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By email to LGF Reform and Pensions Team at LGPensions@communities.gov.uk

Dear Sirs,

**Re: Local Government Pension Scheme: Changes to the Local Valuation Cycle and the Management of Employer Risk - Policy consultation**

**General Observations**

In response to your consultation on Local Government Pension Scheme: Changes to the Local Valuation Cycle and the Management of Employer Risk, please accept this as the response from East Sussex County Council (ESCC) in its capacity as administering authority to the East Sussex Pension Fund (ESPF).

The ESPF has over 74,000 scheme members and 133 contributing employers, including local authorities, academies, private contractors and small local charities. The actuarial valuation of the fund was carried out as at 31 March 2016 and set the employer contribution rates from 1 April 2017 to 31 March 2020, and is discussed in some detail in the Funding Strategy Statement. It is important to note that significant valuation shortfalls are rarely funded in one go. The Pension Fund's strategy is to phase in its own contribution rate increases over three years, with the view of recovering the deficit over 20 years. The Pension Fund Funding Strategy Statement explains how it intends to meet those liabilities over the longer term.

ESPF is a member of various networking groups, such as the CIPFA Pensions Network, where information and ideas are readily shared. The consultation brings together a number of changes, most of which we welcome. The proposal to move the local valuation cycle (which sets employer contributions) from triennial to quadrennial to align with the scheme valuations (carried out by GAD for cost management purposes) has been well trailed although the rationale is weak when considered from a local, funding perspective. MHCLG does, however, appear to recognise this and has proposed a number of potential mitigations, including interim valuations. In addition, the valuation cycle within the private sector has been taking place every three years, which has worked well for over 20 years, and there is a trend there to move to more regular valuations as technology has reduced the manual number crunching required.

The consultation also proposes to address what has proved to be a material oversight in the introduction of the requirement to repay an exit credit to an outgoing employer, i.e. the failure to allow administering authorities to consider any risk sharing or other arrangements which are not consistent with any surplus being repaid on exit. Many administering authorities have put exit credits on hold but clarity will be needed on what should happen where exit credits have already been paid but where risk sharing arrangements were in place – will steps need to be taken to reclaim these payments?

The ESCC/ESPF responses to the specific questions asked in the consultation re Changes to the Local Valuation Cycle and the Management of Employer Risk are set out below:

## Section 1 - Valuation cycle

**Question 1: As the Government has brought the LGPS scheme valuation onto the same quadrennial cycle as the other public service schemes, do you agree that LGPS fund valuations should also move from a triennial to a quadrennial cycle?**

No – the Fund believe that 3 years remains an appropriate period. There are already mechanisms in place to deliver stability of employer contributions via Regulation 62 of the LGPS Regulations 2013 and CIPFA guidance on Preparing and Maintaining a Funding Strategy Statement. Administering authorities do generally make use of various mechanisms available to them to keep contributions stable. Lengthening the valuation cycle to 4 years does not suit the LGPS for a number of reasons including:

- The LGPS is a multi-employer scheme with many different types of participating employers. Employer circumstances and their financial covenant can change quickly, and lengthening the valuation cycle may expose LGPS funds to greater covenant risk.
- The majority of public service schemes are unfunded. However, the LGPS is funded and holds assets with values and performance that can fluctuate significantly over time. This volatility needs careful and regular management - a longer period puts more pressure on funding strategies, and increases the likelihood of bigger changes to employer contribution rates from valuation to valuation (particularly for shorter term employers such as closed charities).
- The Fund has a funding strategy that stabilise contribution rates, commonly for longer term and secure employers. We are not convinced that a 4-yearly cycle will lead to more stability in rates as suggested in the consultation. In fact, as mentioned above, a longer cycle may lead to the funding position drifting over a longer period and therefore a sharper correction to contribution rate being required at the end of the period.
- Moving to a 4-year cycle, with the use of interim valuations, will also add to the burden of already stretched administration teams. When considering any changes to the current arrangements it is equally important to ensure that administering authorities have the capacity to comply with those changes, at no detriment to their current obligations to scheme members and their dependents.
- The fund believe that the rationale would be stronger if the LGPS were only comprised of long-term, secure employers fully backed by taxpayers for which contributions could be set for 4 years without the risk of employer failure with insufficient funds. However, as budget setting becomes more short-term it's questionable whether those employers would favour contributions being set for 4 years reviews. In addition, there are a number of non-taxpayer backed employers, principally community admission bodies, some of which are increasingly short-term and whose covenant is less strong than the Tier 1 employers.

