

Scottish Borders Council Pension Fund

Policy on cessations

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Next review	

1 Introduction

The purpose of this policy is to set out the administering authority's approach to dealing with circumstances where a scheme employer leaves the fund and becomes an exiting employer (a cessation event).

It should be noted that this policy is not exhaustive. Each cessation will be treated on a case-by-case basis, however certain principles will apply as governed by the regulatory framework and the fund's discretionary policies (see below).

1.1 Aims and Objectives

The administering authority's aims and objectives related to this policy are as follows:

- To confirm the approach for the treatment and valuation of liabilities for employers leaving the fund.
- To provide information about how the fund may apply its discretionary powers when managing employer cessations.
- To outline the responsibilities of (and flexibilities for) exiting employers, the administering authority, the actuary and, where relevant, the original ceding scheme employer (usually a letting authority).

1.2 Background

As described in the Funding Strategy Statement (FSS), a scheme employer may become an exiting employer when a cessation event is triggered e.g. when the last active member stops participating in the fund. On cessation from the fund, the administering authority will instruct the fund actuary to carry out a valuation of assets and liabilities for the exiting employer to determine whether a deficit or surplus exists. The fund has full discretion over the repayment terms of any deficit, however is liable for any surplus through the payment of an exit credit.

1.3 Guidance and regulatory framework

The Local Government Pension Scheme (Scotland) Regulations 2018 contain relevant provisions regarding employers leaving the fund ([Regulation 61](#)) and include the following:

- Regulation 61 (2) – this regulation states that, where an employing authority ceases to be a scheme employer, the administering authority is required to obtain an actuarial valuation of the liabilities of current and former employees as at the termination date. Further, it requires the Rates & Adjustments Certificate to be amended to show the revised contributions due from, or the exit credit payable to, the exiting employer.
- Regulation 61 (3) – the administering authority, at its discretion, may issue a suspension notice to suspend payment of an exit amount for up to three years, where it reasonably believes the exiting employer is to have one or more active members contributing to the fund within the period specified in the suspension notice.

- Regulation 61 (4B-4G) – the administering authority may enter into a written deferred debt agreement, allowing the employer to have deferred employer status and to delay crystallisation of debt despite having no active members.
- Regulation 61 (5) – in instances where it is not possible to obtain additional contributions from the employer leaving the fund or from the bond/indemnity or guarantor, the contribution rate(s) for the appropriate scheme employer or remaining fund employers may be amended.
- Regulation 61 (6) – where it is believed a scheme employer may cease at some point in the future, the administering authority may obtain a certificate from the fund actuary revising the contributions for that employer, with a view to ensuring that the assets are expected to be broadly equivalent to the exit payment that will be due.
- Regulation 61 (7) – following the payment of an exit payment to/from the fund, no further payments are due to the fund from the exiting employer.
- Regulation 61B (1) – the administering authority may set out a policy on spreading exit payments.

In addition to the 2018 Regulations summarised above, [Regulation 25A](#) of the Local Government Pension Scheme (Transitional Provisions and Savings) (Scotland) Regulations 2014 (“the Transitional Regulations”) give the fund the ability to levy a cessation debt on employers who have ceased participation in the fund (under the previous regulations) but for whom a cessation valuation was not carried out at the time. This policy document describes how the fund expects to deal with any such cases.

These regulations relate to all employers in the fund.

2 Statement of Principles

This Statement of Principles covers the fund’s approach to exiting employers. Each case will be treated on its own merits but in general:

- it is the fund’s policy that the determination of any surplus or deficit on exit should aim to minimise, as far as is practicable, the risk that the remaining, unconnected employers in the fund have to make contributions in future towards meeting the past service liabilities of current and former employees of employers leaving the fund.
- the fund’s preferred approach is to request the full payment of any exit debt (an exit payment), which is calculated by the actuary on the appropriate basis (as per the FSS and Section 3.1 below). This would extinguish any liability to the fund by the exiting employer.
- the fund’s key objective is to protect the interests of the fund, which is aligned to protecting the interests of the remaining employers who are ultimately responsible for meeting any additional costs arising in respect of the pension obligations of ceased employers. A secondary objective is to consider the circumstances of the exiting employer in determining arrangements for the recovery of any cessation debt.

3 Policies

On cessation, the administering authority will instruct the fund actuary to carry out a cessation valuation to determine whether there is any deficit or surplus as defined in the FSS.

Where there is a deficit, payment of this amount in full would normally be sought from the exiting employer. The fund's normal policy is that this cessation debt is paid in full in a single lump sum within 28 days of the employer being notified.

However, the fund will consider written requests from employers to spread the payment over an agreed period, in the exceptional circumstance where payment of the debt in a single immediate lump sum could be shown by the employer to be materially detrimental to the employer's financial situation (see [3.2 Repayment flexibility on exit payments](#) below).

