

## Public Sector Outsourcing Update

2 February 2012

### Government agrees to retain Fair Deal policy with some important modifications – what are the consequences?

The Government announced in December that it had reached agreement in principle with most public sector unions on the future structure of the main public sector pension schemes. The new schemes are to be career average, with varying accrual rates and rates of revaluation of benefits for active members. The important principle of tying normal pension age to State Pension Age has been agreed.

More information on the terms of the agreement is given on page 3 of this Update. Many details however remain to be finalised through negotiation with the unions and, since then, a number of unions have announced that they do not agree with the proposals and are refusing to participate in the final negotiations, with further strike action being possible.

#### Fair Deal policy review

In the announcement, Danny Alexander also said that the deal the Government has reached on public sector pensions means that it can retain the Fair Deal policy, which requires TUPE-transferred public sector employees to be provided with broadly comparable pensions by their new employer.

But the Government is proposing some important modifications. In particular, it says it will open up more public sector schemes to continued participation by former public sector employees who have transferred under outsourcing contracts. And, he said, it will no longer require *“private, voluntary and social enterprise providers to take on the risks of defined benefit that deter many from bidding for contracts in the first place”*.

Details on how this will work in practice will be announced later this year, when the Government responds formally following the consultation on the Fair Deal policy it carried out last year. As the intention is to encourage more private and third sector organisations to participate in outsourcing contracts, we expect the solution will include arrangements similar to the admission body agreements that already operate in the Local Government Pension Scheme (LGPS), with a considerable degree of risk retained by the public sector. Such changes are likely to require primary legislation and, therefore, it is likely that they will take some time to come into effect.

The Government says it intends to retain the Fair Deal policy, but with changes that reduce the risks for contractors

The Government is to consider practical options to reform the terms of access to public sector schemes such as the NHSPS which do not currently offer this option

### GAD passports

While the discussions continue, the Government Actuary's Department (GAD) is carrying on business as usual in its role in overseeing and operating the Fair Deal policy, in particular with its requirements to certify a contractor's pension scheme as satisfying the "broadly comparable" provisions of the Fair Deal.

In one small concession, however, GAD has announced that contractors with existing NHS, Civil Service or Teachers pension scheme passports may in some circumstances incorporate the increased April 2012 member contribution rates (announced in the middle of December) by requesting a simple addendum. Note that this change will only apply for employees transferring after April 2012. If the contractor wants to change contribution rates for existing members of a broadly comparable scheme, it will need to go through a separate employee consultation process. These arrangements will also not deal with the longer-term member contribution increases being discussed as part of the current reforms.

Existing GAD passports are not being withdrawn – and can be amended to incorporate the new employee contribution rates from April 2012

### Comment

LCP welcomes the tone of the Government's announcement about the Fair Deal. However, we remain concerned that the statements lack clarity on how defined benefit risks will be shared between the public sector pension plan and the contractor. Unless there is a realistic retention of risk by the public sector, there is the danger that the new arrangements will not prove attractive to those potential outsourcers who are currently reluctant to bid for outsourcing contracts.

It is not clear when the Government will provide its formal response to the Fair Deal consultation. The timing may well depend on how quickly it is able to progress the negotiations with the unions in finalising the details of the public sector pension scheme reforms. We await further developments with interest.

### Key actions:

- § Contractors with existing NHS, Civil Service or Teachers scheme passports - consider applying to GAD for an addendum to be added to existing passport to reflect future changes in member contributions from April 2012, if you expect to use your existing scheme for new contracts.
- § Contractors bidding for new contracts – when pricing your bids, consider carefully how the impending changes to the public sector pension schemes and the Fair Deal may impact on the pensions costs and risks for the outsourced business.
- § Future planning for all organisations – consider if public sector outsourcing could become a more viable option in future, given the proposals for allowing transferred staff to stay in their existing public sector schemes.

### Public sector pensions reform

More details about the announced changes to the public sector schemes are as follows:

- § The new schemes for the NHS, Civil Service and Teachers will come into effect in April 2015, as originally planned, with phased implementation of increased member contributions starting in April 2012.
- § The member contribution increases in April 2012 will depend on the employees' rates of pay.
  - § For the NHS, there will be no increase for employees earning less than £26,558, with increases of 1.5% or 2.4% for employees on higher earnings.
  - § For the Civil Service and Teachers schemes, there will be no increase for employees earning less than £15,000, with increases of between 0.6% and 2.4% for employees on higher earnings.
- § An important concession made by the Government towards the end of the initial negotiations was that scheme members who are within 10 years of current pension age will see no change in when they can retire, and no decrease in the pension they will receive at normal pension age.
- § The Government has agreed a revised timetable for changes to the Local Government Pension Scheme (LGPS), under which both the changes to benefit structure and to member contribution rates implemented simultaneously in April 2014. The increases to member contributions for all, or the large majority, of members are likely to be low or zero – and there will be no changes in April 2012.

The new NHS, Civil Service and Teacher schemes will start in 2015, with member contribution increases phased in from 2012

For the LGPS, all the changes will come in together in April 2014

This update is a supplement to LCP's Public Sector Outsourcing Report 2011, published in November 2011, and available at: <http://www.lcp.uk.com/psogreport2011>

This Update outlines legal, technical and professional developments that may be of interest to you as a pensions professional. This Update should not be relied upon for detailed advice or taken as an authoritative statement of the law. For further help, please contact Bart Huby or Tim Sharples at our Winchester office or the partner who normally advises you.

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