

*H M Treasury June  
1999*

**STAFF TRANSFERS FROM CENTRAL GOVERNMENT:  
A FAIR DEAL FOR STAFF PENSIONS**

*Guidance to Departments and Agencies*

**Introduction**

1. This paper sets out in general terms how pensions issues are to be handled in future when staff from central government Departments and Agencies are transferred to a new employer as part of a business transfer. The new approach set out here builds upon earlier guidance, and extends and strengthens its application in order to ensure that staff are treated fairly. It is mainly concerned with transfers between the Government and the private sector when contracts are awarded under public-private partnership (PPP) deals.

2. *Better Quality Services* gives guidance on the treatment of staff pensions in PFI and PPP deals, and there are also policy statements and guidance issued by the Treasury Task Force covering, for instance, the Government's continuing commitment to dialogue with staff and other interested parties about the way in which PPP projects are managed.

3. This new guidance should be reflected in procurement practice as soon as is practicable without disruption to projects which are already at an advanced stage. Detailed guidance will be issued to contracting authorities later this year.

**Background**

4. Pensions are often an important element in the overall remuneration of staff, particularly within the public services where there are occupational pension schemes offering a high quality of benefits. Sometimes public service schemes require very low employee contributions to earn pension benefits, such as in the Principal Civil Service Pension Scheme (PCSPS) where employee contributions are set at only 1½% of pay, and in these cases employee pay is somewhat lower than it would otherwise be, to reflect the value of the pension scheme.

5. If appropriate arrangements were not made for staff pensions as part of business transfers, the result could be disadvantageous to public service staff who were transferring to the new employer. Not only are pension arrangements an important subject, but they are complex and likely to cause confusion and apprehension if not handled openly and consistently by the contracting authority. It is not in the interests of the contracting authority, or the new employer, or the taxpayer, for staff to be alarmed about the prospects for their pensions in a business transfer which depends upon staff motivation for delivery of good quality public services.

6. Occupational pensions are not covered by the Transfer of Undertaking (Protection of Employment) Regulations 1981 (the TUPE regulations). The new EU Acquired Rights Directive 12 gives Member States the option of including occupational pensions within the terms which are protected by national legislation when an undertaking transfers between employers, and the Government is reviewing whether and if so, how, to include pensions within new TUPE regulations.

7. Independently of the TUPE review, and without prejudice to its conclusions, this paper sets out the standard practices which the Government will follow when its own staff are transferred to other employers. Contracting authorities in other parts of the public sector will continue to make their own arrangements consistent with the law and good employment practice. It would be welcome if they adopted approaches comparable to those set out here. Separate consideration is being given to staff transfers from local government.

8. The principles which Government will apply as a contracting authority in relation to the pensions of transferring staff are:-

- to treat staff fairly;
- to do so openly and transparently;
- to involve staff and their representatives fully in consultation about the process and its results; and
- to have clear accountability within Government for the results.

9. There are two separate but related aspects to treatment of pensions in a business transfer:-

- first, staff should continue to have access after the transfer to a good quality occupational pension scheme under which they can continue to earn pension benefits through their **future service**;
- second, staff should be given options for the handling of the **accrued benefits** which they have already earned.

Each of these aspects is discussed, in turn, in the following sections.

### **FUTURE SERVICE**

10. The focus of this guidance is upon those cases, likely to be in the majority, where a business transfer means that staff have to be 'early leavers' of the occupational pension scheme associated with their former employment. The Government has no plans to seek amendment to the Superannuation Act 1972 to broaden the categories of employees eligible for membership of the PCSPS. Where Civil Servants transfer to private sector employment they will therefore cease to be eligible for PCSPS membership, and their ability to earn further occupational pension benefits through future service will depend upon the occupational pension arrangements offered by the new employer.

11. Not all private sector employers offer occupational pension schemes which are as valuable to employees as the public service schemes, and where good quality pension schemes are offered they typically differ in major respects: for instance, the age of normal retirement, the rate of accrual of pension entitlements, provision of a lump sum on retirement, the degree of indexation of pensions increases, and so on. If care were not taken over staff pensions, the unintended upshot of a business transfer might be a detriment to staff pension benefits.

12. The terms of the business transfer should specifically protect staff pensions. The arrangements made to achieve this need to be considered within the overall context of the business transfer negotiations between the contracting authority and prospective private sector partners and should not be so cumbersome or expensive to administer as to militate against finding a justifiable business solution.

13. To require that the new employer should offer transferring staff access to a pension scheme which is in all respects identical to the public service scheme which they are leaving would be unduly restrictive. It would add to administrative costs and it could hamper harmonisation of terms and conditions. In the case of the PCSPS it would be an unrealistic requirement, because a non-statutory scheme which was identical to the PCSPS would not qualify for tax exemption. A requirement for an identical scheme would also prevent employers from offering different benefit packages, more in line with private sector standards, which might overall be of greater value to many transferring employees.