In circumstances where there is a surplus, the administering authority will determine the amount of exit credit to be paid to the exiting employer in line with the Regulations.

3.1 Approach to cessation calculations

Cessation valuations are carried out on a case-by-case basis at the sole discretion of the fund depending on the exiting employer's circumstances. However, in general the following broad principles and assumptions may apply, as summarised below:

Type of employer	Cessation exit basis	Responsible parties for unpaid or future deficit emerging
Local Authority	Low risk basis ¹	Shared between other fund employers
College	Low risk basis ¹	Shared between other fund employers
Admission bodies ("TABs" – typically contractors)	Ongoing basis ²	Letting authority (where applicable), otherwise shared between other fund employers
Admission bodies ("CABs" – typically any ABs other than contractors)	Low risk basis	Shared between other fund employers (if no guarantor exists)

¹Cessation is assumed not to be generally possible, as Scheduled Bodies are legally obliged to participate in the LGPS. In the rare event of cessation occurring (e.g. machinery of Government changes), these cessation principles would apply.

²Where a TAB has taken, in the view of the administering authority, action that has been deliberately designed to bring about a cessation event (e.g. stopping future accrual of LGPS benefits), then the cessation valuation will be carried out on a low-risk basis.

Risk-based cessation approach

The fund uses a risk-based approach to set employer funding strategies, including within cessation calculations. In particular, the likelihood of the fund's assets achieving particular future investment returns is analysed.

Where appropriate, the fund will use this approach to set an upper and lower amount (or "corridor") for the amount of assets a ceasing employer must leave behind to pay for its members' benefits.

Under this approach, if an employer's asset value in the Fund at the cessation valuation is:

- Within the corridor (which is calculated as part of the cessation valuation), then there is no cessation debt due from the employer or cessation surplus payable to the employer.
- Lower than the corridor, then a cessation debt will be due from the employer.
- Higher than the corridor, then a cessation surplus may be payable to the employer (the surplus will be included in the Fund's considerations when determining if an exit credit is payable).

The upper bound of the corridor is defined as the assets required to meet liabilities, where the liabilities have been calculated using a future investment return assumption that is expected to be achieved in 95% of outcomes over the next 20 years (based on the Fund's investment strategy at the calculation date).

The lower bound of the corridor is defined as the assets required to meet liabilities, where the liabilities have been calculated using a future investment return assumption that is expected to be achieved in 85% of outcomes over the next 20 years (based on the Fund's investment strategy at the calculation date).

The Fund reserves the right to review the definition of the corridor as part of any review of this policy.

3.2 Repayment flexibility on exit payments

Deferred spreading arrangement (DSA)

The fund will consider written requests from exiting employers to spread an exit payment over an agreed period, in the exceptional circumstance where payment of the debt in a single immediate lump sum could be shown by the employer to be materially detrimental to the employer's financial situation.

In this exceptional case, the fund's policy is:

- The agreed spread period is no more than three years, but the fund could use its discretion to extend this period in extreme circumstances.
- The fund may consider factors such as the size of the exit payment and the financial covenant of the exiting employer in determining an appropriate spreading period.
- The exiting employer may be asked to provide the administering authority with relevant financial information such as a copy of its latest accounts, sources of funding, budget forecasts, credit rating (if any) etc. to help in this determination.
- Payments due under the DSA may be subject to an interest charge.
- The fund will only consider written requests within three months of the employer exiting the fund. The exiting employer would be required to provide the fund with detailed financial information to support its request.
- The fund would take into account the amount of any security offered and seek actuarial, covenant and legal advice in all cases.
- The fund proposes a legal document, setting out the terms of the exit payment agreement, to be prepared by the fund and signed by all relevant parties prior to the payment agreement commencing.
- The terms of the legal document should include reference to the spreading period, the annual payments due, interest rates applicable, other costs payable and the responsibilities of the exiting employer during the exit spreading period.

- Any breach of the agreed payment plan would require payment of the outstanding cessation amount immediately.
- Where appropriate, cases may be referred to the Pensions Committee for consideration and considered on its individual merit. Decisions may be made by the Chair in consultation with officers if an urgent decision is required between Committee meetings.

Deferred debt agreement (DDA)

The fund's preferred policy is for the spreading of payments, as detailed above, to be followed in the exceptional circumstances where an exiting employer is unable to pay the required cessation payment as a lump sum in full. However, the fund may exercise its discretion to set up a deferred debt agreement as described in [Regulation 61 \(4B\)](#).

The employer must meet all requirements on Scheme employers and pay the secondary rate of contributions as determined by the fund actuary until the termination of the DDA.

The administering authority may consider a DDA in the following circumstances:

- The employer requests the fund consider a DDA.
- The employer is expected to have a deficit if a cessation valuation was carried out.
- The employer is expected to be a going concern.
- The covenant of the employer is considered sufficient by the administering authority.