The Fund has developed much more robust risk management policies in relation to employer risk and moving to a quadrennial valuation cycle where contributions are only reviewed every 4 years would represent a backwards step. It could even increase costs if it meant interim valuations were carried out every 2 years for these employers.

It is difficult to be certain that moving to a 4 yearly cycle will save costs. This will largely depend on the balance of savings made due to a one year increase to the cycle versus the cost of carrying out interim valuations and any other additional employer work required as a result. We are also of the opinion that any cost saving analysis should consider the more substantive possible costs arising from the funding impacts of a delayed valuation as well as costs directly associated with carrying out the valuation process, as well as any interim valuations.

**Question 2: Are there any other risks or matters that you think need to be considered, in addition to those identified above, before moving funds to a quadrennial cycle?**

The impact on annual pension accounting disclosures should be considered. Actuaries in the LGPS use a ‘roll forward’ approach from the latest formal valuation to estimate balance sheets and other figures in FRS102 and IAS19 reports. This approach helps to control the costs of producing disclosures for employer and avoids the need to carry out a full annual valuation based on fresh data. The downside to the ‘roll forward’ approach is its accuracy –the ‘tracking error’ (i.e. the extent to which the estimated figures deviate from the true figures that would arise if a full annual valuation was undertaken) increases over time. Auditors are increasingly querying the use of a ‘roll forward’ approach to cover a 3 year period, and are likely to be very concerned if this were lengthened to 4 years. Moving to a full annual valuation would be time consuming, leading to delays in reporting deadlines and significantly higher costs to employers for producing the disclosures.

One other benefit of a more regular valuation cycle is to recognise that a formal valuation is not just about number crunching. It provides a governance opportunity to undertake a ‘health check’ on the Fund’s data and risk management policies, and the metrics provided (cash flows, benefit projections, funding positions etc.) are often used for strategic investment reviews. Funds following best practice already carry out annual data validation checks and reviews of contributions for short term employers. However, whilst tPR's requirements in relation to data scoring should assist in relation to annual assessments of data quality, if there is no formal requirement for interim valuations the proposed mitigations may have no effect. Increasing the cycle may encourage less governance, and less frequent valuations may therefore be detrimental to data quality.

The Fund is aware that the cost management process is under review, but alignment of the scheme and local valuations on a triennial cycle has not proved to be helpful for the 2019 local valuations. A further consideration should therefore be the timing of benefit/member contribution changes following the cost management process, and how these align with local valuation calculations. The aim should be to avoid a repeat of the current situation, where the 2019 valuations are to be carried out without knowing what the benefit structure of the LGPS as at the valuation date will be.

**Question 3: Do you agree that the local fund valuation should be carried out at the same date as the scheme valuation?**

We can understand why MHCLG may believe this will be helpful, e.g. that the calculations could be based on the same set of data, but we do not believe that this will bring the hoped for benefits. We are aware that GAD had some material concerns in relation to the quality of the data needed to establish the baseline for cost management calculations and that it was thought that accuracy would have been improved had the date coincided with a local funding valuation. However, if funds are adhering to the new tPR requirements, data accuracy should be improved regardless of the local valuation date. To the extent that there are concerns this isn't happening, extending the local valuation cycle may simply make the issue worse, as it will be longer between formal valuation data validation exercises.

Ideally, we think that the ‘as at’ date of the scheme valuation should be ahead (by perhaps a year?) of the local fund valuations. This would allow time for:

- the Government Actuary’s Department (GAD) to gather the necessary data and do the calculations;
- discussion to take place on the results with the various national oversight bodies;
- agreement to be reached over any changes to the benefit structure or employee contribution rates to get the cost of the scheme within the +/- 2% of pay corridor; and
- software providers to make the necessary changes to systems and for those changes to be fully tested ahead of the effective date.