14. The guiding principle should be that the new employer offers transferring staff membership of a pension scheme which though not identical is '**broadly comparable**' to the public service pension scheme which they are leaving. To satisfy the criteria for broad comparability there must be a rigorous scrutiny of the alternative pension arrangements by a professionally qualified actuary which compares the alternative scheme with the public service scheme in detail. A broadly comparable scheme will be one which, in the professional opinion of the actuary, satisfies the condition that there are no identifiable employees who will suffer material detriment overall in terms of their future accrual of pension benefits under the alternative scheme. The PCSPS takes actuarial advice from the Government Actuary's Department, as do a number of other public service pension schemes.

15. There may be cases where although there are no identifiable classes of employee who would be materially worse off overall, transfer to the new scheme might be materially detrimental to a few individuals. In such cases it will be a matter of judgement whether the new scheme should be adjusted, or whether it would be better simply to make appropriate compensation arrangements to protect the disadvantaged individual(s).

16. Each case should be considered on its merits. There may be exceptional circumstances where there are special reasons for not providing a broadly comparable pension scheme. The strength of those reasons should be tested rigorously and it would then be necessary for the terms of the business transfer to ensure appropriate compensation for all the staff. Actuarial advice should be taken by the contracting authority on the calculation of any compensation in these exceptional circumstances if

a broadly comparable scheme is not to be provided, or if there are identified individuals who would be materially worse off overall in the new scheme. In all cases the preference should be for the new employer to offer transferring staff membership of a broadly comparable scheme, and this should be a contract condition in the procurement. Only in exceptional circumstances should the combination of pension arrangements which are less than broadly comparable plus appropriate compensation for employees be accepted.

17. This principle is already being followed by the Government. Its practical application will now be strengthened, extended and made more open:-

- (i) for transfers of staff from Government Departments and Agencies it will continue to be a requirement for the Government Actuary's Department (GAD) to certify the broad comparability of specified alternative pension arrangements before any contractual commitment is made;
- (ii) if for exceptional reasons the requirement for broad comparability is to be waived, GAD advice on appropriate compensation to staff must be followed;
- (iii) GAD will follow a published Statement of Practice in certifying broad comparability (attached). This sets out clearly the principles which are already being followed. Publishing these principles in the form of this Statement for the first time will increase transparency and accountability;
- (iv) GAD will provide to the contracting authority an analysis of the key differences between the alternative pension scheme and the public service scheme, and the ways in which the differences balance out overall to satisfy the condition of no material detriment overall, by reference to the different groups of employees identified in the staff to be transferred;
- (v) the full GAD analysis will be made available to trades unions and staff representatives, and GAD will respond to any queries or observations which staff representatives have. A reasonable period will be allowed by the contracting authority for discussion, if requested, of any points arising from the GAD analysis;
- (vi) at the conclusion of this period, if any points of concern about the suitability of the proposed alternative pension arrangements remain which cannot be settled by discussion between staff representatives and the contracting authority, staff representatives may raise their concerns directly with a nominated Minister responsible for the affairs of the Department or Agency;
- (vii) no contractual commitments will be made whilst this process of review and consultation is underway, but a reasonable time limit may be set by the contracting authority;
- (viii) the contract for the business transfer must specifically require the implementation of the alternative pension arrangements which have been accepted.

18. In practice this will mean that in order to avoid delay or having to retrace steps, contracting authorities will need to be satisfied about the broad comparability of alternative pension arrangements well in advance of moving a procurement to selection of short-listed bidders or a preferred bidder. Bidders will need to provide GAD with detailed specifications of their proposed pension arrangements in good

time to allow the analysis required and, if necessary, subsequent discussion of it with staff representatives. Contracting authorities will have to reflect this in their procurement logistics. There can be no proper evaluation of options for public-private partnership without a full analysis of the future staff pension arrangements.

19. Ministers will not authorise a procurement contract, and contractual commitments should not be made under delegated powers, if the conditions set out in paragraph 17 (above) have not been satisfied. This provides a guarantee to staff that the process of identifying acceptable alternative pension arrangements will be fair and open and carried out in full consultation with their representatives.

### **Subsequent transfers of staff**

20. Current practice restricts the contracting authority's concern about broad comparability to transfers from Government to another employer. Once staff have transferred to a new employer, they may be involved in subsequent business transfers. As a contracting authority, the Government will usually not be involved directly as a party to those arrangements. A contracting authority cannot take responsibility for the treatment of its former staff throughout the remainder of their working lives. But a contracting authority does take an interest in the conduct of business transfers which occur as the direct consequence of actions which it takes as a contracting authority.

21. Therefore:-

- (i) where a contract for services is terminated and the work is given to another contractor, the contracting authority will require that pension arrangements are made for staff transferring from the first contractor to the second contractor which would at least be broadly comparable with the public service pension scheme which those staff were in originally. The requirement will be limited to staff originally transferred from the contracting authority, although employers may find it convenient to harmonise terms and conditions in the workforce; and
- (ii) where a primary contractor under a Government contract transfers staff whose work is integral to performance of the contract to a sub-contractor in consequence of the terms of the primary contractor's obligations to the Government, it should be a condition of that subcontracting that broadly comparable pension arrangements are made for the transferring staff who were originally in the employ of the contracting authority.

