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West Midlands Pension Fund

Employers' Briefing Note

Consultation on a Public Sector Exit Payment Cap - closes 27 August

HM Treasury has recently launched a short consultation on capping exit payments to employees leaving the public sector. The proposal is likely to impact future workforce re-structuring exercises - affected employers should consider responding directly by 27 August.

Headline proposal - £95,000 cap on exit payments

The proposed cap would include the cost of providing early access to unreduced pension benefits. LGPS members over age 55 currently have an entitlement to early access unreduced benefits when they are made redundant or leave on grounds of business efficiency.

The consultation suggests that members would still be given the option of early access to unreduced benefits but only to the extent they can be provided within the proposed total cost cap of £95,000. In practice, changes would need to be made to the regulations governing the LGPS to facilitate this, and the consultation also notes that the Government is, in any event, considering further reforms to employer-funded early retirement promises.

It is unclear at this stage exactly how the cap (which would capture both cash sum redundancy payments and the additional cost to employers of early pension payments) will work in practice and how members' pension benefits will be affected. The timing of the consultation does, however, indicate it is something the Government would like to establish as soon as possible – the cap could apply as early as April 2016.

Who is affected?

The cap is intended to apply to central and local government bodies (including district councils, arms-length council operations (ALMOs) and academies). It is not expected to apply to other employers (eg, colleges, universities, charities, community admission bodies) but there is some uncertainty, particularly around the extent it could be applied to contractors and TUPE-protected rights. Even where it does not apply directly, employers are expected to set their own exit cap mechanism.

It will be possible to "waive" the cap in exceptional circumstances, but details of exit payments and any wavers will need to be published annually. Details of the waiver process are limited but, as a default, it is expected that waiver would require Full Council approval.

Fund early retirement strain costs

Recent Fund experience is similar to the LGPS as a whole.

- Over the last four years, the Fund has paid unreduced early retirement pensions to just over 2,350 members.
- The total funding strain associated with these pensions and charged to employers was £8.5 million.
- In around 3% of cases, the pension strain cost alone would have exceeded the proposed cap, with costs in these cases making up around 15% of the total funding costs.

What the proposed cap could mean for pension benefits

Pension benefits of older, longer serving staff (and not necessarily just those on the highest pay) are likely to be restricted if the cap is implemented at the level proposed.

For example (as a rough guide based on illustrative figures provided to the Fund and allowing for an element of redundancy payment equal to the current maximum statutory redundancy pay of £14,250), the following members' pension options could be restricted by the cap in the event they are offered exit benefits including retirement benefits paid ten years' early:

- 20 years' service and final pay above £45,000; or
- 40 years' service and final pay above £25,000.

If benefits are paid five years' early, the cap would impact members on broadly double the level of pay (eg, a member with 20 years' service and final pay of £90,000). Please note that the impact on individual members will vary considerably based on their individual circumstances.

There is likely to be some uncertainty on the level of benefits members will be able to draw from the Fund as it will depend on other elements of the exit package. It is unclear how the LGPS regulations could be changed to facilitate the cap (and interaction between the various exit payments) or how retirement benefit costs should be measured to ensure consistency between funds and the LGPS and other public sector schemes. For the Fund, the administrative burden could increase substantially.

Wider implications for employers

We anticipate the introduction of the cap could have much wider HR implications. At a time when councils are looking to identify and implement cost-saving initiatives, a valuable tool, historically used to facilitate headcount reduction, will be restricted. This could lead to sub-optimal workforce restructuring and undermine longer term succession planning.

In our view, the cap could prove to be counter-productive with the potential for an unintended impact on recruitment and retention in the future.

Responding to the consultation

The consultation closes on 27 August. Details of how you can respond on the pension and wider implications can be found on page 5 of the consultation.

The Fund would prefer pension cost control to be driven by changes to the LGPS benefit regulations. This would avoid the additional administrative burden and complexity of operating the cap (including an estimated value of pension benefits) across multiple sources of exit payment. It would also give members greater clarity of their pension benefits and avoid the potential disconnect between emerging benefit entitlements and payments to the Fund to meet the cost.

Please let us know if there is any further information you would like from the Fund to assist your consideration and response as a participating employer. As an LGPS fund, we are sharing our views on the pension aspects with the LGA, who are preparing a response on behalf of the local government sector.

Further Information Available to Employers and Members

Further information can be found on the Fund's website at wmpfonline.com

The website can also be used to provide information to members or as signposting for them to access information about the new scheme.

We always welcome feedback on our services, if you would like to make any further suggestions for improvement, please email:

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