This should avoid changes to benefits or employee contributions being implemented retrospectively and allow time for administration and valuation systems to be updated to reflect the correct structure for the local valuations.

**Question 4: Do you agree with our preferred approach to transition to a new LGPS valuation cycle?**

Yes, we agree that approach b) (completion of the 2019 valuation with a three year Rates and Adjustments Certificate followed by another valuation as at 31 March 2022 and a two year Certificate) is preferred to a five year gap between the 2019 valuation and the next.

Approach a) has the disadvantages relating to scheme governance, potential larger changes in contribution rates due to additional intervaluation experience, and accounting implications referred to above, exacerbated by the period being 5 years rather than 4 years.

**Question 5: Do you agree that funds should have the power to carry out an interim valuation in addition to the normal valuation cycle?**

Yes, this power is needed. LGPS funds have a diverse range of sponsoring employers, and they bring varying degrees of risk. The Fund already closely monitor employer funding positions between valuation dates, particularly for short term contractors or closed bodies close to exit, and use the results to align contribution rates with funding targets. Giving funds full power to carry out an interim valuation and amend the Rates and Adjustment certificate under a wider range of circumstances than the current Regulations allow would be welcome from a risk management perspective.

The consultation is not specific on whether an interim valuation refers to the whole fund only, or if it could be applied only to certain employers. A whole fund valuation would normally require full up-to-date membership data and would be more time consuming and onerous than a valuation undertaken using an approximate ‘roll-forward’ approach. We think it would be sensible for funds to have the discretion to do an interim valuation at either whole fund or specific employer level (on an approximate basis or otherwise), with the decision depending on the reasons for undertaking the valuation.

**Question 6: Do you agree with the safeguards proposed?**

The Fund agrees that safeguards should be put in place to ensure that the power to do interim valuations is being used appropriately by funds and employers. Regulations and statutory guidance on protections is also welcome to ensure that there is some consistency across funds – this will be important for employers that participate in multiple LGPS funds. Whilst the Local Pension Board is not a decision-making body in the LGPS, it does have an oversight role to ensure that funds are complying with legislation and regulations and to hold the

Pension Committee to account. The proposal to consult with the Board should provide comfort to funds and employers that due process is being followed.

We note the proposal for the Secretary of State (SoS) to have the power to require an interim valuation on representation from scheme employers. It would be helpful for funds to understand the factors that the SoS may take into account before using this power – funds will be keen to avoid 'moral hazard' situations where employers lobby for a valuation to take advantage of favourable market conditions.

Consideration also needs to be given to the administrative burden of providing data for interim valuations, particularly where requested by scheme employers. If the scope for requesting and agreeing to interim valuations is not clearly defined, such requests could be an unwelcome distraction and divert attention from the delivery of administration services to scheme members and their dependants.

**Question 7: Do you agree with the proposed changes to allow a more flexible review of employer contributions between valuations?**

We welcome the ability for funds to deal more flexibly with employer contributions between valuations, as the current Regulations only allow for limited circumstances. We believe that this principle should apply to all employers and include contribution rates that apply in the period after cessation (where such arrangements have been agreed). We believe that more flexibility is already needed to amend contributions between valuations so we welcome proposals to facilitate this. It will be important to be able to amend contributions more frequently than quadrennially for all non-permanent employers. But as the consultation suggests, employer contribution reviews may be needed in other areas too, such as following a merger or take-over and this should be extended to material transfers of staff to or from any employer, whether involving another scheme or employer within the fund.

Suggestion would be that any proposals should explicitly allow contributions to be changed:

- if an employer closes the fund to new entrants, including where one employer within a group or pool closes to new entrants;
- if there is a material transfer of staff to or from an employer (noting this has become common in certain sectors, such as mergers of colleges and housing associations), or following a material outsourcing or insourcing;
- if there is a change in covenant, including but not limited to a material change in the level or source of funding of an employer. (It is important that employers provide such information proactively to funds rather than it being for the administering authority to seek out such information);
- where an employer pays contributions above the level specified in the Rates and Adjustments certificate in any year then arguably remaining deficit contributions should be reduced. However, protections maybe needed to prevent payment of additional contributions to trigger a full review when market conditions are favourable, perhaps by limiting contributions reductions to those justified by the additional payment.
- other situations where contributions should be reviewed should be at the discretion of the administering authority as set out in the FSS.