## ACCRUED BENEFITS

22. The treatment in procurement practice of the accrued pension benefits of transferring staff is more complex, but raises issues of equal importance. Regulations applicable to pension schemes require 'early leavers' to be given the option of 'preserving' their accrued benefits in the pension scheme which they are leaving, or transferring them to another pension arrangement. In the former case (preservation), the early leavers become 'deferred pensioners' of the scheme which they are leaving. The value of their benefits in that scheme will be uprated by price inflation until they come into payment at normal retirement age. This option may often be preferred by staff, especially those who are closer to retirement and do not expect significant future real earnings growth. In the latter case, where accrued benefits are transferred, the transferor scheme makes a transfer payment to the transferee scheme which extinguishes its liability to the early leaver; in return the new employer's scheme awards a past service credit to the individual. (If the transfer were made to a personal pension plan instead, it would be invested in the normal way.)

23. Regulations stipulate a basis for calculating a minimum transfer value where accrued credits are transferred. Typically this will not result in individuals securing full credits in the new employer's scheme in relation to the credits they are surrendering in the transferor scheme, unless there is a specific agreement between the two pension schemes that they should do so. Typically there is then a different basis for calculation of the transfer value involving the transferor scheme in making higher transfer payments. Such agreements between pension schemes are called '**bulk transfer agreements**' (although they may in fact cover only a few members of staff, or just one). A bulk transfer agreement specifies the basis for calculating the transfer payment and the size of the transfer credits it will secure.

24. It is desirable where staff are obliged by a transfer of undertaking to be early leavers of a public service pension scheme for there to be bulk transfer agreements covering the award of past service credits by the new employer's pension scheme. Current practice, as set out in *Better Quality Services* is to treat the absence of a bulk transfer agreement as a significant disadvantage of a bid. In practice this means that bids should be unlikely to succeed unless there is a very good prospect of a bulk transfer agreement being concluded to cover transferring staff. But it is still possible for the business transfer to become dissociated from negotiation of the bulk transfer agreement between the two pension schemes, leaving staff uncertain about the arrangements which will eventually be made.

25. The existing approach will therefore now be strengthened by making it a condition for the business transfer that there will be a bulk transfer agreement under which the pension scheme of the new employer will provide day for day past service credits (or an equivalent recommended by the Government Actuary's Department as a suitable reflection of differences in benefit structures between the schemes) to staff choosing to transfer their accrued credits.

26. It will therefore be essential in future that negotiations between the public service pension scheme and the new employer's pension scheme are settled at a sufficiently early stage in the procurement. The contracting authority should then be able to explain to staff and their representatives what the terms for award of past service

credits will be. Staff representatives will be able to discuss this with the contracting authority and GAD, and they will have a reasonable period in which to make any observations and, if necessary, to make representations directly to the Minister nominated as responsible for the project.

27. Only in exceptional circumstances should staff transfers be contemplated where the contract terms will not ensure appropriate bulk transfer terms. If there are exceptional circumstances justifying a waiver of this contract requirement, these should be explained and discussed with staff representatives at an early stage.

28. As in current practice, staff should normally be given a three month period following the issue to them of pension option forms in which to elect whether to preserve their accrued benefits or transfer them. Pension option forms should be issued as soon as practicable following the staff transfer.

29. Further guidance will be issued to contracting authorities concerning the mechanics of bulk transfer negotiations.

### **Subsequent transfers**

30. Where a public service pension scheme associated with the public contracting authority is not a party to a bulk transfer agreement involving a further transfer of former public servants, the position is substantially more complicated. But appropriate bulk transfer terms should be sought for staff in transfers arising from second-round and subsequent contracting, and sub-contracting. Further guidance will be issued to contracting authorities concerning appropriate contractual safeguards covering availability of bulk transfer terms in subsequent TUPE transfers involving staff who in initial transfers from the Government were the subject of bulk transfer payments by a public service pension scheme.

31. Making these reforms to procurement arrangements will ensure fair treatment of staff pensions in public-private partnerships. It will continue to be important to look at each case on its merits, and to allow contractual mechanisms to continue to evolve towards better practice. The new approaches described above will guide current practice and new developments to ensure that staff are treated consistently on terms which are fair and predictable, and that there is in every case an opportunity for staff to understand fully the implications for their pensions and to make any representations they wish to the responsible Minister *well before* a Government contracting authority makes final arrangements for a business transfer involving the transfer of staff.

32. The Government will be ready to consider any further reforms which may be needed to cope with developments. In addition, for the longer term, it will review with representatives of employers and employees the scope for simplifying the administration of public – private partnerships, for instance by developing ‘model schemes’ or industry-wide multi-employer schemes which are broadly comparable with public service schemes and can facilitate transfers of staff between employers more easily as public - private partnership arrangements become more important to the delivery of public services.