The administering authority will normally require:

- A legal document to be prepared, setting out the terms of the DDA and signed by all relevant parties prior to the arrangement commencing. (including details of the time period of the DDA, the annual payments due, the frequency of review and the responsibilities of the employer during the period).
- Relevant financial information for the employer such as a copy of its latest accounts, sources of funding, budget forecasts, credit rating (if any) to support its covenant assessment.
- Security be put in place covering the employer's deficit on their cessation basis and the fund will seek actuarial, covenant and legal advice in all cases.
- Regular monitoring of the contribution requirements and security requirements
- All costs of the arrangement are met by the employer, such as the cost of advice to the fund, ongoing monitoring or the arrangement and correspondence on any ongoing contribution and security requirements.

A DDA will normally terminate on the first date on which one of the following events occurs:

- The employer enrolls new active fund members.
- The period specified, or as varied, under the DDA elapses.
- The take-over, amalgamation, insolvency, winding up or liquidation of the employer.
- The administering authority serves a notice on the employer that the administering authority is reasonably satisfied that the employer's ability to meet the contributions payable under the DDA has weakened materially or is likely to weaken materially in the next 12 months.

- The fund actuary assesses that the employer has paid sufficient secondary contributions to cover all (or almost all) of the exit payment due if the employer becomes an exiting employer on the calculation date (i.e. employer is now largely fully funded on their low risk basis).
- The fund actuary assesses that the employer's value of liabilities has fallen below an agreed *de minimis* level and the employer becomes an exiting employer on the calculation date.
- The employer requests early termination of the agreement and settles the exit payment in full as calculated by the fund actuary on the calculation date (i.e. the employer pays their outstanding cessation debt on their cessation basis).

On the termination of a DDA, the employer will become an exiting employer and a cessation valuation will be completed in line with this policy.

4 Practicalities and process

4.1 Responsibilities of ceasing employers

An employer which is aware that its participation in the fund is likely to come to an end must:

- advise the fund, in writing, of the likely ending of its participation (either within the terms of the admission agreement in respect of an admission body (typically a 3 month notice period is required) or otherwise as required by the Regulations for all other scheme employers). It should be noted that this includes closed employers where the last employee member is leaving (whether due to retirement, death or otherwise leaving employment).
- provide any relevant information on the reason for leaving the fund and, where appropriate, contact information in the case of a take-over, merger or insolvency.
- provide all other information and data requirements as requested by the administering authority which are relevant, including in particular any changes to the membership which could affect the liabilities (e.g. salary increases and early retirements) and an indication of what will happen to current employee members on cessation (e.g. will they transfer to another fund employer, will they cease to accrue benefits within the fund, etc.).
- meet the cost of all fees and charges incurred by the Fund in the course of cessation including, but not limited to, the cost to obtain the cessation valuation report from the Fund Actuary and the cost of implementing a flexible repayment option (as set out in section 3.2).

4.2 Responsibilities of administering authority

The administering authority will:

- gather information as required, including, but not limited to, the following:
 - details of the cessation - the reason the employer is leaving the fund (i.e. end of contract, insolvency, merger, machinery of government changes, etc.) and any supporting documentation that may have an effect on the cessation.
 - complete membership data for the outgoing employer and identify changes since the previous formal valuation.
 - the likely outcome for any remaining employee members (e.g. will they be transferred to a new employer, or will they cease to accrue liabilities in the fund).
- identify the party that will be responsible for the employer's deficit on cessation (i.e. the employer itself, an insurance company, a receiver, another fund employer, guarantor, etc.).
- commission the fund actuary to carry out a cessation valuation under the appropriate regulation.
- where applicable, discuss with the employer the possibility of paying adjusted contribution rates that target a 100% funding level by the date of cessation through increased contributions in the case of a deficit on the cessation basis or reduced contributions in respect of a surplus.
- where applicable, liaise with the original ceding employer or guarantor and ensure it is aware of its responsibilities, in particular for any residual liabilities or risk associated with the outgoing employer's membership.

- having taken actuarial advice, notify the employer and other relevant parties in writing of the payment required in respect of any deficit on cessation and pursue payment.

4.3 Responsibilities of the actuary

Following commission of a cessation valuation by the administering authority, the fund actuary will:

- calculate the surplus or deficit attributable to the outgoing employer on an appropriate basis, taking into account the principles set out in this policy, including (where appropriate) the corridor amounts.
- provide actuarial advice to the administering authority on how any cessation deficit should be recovered, giving consideration to the circumstances of the employer and any information collected to date in respect to the cessation.
- where appropriate, advise on the implications of the employer leaving on the remaining fund employers, including any residual effects to be considered as part of triennial valuations.