We are less supportive of the reference to a scheme employer being able to request a reassessment because it believes this would lead to a reduction in its contribution rate unless there are safeguards around it, as this provision may lead to employers picking the timing to request such a review, or pay a lump sum deficit contribution to trigger a review, to coincide with favourable market conditions. This would negate MHCLG's objective of stability of contributions and acknowledgement that safeguards are needed to avoid interim valuations being timed to reduce contributions. Therefore, we believe that any provision to allow employers to request reviews of contribution rates should not be so wide ranging that it is open to such manipulation.

**Question 8: Do you agree that Scheme Advisory Board guidance would be helpful and appropriate to provide some consistency of treatment for scheme employers between funds in using these new tools?**

Yes, we think (statutory) guidance would be helpful to ensure some consistency across funds around the process and reporting. It would also be helpful if such guidance were to cover the tests that would need to be met in order for a scheme employer to request an interim valuation itself from the SoS. Any guidance however needs to recognise local circumstances and funding plans, and not fetter the ability for funds to carry out interim valuations in line with their own FSS's.

We suggest that a principles-based approach to guidance would be preferable to a prescriptive approach, and give funds the discretion to demonstrate compliance using methods that work for their own circumstances and employers.

We note that little guidance (other than the CIPFA guidance mentioned in the consultation) is in place about the principles that should apply to full valuations. It seems odd that SAB guidance should be created for interim valuations and yet be missing for full valuations, and we suggest that any guidance should cover both types of valuation, and point out how the process and reporting may differ.

We don't believe that administering authorities need to have identical policies, noting that this is not compatible with local decision-making nor the diversity of funding levels and employers within funds. However, it would be helpful for funds and employers alike if the process by which administering authorities' policies were derived were governed by a single set of principles set out within national guidance.

**Question 9: Are there other or additional areas on which guidance would be needed? Who do you think is best placed to offer that guidance?**

The Regulations make it clear that the Fund Actuary is responsible for undertaking full valuations. Actuaries are bound by professional standards and a code of conduct, and have experience of providing advice that is proportionate to the work being undertaken. The fact that a valuation is interim rather than full does not take away the need for professional advice; the actuary would apply professional judgement over the amount of advice needed under either approach.

It will be important that it is clear that it is administering authorities and not employers who have the final say on reviewing employer contributions. Employers may request interim valuations for accounting purposes and administering authorities should be able to accede to those requests without then being obliged to review the employer's contributions. Other areas which the guidance could cover include:

- Situations that the fund is expected to be included in their FSS as requiring an interim valuation;
- Timescales: "as at" dates for interim valuations, timescales for signing off interim valuations and timing of implementing new contribution rates;
- Situations that shouldn't, on their own, trigger an interim valuation.
- An indication of the circumstances that may or may not 'trigger' the need for an interim valuation, particularly if requested by a scheme employer

## Section 3 - Flexibility on exit payments

**Question 10: Do you agree that funds should have the flexibility to spread repayments made on a full buy-out basis and do you consider that further protections are required?**

It should be noted that the Regulations as they currently stand do not subscribe any one basis for valuing exit debts and in practice, these can differentiate materially between different types of employer and between funds. Funding strategies are set locally and any suggestion that there is (or could be) a standard exit basis would not be welcome. We are not aware of any cessations being carried out on a full 'buy-out' basis as can happen in the private sector. However, we do believe that additional flexibilities would be helpful in constructively managing the exit of any employer, independent of the basis of the exit valuation.

Regulation 64(4) already offers the flexibility for Administering Authorities to agree the repayment of deficits beyond the effective exit date if the agreement takes place while the employer still employs active members of the scheme. The timing of an exit event and the magnitude of any exit debt may not be known until well after the exit event. Therefore, we would welcome any clarification in the Regulations to extend this flexibility to exited employers. This would require an examination of how Regulation 64(4) interacts with 64(2).

