service contract, a replacement bond will need to be provided.

The scope and frequency of the bond 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 the Contractor is 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.

7. Risk Sharing

Risks of Participating in the LGPS

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:

- **Increases in employer contributions** - The Administering Authority is required to undertake an actuarial valuation of the Fund every three years to assess the Fund's assets and liabilities. This can result in increases (or decreases) in employer contribution rates which the admission body is required to pay. The Administering Authority may, in certain circumstances, undertake more frequent valuations for the admission body.
- **One-off ('strain') payments** - Certain early retirement events, for example redundancy, can lead to a call for immediate contributions from the admission body to fund the cost of such benefits.
- **Exit payments** - When the admission agreement terminates, usually at the termination of the service contract or if the last active member leaves before then, the Administering Authority will undertake a closing valuation to determine if the admission body is in deficit (or surplus) within the Fund. Where there is a funding deficit, this will result in the payment of an exit payment by the admission body. Where there is a surplus in the Fund this may result in the payment of an exit credit.

The Fund's Default 'Pass Through' Policy

To address the above risks of Contractors participating in the LGPS and the fact that Contractors are increasingly seeking protection against such risks, the Administering Authority has since 1 April 2019 set a policy that any new Contractor admission agreements are set up using a default 'pass through' arrangement.

Pass through arrangements allow for the pension risks to be shared between the Contracting Authority and the Contractor. Typically the majority of the pension risk is borne by the Contracting Authority and thus the liability is retained by them. As such the Contractor would not be required to pay any exit payment on termination (or equally receive any exit credit) subject to any agreed exceptions.

However, there is some flexibility within a pass through arrangement. In particular there are two different options that a Contracting Authority can adopt:

- **Fixed Contribution Rate** - Under this option the Contractor pays a fixed contribution rate during the term of the admission agreement and does not pay any exit payment (or receive an exit credit) on termination of the admission agreement; and
- **Pooling** - Under this option the Contractor is pooled with the letting Contracting Authority and so will pay the same employer contribution rate as the Contracting Authority. The rate may change over the term of the admission agreement but should provide some stability. As with the fixed rate option, the Contractor does not pay any exit payment (or receive an exit credit) on termination of the admission agreement.

The Administering Authority's default approach will be to set up pass through arrangements using the fixed contribution rate option for all new Contractors.

However, the Administering Authority will equally administer the pooling option if the Contracting Authority would prefer to use that option.

As the risk and therefore the financial liability ultimately rests with the Contracting Authority, it is for the Contracting Authority to agree the appropriate option with the Contractor.

In either case, the option must be documented in the admission agreement. This should also ideally be referenced in the pension terms of the service contract (see [Section 3](#) above).

Under either option, some element of risk will still transfer to the Contractor relating to the Contractor's decisions as it is unfair to burden the Contracting Authority with such risks. For example, the Contractor will typically be responsible for pension costs relating to:

- above average pay increases, including the effect in respect of membership accrued prior to the contract commencement; and
- redundancy and certain other early retirement decisions.

Bond Requirements Under the Default 'Pass Through' Policy

Where the pass through option is used, the risk assessment for the Bond will normally be limited to redundancy risks only. The requirement for a bond will generally be a decision for the Contracting Authority.

Exceptions to the Default 'Pass Through' Policy

Exceptions to the policy will be considered on a case-by-case basis at the Administering Authority's discretion.

If the Contracting Authority does not want to use the default approach but instead wishes to pass all risks of participating in the LGPS to the Contractor then it must notify the Administering Authority.

Again, early engagement with the Administering Authority is essential to ensure there is sufficient time to resolve these issues.

8. Contact Details

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

Sian Kunert
Head of Pensions
East Sussex County Council
County Hall
St Anne's Crescent
Lewes
East Sussex
BN7 1UE

Email: pensions@eastsussex.gov.uk

Website: www.eastsussexpensionfund.org

Appendix 1