Any change to allow repayment of exit debts to the Fund increases the level of risk faced by remaining employers. To manage the additional risks involved in extending this ability, we would suggest –

- This is at the discretion of the Administering Authority (and the guarantor where appropriate), allowing them to make a judgement on the covenant of the underlying employer;
- There is a maximum period for repayment, we suggest this is left as a local decision and included in the funding strategy statement or cessation policy (where applicable);
- Interest be charged at an appropriate rate; and
- The Administering Authority should have the ability to request additional security be put in place during the repayment period.

We would also encourage consideration be given to the interaction of these changes with suspension notices under Regulation 64(2A) and the extension of asymmetries where exit credits are identified (these must be paid within 3 months of an exit event where as we may be giving years to repay exit debts).

**Question 11: Do you agree with the introduction of deferred employer status into LGPS?**

Yes. We agree with the introduction of a deferred employer status and the approach to deferred employer debt arrangements. However, we would suggest that a significant deterioration in covenant is enough to trigger termination (there should not be an attaching other 'relevant event').

It will be important for any proposed regulatory provisions and associated guidance to be robust and subject to a further, detailed consultation. We would be particularly keen to ensure that any regulatory changes flow through to Regulation 62 and other relevant regulations. We would also observe that if a deferred debt arrangement can only be entered into when an employer "has just, or is about to become an exiting employer" this make may it more difficult for administering authorities to develop their funding strategy to cope with the possibility of these arrangements. Employers not admitting new entrants may wish to have clarity years in advance of their potential exit that they will be able to continue to participate as a deferred employer and may be hoping to reduce certified contributions as a result. Given the uncertainty of the timing of any exit and the employer's covenant at that point, it may not be prudent for administering authorities to reduce employer contributions in anticipation of them becoming a deferred employer. Thus whilst it will assist in reducing the effect of a one-off exit payment being required, it may not have the desired effect of reducing ongoing contributions in the meantime.

**Question 12: Do you agree with the approach to deferred employer debt arrangements set out above? Are there ways in which it could be improved for the LGPS?**

We agree that any deferred employer arrangements need to include safeguards for the administering authority. We have seen legal side agreements which appear to commit the administering authority to continue to adopt "an ongoing basis" (i.e. the funding target adopted for local authorities) during the period of the agreement which appears to significantly favour the employer to the detriment of the fund (the only benefit to the fund being that there is an ongoing employer which would meet future funding risks). If the employer had sufficient resources at the point of exit to pay a gilts basis exit valuation entering into such an agreement would represent poor risk management by the fund.

However, viewing the proposed changes through the lens of a contractor/other employer, we can see that being able to request deferred status may be beneficial and justifiable in certain circumstances. Assuming letting authorities support that view (noting that if the deemed employer route is implemented there may be far fewer transferee admission bodies exits in future), the option to spread exit payments could be made available for employers to request as long as suitable guidance is provided to administering authorities on how to assess such requests. We would like to see provisions that –

- termination could be triggered on significant deterioration of covenant without an associated insolvency event, as by that point it could be too late to recover the full remaining exit debt;
- either the employer or the fund can trigger termination without agreement of the other party providing that this then leads to an exit valuation being carried out.

There is a difference of opinion between administering authorities as to whether or not operating different investment strategies for different employers is consistent with the LGPS Regulations. Where deferred debt arrangements are being entered into, and the liabilities will become orphan when the arrangement ends (it unlikely administering authorities will wish to enter into open-ended agreements), a "flight plan" approach whereby the funding and investment strategy are regularly reviewed in light of the longer-term target of being fully funded on a gilts basis may be appropriate, particularly for larger employers. In order to ensure consistency of understanding of what is possible within the Regulations, it would be useful if specific reference could be made to an alternative investment strategy being permitted for deferred employers. This may be of benefit to both the fund and employer in terms of risk management.

**Question 13: Do you agree with the above approach to what matters are most appropriate for regulation, which for statutory guidance and which for fund discretion?**

We agree only the key obligations and entitlements of parties should be set out in the Regulations. Careful consideration should be given to any supporting guidance and whether this is statutory in nature. In particular, funds are not required to follow guidance issued by the Scheme Advisory Board. Therefore, where there is desire for commonality of approach across Funds, this should be detailed in statutory guidance from the Secretary of State. Any commonality must be balanced with local funding strategies and therefore any guidance should have significant input from LGPS practitioners throughout the drafting and consultation stages.

Ultimately it should be for administering authorities, having taken appropriate advice, to weigh up the risks and competing interests of stakeholders so we agree that these matters should be for fund discretion. However, if SAB guidance is only "advisory" the risk will remain of some administering authorities entering into arrangements without as thorough an assessment or understanding of the various risks as would be best practice. As these proposals represent a material shift in how employer exits are dealt with, we believe the guidance should be statutory rather than advisory. It should be noted that a deeper risk analysis does not imply a more risk averse approach leading to infrequent use of deferred employer arrangements. Such analysis could in fact provide administering authorities with the confidence to enter into such arrangements. Statutory guidance could therefore be in the interests of exiting employers if it results in more administering authorities being willing to enter into deferred employer arrangements. Given changes to the Regulations implemented earlier this year we note that it seems that only the Secretary of State can issue statutory guidance. We are not sure if that was intended to preclude SAB from developing guidance, which is then adopted and issued by the Secretary of State; it would be useful if MHCLG could confirm.

**Question 14: Do you agree options 2 and 3 should be available to current rules on exit payments?**

We agree options 2 and 3 should be available as alternatives to the current rules on exit payments. However, as set out in our response to Questions 10, 11 and 12, careful consideration should be given to the need for suspension notices under Regulation 64(2A) and the extension of asymmetries where exit credits are identified.

**Question 15: Do you consider that statutory or Scheme Advisory Board guidance will be needed and which type of guidance would be appropriate for which aspects of these proposals?**

The additional options for managing exits could increase the overall administration costs of the scheme for both employers and administering authorities (whether in relation to actuarial fees or the time required from officers to consider and monitor proposals). Therefore, we believe there needs to be some level of statutory guidance in terms of the interpretation and application of the new Regulations. A balance will need to be struck between compulsion to ensure a consistent interpretation of the Regulations and the ability of funds to manage their own funding and employer risks. We would strongly encourage any guidance to go out for full public consultation.

**Section 4 - Exit credits under the LGPS Regulations 2013**

**Question 16: Do you agree that we should amend the LGPS Regulations 2013 to provide that administering authorities must take into account a scheme employer's exposure to risk in calculating the value of an exit credit?**

We agree that changes are required to remove the unintended consequences of the 14 May 2018 amendments. However, it is worth noting that there is a very wide range of risk sharing arrangements in place so it is not as simple as saying that if pass through is in place no exit credit is payable. In addition, by putting the onus on the administering authority, the fund will then be adjudicating on what is, in many cases, a contractual arrangement between two employers.

It should be noted that the Regulations as they currently stand do not subscribe any one basis for valuing exit credits and in practice, these can differentiate materially between different types of employer and between funds. Funding strategies are set locally and any suggestion that there is (or could be) a standard exit basis would not be welcome. We are not aware of any exit valuations being carried out on a 'full buy-out' basis as can happen in the private sector. However, we agree the Regulations should be amended to take account of a scheme employer's exposure to risk when calculating an exit credit.

**Question 17: Are there other factors that should be taken into account in considering a solution?**

Our concerns around exit credits go beyond contractors with risk sharing agreements. The use of pass through and risk sharing agreements has grown in prominence, however, there are still a significant number of former transferee admission bodies where risk sharing does not apply. The funding strategy of these employers, from the allocation of assets to cover past service liabilities at their date of joining to their ongoing contributions and bond requirements, were predicated by the Regulations and Funding Strategy Statements that were in force at the time they joined (and any subsequent formal valuations). The introduction of exit credits effectively changed the risk these employers posed to ceding authorities which would have may have resulted in significantly different treatment throughout their time in the LGPS. As a result, we strongly believe that exit credits should not be applied retrospectively to any contracts that were in force prior to 14 May 2018, whether on a risk-sharing basis or otherwise. In other words, the exit credit regime should only apply to new contracts that were set up from 14 May 2018 onwards.

There are wide ranges of risk sharing agreements in existence in the LGPS, many of which may be made without the knowledge of administering authorities. The requirement for the administering authority to be satisfied the provider has not borne any risk is an extremely high hurdle given the nature of these arrangements (i.e. would an arrangement where the guarantor takes on all the pension risks with the exception of say excessive pay increases fail this test, even if pay awards were sensible?). Putting the onus on the administering authority to carry out this additional function may significantly increase costs (either through external consultancy or internal time of officers) as agreements are likely to be legal agreements that may need professional interpretation. The risk of challenge of any decisions would be material.

The 3 month timeframe on which to pay an exit credit remains overly onerous and will be exacerbated by this change. We would expect administering authorities to make a determination on whether the service provider has not borne any risk prior to instructing an exit valuation. It is questionable, especially where interpreting potentially complex legal agreements that this could be done within 3 months. In addition, if further flexibilities are added to manage exit debts, you could face a situation where you have to return a surplus within 3 months of an exit date, but deficits may not be recovered for a number of years. Therefore, we believe the 3 month limit on exit credits is asymmetric in favour of employers and consideration should be given as to whether it remains appropriate.

**Section 5- Employers required to offer LGPS membership**

**Question 18: Do you agree with our proposed approach?**

It is a policy decision to allow higher and further education bodies to close to new entrants. We are aware that some bodies are struggling to meet the cost of participating in the LGPS, and recent changes in the sector (as outlined in the consultation) do raise questions about their ongoing treatment as ‘scheduled bodies’ under the Regulations.

It is not uncommon for the LGPS liabilities of these bodies to be worth tens of millions of pounds. We expect funds to keep in close touch with these employers and regularly monitor their financial strength, and wherever possible seek security to reduce the risk of unpaid liabilities falling on other employers in the event of insolvency. Those bodies that close to new entrants may well see their pension costs increase in the short term as exit funding strategies are agreed between funds and employers. The extent to which total employer pension costs in the medium to longer term rise or fall will depend on the type of pension arrangement that employers put in place for new entrants to replace the LGPS.

Employers that use this proposal would create a two-tier work force in terms of pension's provision. There will be a need to monitor and ensure that promises are kept to those members currently in the LGPS i.e. that they are not induced out of the LGPS. The accompanying legislation should make it clear where that responsibility lies and the possible penalties for non-compliance.

Employers should also be aware that choosing this approach may not immediately reduce their pension costs. Indeed contributions may even increase in the short term, as administering authorities are likely to want to recalculate the employer contribution rate, allowing for the fact the employer is now closed to new entrants and potentially altering the funding basis to reflect the shorter term nature of the participation of the employer.

**Section 6 – Public sector equality duty**

**Question 19: Are you aware of any other equalities impacts or of any particular groups with protected characteristics who would be disadvantaged by the proposals contained in this consultation?**

We would agree that in relation to sections 1 to 4 of the consultation document there should be no equality issues to consider, given that member benefits and contributions would not be impacted by any eventual outcome from this consultation exercise. We assume that the current safeguards in relation to ongoing entitlement to member benefits would not be impacted on any relaxation of recovery of exit payments (i.e. it would fall to the Fund to make payment of benefits where it has not been possible to recover some or all of an exit payment and the remaining liability is spread across remaining employers with active members).

In relation to section 5 the consultation document refers to the fact that "It will be up to each institution to consider the potential equalities impacts when making their decision on which, if any, new employees should be given access to the scheme." Our concern would be whether such institutions may seek to offer inducements to existing active scheme members to opt to leave the scheme in order to accelerate their departure from the scheme as a whole. Appreciating that such action would be unlawful and counter to the requirements of automatic enrolment provisions there is a risk that such actions could be taken, disadvantaging existing active members.

I trust that these comments are helpful and would be happy to expand on or clarify any aspect if required.

**ESPF Pension Board and Pension Committee**

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